ALBEMARLE COUNTY ATTORNEY'S OFFICE

MEMORANDUM

TO: Albemarle County School Board

FROM: Chris Brown, Senior Assistant County Attorney

DATE: February 17, 2012

RE: Pension Plan for Permanent Part-Time Employees

In 1985 the Board of Supervisors adopted a Pension Plan for Permanent Part-Time Employees (the Plan) to provide a retirement benefit for Albemarle County's part-time employees. A brief description of the Plan is found on page 2 of Albemarle County Policy P-63. Permanent part time employees of the School Board also participate in the Plan. As of January 1, 2012, nine local government employees and 253 school division employees participated in the Plan. The contributions to the Plan for January, 2012 totaled $27,200. The Plan needs to be updated in order to comply with applicable tax law and IRS regulations and to make a couple of recommended substantive changes. The Human Resources Department has retained legal counsel specializing in local government benefits to assist in updating the Plan Document and securing the Plan's approval by the IRS. Human Resources also has secured a new plan administrator to maintain the Plan in the future.

Under the terms of the Plan, the County or, in the case of School employees, the School Division, deposits a contribution each payroll reflecting a percentage of pay of each eligible part-time employee. The percentage for each employee is based on the employee's years of service with the Division. Part-time employees become eligible for contributions into the Plan once they have completed five years of continuing service. The percentage of pay starts at 5% and increases 2% every 5 years, capping at 11% for employees with 20 or more years of service. The amount deposited into the employee's account is considered taxable income, and the applicable tax is withheld from the employee's income. The deposits are included in the employee's taxable income for W-2 reporting purposes for the year of the deposit. Investment earnings on the Plan accounts are not reported as taxable income for the year of accrual in the employee's account. When an employee terminates employment with the Division, the account balance is distributable at the request of the employee, with investment earnings reported as taxable income to the employee.

The Plan is intended to be a "tax qualified' retirement plan, meaning that the investment earnings on the accounts would not be taxable to the participants until distributed from the Plan.

Retirement plans intended to be tax qualified are required to be amended from time to time to reflect changes in federal tax laws and IRS regulations. Failure to timely amend the Plan would result in it being viewed by the IRS as "disqualified", resulting in the immediate taxation of accrued investment earnings in participants' accounts and possible sanctions in the form of penalties against the County as the Plan Sponsor and possibly the School Board as a participating employer.

Staff has worked with outside counsel and a new administrator to update the Plan to reflect all necessary technical changes. Our outside counsel recommends that we submit the amended plan to the IRS in order to receive a determination letter from the IRS stating that the Plan is tax qualified

In addition to the technical amendments necessary to bring the Plan into compliance with federal tax law and IRS regulations, staff recommends two substantive changes to the Plan:

1. Any participating employee who terminates employment for any reason but is reemployed must complete an additional 5 years of continuous employment in order to again become qualified for participation in the Plan.

2 Contributions to an employee's account would become taxable upon distribution to the employee instead of in the year contributed. This will bring the Plan more into line with traditional tax deferred plans, will give the School Division more investment options, allow the employee to rollover distributions to other tax deferred investment options and lower administrative costs for the Division.

Albemarle County will remain the Plan's sponsor, but the School Board must approve the amended Plan as a participating employer.

The filing fee for the IRS review is $5,000. The user fee for obtaining a determination letter from the IRS that the updated Plan Document qualifies in form as "tax qualified" is $2,500. Most of the attorney's fees for this project have already been paid by the Human Resources Department. The filing fees and any additional attorney's fees will likewise be paid thru the Human Resources Department, resulting effectively in a split of the fees between the County and School Division. Our proposed Third Party Administrator advises that the new plan should lower administrative costs in a yet to be determined amount.

Staff recommends that the School Board approve the amended Plan and the submission of the amended Plan Document to the IRS for review in order to receive a determination letter that the Plan is tax qualified.