



State of New Jersey

DEPARTMENT OF THE TREASURY
DIVISION OF PENSIONS AND BENEFITS
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ELIZABETH MAHER MUOIO
State Treasurer

JOHN D. MEGARIOTIS
Acting Director

PHILIP D. MURPHY
Governor

SHEILA Y. OLIVER
Lt. Governor

April 5, 2019

Mary Markowsky

[REDACTED]
[REDACTED]

RE: [REDACTED]

Dear Ms. Markowsky:

FINAL ADMINISTRATIVE DETERMINATION

I am writing in reference to the Board of Trustees of the Teachers' Pension and Annuity Fund's (TPAF) denial of your request to waive the amount of accrued interest on the outstanding balance of your pension loan as determined by the Division of Pensions and Benefits (Division). The TPAF Board initially reviewed and denied your request to waive the accrued interest assessed on your outstanding loan obligation at its January 10, 2019 meeting. On February 5, 2019, you appealed the Board's decision. You did not dispute that you took the loan or that you owed interest as originally calculated on the loan. However, you dispute the accrued interest owed on the outstanding loan obligation. On March 7, 2019, the Board considered your appeal and determined that no material facts are in dispute and directed the Board Secretary in conjunction with the Attorney General's Office to prepare Findings of Fact and Conclusions of Law, which were presented and approved by the TPAF Board at its March 7, 2019 meeting.

The TPAF Board has reviewed your correspondence and the relevant documentation and finds that the laws governing the TPAF do not permit the Board to grant your request to waive the accrued interest charged by the Division on the outstanding balance of your loan obligation.

FINDINGS OF FACT

You were enrolled in the Teachers' Pension and Annuity Fund on September 1, 1973 as a result of your employment as a Teacher with Englewood City Board of Education. The record indicates you purchased three (3) years of former membership with the Edgewater Borough Board of Education. According to the records posted to your pension account, the last time you borrowed from your pension account was in the second quarter of 1986. The Division was not able to determine the exact amount you borrowed, but this amount was added to your previous outstanding loan balance to determine the new payment schedule. The payment schedule was for 22 monthly deductions at \$191.17 per month, for a total of \$4,205.75. Interest was calculated at 4.00% per year, based on a decreasing balance each month. The record indicates that the loan deductions began September 1, 1986, and continued through September 30, 1987. No deductions were reported for July and August 1987 since you were a 10-month employee and did not get paid for this period. At the time you separated from employment, the unpaid principal balance of the loan was \$2,057.04 and this balance continued to accrue interest for the period of time you did not participate in the pension plan.

In June 2005, you filed an application for Deferred retirement requesting a January 1, 2006 retirement date. On October 6, 2005, the TPAF Board approved your application for Deferred Retirement effective January 1, 2006. A Quotation of Retirement Benefits, dated November 15, 2005, informed you that the outstanding balance of your loan was \$4,270.59 and that once you retired and began receiving a pension, loan deductions would be taken from your pension check. Although, this did not occur, there is no record you inquired about the status of your loan repayment obligation between 2006 and August 2017.

On September 11, 2017, the Division notified you that a review of your TPAF membership account revealed that you had an existing loan balance in the amount of \$4,270.59 that was not carried into retirement. No loan payments were deducted from your pension checks. In that

letter, you were informed that the Division would begin deducting monthly loan payments in the amount of \$248.69, beginning with your pension check dated October 1, 2017, to satisfy the outstanding obligation including accrued interest. On September 21, 2017 you faxed a letter to the Division disputing the obligation. You indicated that the error on the part of the Division would cause an undue financial hardship and if this loan existed, it should have been deducted while you were employed by the Englewood Public Schools 30 years ago.

On October 5, 2017, Michael Kusmierczyk, Supervising Accountant with the Division responded to your letter regarding your loan obligation. According to federal guidelines, pension loans must be paid within a limited period of time; and therefore, the Division was not able to reduce your monthly payments. Additionally, Mr. Kusmierczyk provided you with copies of screen prints and documents regarding your loan obligation. Lastly, you were provided with appeal rights to the TPAF Board.

On November 5, 2017, you appealed to the TPAF Board noting that due to the Division's error, you are being asked to repay \$248.69 a month instead of the \$191.17 that was set forth in the initial terms of the loan. In addition, you argue that the Board is precluded from seeking reimbursement of the original amount of the loan plus the accrued interest because the statute of limitations on such action has expired.

On January 18, 2018, you were notified that your appeal was being held in abeyance until finalization of discussions with the Internal Revenue Service (IRS).

The TPAF Board notes that after the January 18, 2018 letter to you, the State of New Jersey entered into a Closing Agreement with the IRS that identifies problems with pension loans and a method to correct the identified errors, while maintaining the tax-qualified status of the TPAF.

On September 18, 2018, you were notified that the TPAF Board would consider your appeal at its meeting on January 10, 2019.

On January 10, 2019, the Board considered your submissions and all of the documentation; however, the Board denied your request to waive the accrued interest owed on the outstanding balance of your loan obligation. The basis of the Board's decision was set forth in its letter dated January 18, 2019.

Thereafter, you appealed the Board's determination. You assert that an inordinate amount of interest is added to your loan because of an error by the State. You argue that the error was made by the Division and you should not be penalized additional interest due to the error. In addition, you argue that it is the responsibility of the Division to deduct the loan payment from your pension check and that the Division must take responsibility for the lack of attention to the usual practice. Further, you are requesting that the usual practice of deducting loan payments at the initial pension check be applied to the calculation of the interest to reflect the one and half years during which the principal was paid.

At its meeting on February 7, 2019, the Board determined that there were no material facts in dispute and directed the Board Secretary in conjunction with the Attorney General's Office to prepare Findings of Fact and Conclusions of Law, which constitutes the Board's Final Administrative Determination.

CONCLUSIONS OF LAW

The Board denied your request to waive the accrued interest owed on the outstanding loan balance due your TPAF account or reduce the amount of accrued interest to the original term of the loan (5 years). The Board relied upon N.J.S.A. 18A:66-35 and N.J.S.A. 18A:66-35.1.

N.J.S.A. 18A:66-35 states in pertinent part:

an amount equal to not more than 50% of the amount of his accumulated deductions, but not less than \$50.00; provided, that the amount so borrowed, together with interest thereon, can be repaid by additional deductions from compensation, not in excess of 25% of the member's compensation, made at the same time compensation is paid to the member. The amount so borrowed, together with interest on any unpaid balance thereof, shall be repaid to the retirement system in equal installments by deduction from the compensation of the member at the time the compensation is paid or in such lump sum amount to repay the balance of the loan but such installment shall be at least

equal to the member's rate of contribution to the retirement system and at least sufficient to repay the amount borrowed with interest thereon.

...

Loans shall be made to a member from his accumulated deductions. The interest earned on such loans shall be treated in the same manner as interest earned from investments of the retirement system.

Further, "[t]he rate of interest for a loan requested by a member prior to the effective date of P.L.2007, c.92 (C.43:15C-1 et al.) shall be 4% per annum on any unpaid balance thereof." N.J.S.A. 18A:66-35.

After the enactment of Chapter 92, the State Treasurer sets "a commercially reasonable rate" on January 1 of each calendar year. Ibid. Additionally, N.J.S.A. 18A:66-35.1 states:

In the case of any member who retires without paying the full amount so borrowed, the Division of Pensions and Benefits shall deduct from the retirement benefit payments the same monthly amount which was deducted from the compensation of the member immediately preceding retirement until the balance of the amount borrowed together with the interest is repaid. In the case of a pensioner who dies before the outstanding balance of the loan and interest thereon has been recovered, the remaining balance shall be repaid from the proceeds of any other benefit payable on the account of the pensioner either in the form of monthly payments due to his beneficiaries or in the form of lump sum payments payable for pension or group life insurance.

The TPAF is a "qualified governmental defined benefit plan[] pursuant to sections 401(a) and 414(d) of the federal Internal Revenue Code of 1986, as amended, or such other provision of the federal Internal Revenue Code, as applicable, regulations of the U.S. Treasury Department, and other guidance of the federal Internal Revenue Service." N.J.S.A. 43:3C-18(a). The Director of the Division is "authorized to modify the provisions of the [TPAF], when a modification is required to maintain the qualified status of the [TPAF] under the Internal Revenue Code of 1986, applicable regulations of the U.S. Treasury Department, and other guidance of the federal Internal Revenue Service (IRS)." N.J.S.A. 43:3C-18(c).

IRC Section 401(a) and federal tax law require that pension loans comply with IRC Section 72(p). Specifically, IRC Section 72(p)(2)(B) requires pension loans to be repaid within 5 years of issuance and IRC Section 72(p)(2)(A) prohibits total outstanding loan amounts from exceeding

\$50,000. Ibid. If a member fails to repay the pension loan within the 5-year period or the amount exceeds the IRS limit, then the loan becomes a “deemed distribution” taxable as income to the member and subject to additional penalties. IRC Section 72(p)(1). The deemed distribution does not cancel the loan obligation, which still must be repaid to the Plan, with applicable interest. See Rev. Proc. 2016-51, Section 6.02(1).

There is no dispute that you took a loan from your TPAF account, and that you took the last loan in the second quarter of 1986. There is also no dispute that you began repaying your loan through payroll deductions and that prior to your separation from employment, a total of 22 monthly deductions were taken. There is also no dispute that the repayment ceased when you separated from employment. There is also no dispute that loan deductions did not occur after you began receiving your monthly pension benefit. The TPAF Board acknowledges that your loan payments were not carried into retirement and automatically deducted from your pension checks by the Division. When the Division realized your loan was not being repaid, you were informed by the Division of the outstanding loan obligation, and thereafter the Division implemented a modified repayment schedule to repay your loan.

The TPAF Board is also aware that the issue of the repayment of loans in retirement implicates more than just your loan. Because the TPAF is a federally tax-qualified plan, as required by N.J.S.A. 43:3C-18(a), the TPAF’s failure to comply with all the requirements of the IRC could result in the IRS determining that the TPAF would no longer be a tax-qualified plan under IRC Sections 401(a) and 414(d). To that end, the Board is aware that the State Treasurer and Director of the Division, in accordance with her authority and responsibility under N.J.S.A. 43:3C-18(c) to keep the TPAF tax-qualified, signed a Closing Agreement with the IRS. In addition to setting forth methods to repay certain loans, the Closing Agreement reiterates that the plan is subject to IRC Section 72(p). Even when a loan is not properly repaid under the provisions of IRC Section 72(p),

and there is a reported deemed distribution, the deemed distribution would not relieve a member of the obligation to repay the loan, with interest.

You assert that you should only be required to repay the principal and interest as originally calculated when you took the loan in 1986. Additionally, you contend that the interest that accrued is not a result of your error. While the Board acknowledges that the Division did not withhold loan repayments from your pension check, you took the loan and never made an inquiry of the Division about its status. Per N.J.S.A. 18A:66-35 and 35.1, interest accrues on any unpaid loan balance. Because loan payments were not made or taken from your pension checks, the balance of your loan did not decrease as contemplated by the original loan term. Therefore, per the statutory requirements that govern the loan, N.J.S.A. 18A:66-35 and -35.1, there is additional interest that accrued on your loan that must be repaid.

The TPAF Board also relies on its ability to correct errors pursuant to N.J.S.A. 18A:66-63, which states, in pertinent part:

If any change or error in records results in a member or beneficiary receiving from the retirement system more or less than he would have been entitled to receive had the records been correct, then on discovery of the error, the board of trustees shall correct it and, so far as practicable, adjust the payments in such a manner that the actuarial equivalent of the benefit to which he was correctly entitled shall be paid

While the Board noted your original arguments, and those in your appeal letter, the Board has no authority to grant your request to waive the amount of accrued interest charged on your loan because doing so could harm the overall pension scheme. See Sellers v. Bd. of Trs., Police & Firemen's Ret. Sys., 399 N.J. Super. 51, 62 (App. Div. 2008). Reducing interest on the outstanding loan balance would violate N.J.S.A. 18A:66-35, N.J.S.A. 18A:66-35.1, IRC Section 72(p), and the State's Closing Agreement with the IRS, which could result in the TPAF no longer being considered a tax-qualified plan, which would affect the entire State, all employers in the TPAF, and every member and retiree.

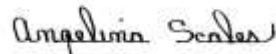
The Board notes that the statute of limitations you cited in your appeal letter, N.J.S.A. 2A:14-1, does not apply to this matter as it is not the filing of civil litigation, and, as noted above, the Board has the authority to correct errors pursuant to N.J.S.A. 18A:66-63.

The TPAF Board has considered your written submissions and because this matter does not entail any disputed questions of fact, the TPAF Board was able to reach its findings of fact and conclusions of law in this matter on the basis of the retirement system's enabling statutes and without the need for an administrative hearing. Accordingly, this correspondence shall constitute the Final Administrative Determination of the Board of Trustees of the Teachers' Pension and Annuity Fund.

You have the right, if you wish to appeal this final administrative action to the Superior Court of New Jersey, Appellate Division, within 45 days of the date of this letter in accordance with the Rules Governing the Courts of the State of New Jersey. All appeals should be directed to:

Superior Court of New Jersey
Appellate Division
Attn: Court Clerk
PO Box 006
Trenton, NJ 08625
Phone: (609) 292-4822

Sincerely,



Angelina Scales, Secretary
Board of Trustees
Teachers' Pension and Annuity Fund

G-6

c: DAG Amy Chung (ET)
DAG Robert Garrison (ET)
C. Chianese/M. Kusmierczyk/D. Dinkler (ET)