

A RESOLUTION APPROVING THE ORDINANCE AMENDING SECTION 65 OF THE WASHTENAW COUNTY EMPLOYEES' RETIREMENT SYSTEM TO COMPLY WITH THE INTERNAL REVENUE CODE AND RELATED AUTHORITY TO MAINTAIN THE QUALIFIED STATUS OF THE DEFINED BENEFIT PLAN

WASHTENAW COUNTY BOARD OF COMMISSIONERS

January 16, 2002

WHEREAS, the Washtenaw County Board of Commissioners has previously approved the Washtenaw County Employees' Retirement System; and

WHEREAS, it is necessary to revise and amend these plans to conform with changes in the Internal Revenue Code; and

WHEREAS, the Board of Trustees of the Washtenaw County Employees' Retirement System has retained Legal Counsel to review and prepare necessary amendments to the plan in order to maintain the qualified status of the plan; and

WHEREAS, the Washtenaw County Employees' Retirement System has unanimously recommended the approval of these plan amendments; and

WHEREAS, the Corporation Counsel has reviewed the plan amendments and has recommended their approval; and

WHEREAS, these requests have been considered by the Board of Commissioners

NOW THEREFORE BE IT RESOLVED that the Washtenaw County Board of Commissioners hereby approves the ordinance amending Section 65 of the Washtenaw County Employees' Retirement System to comply with the Internal Revenue Code and related authority to maintain the qualified status of the defined benefit plan, a copy of which is attached hereto and made a part of.

BE IT FURTHER RESOLVED that the Washtenaw County Board of Commissioners authorizes Michael J. VanOverbeke, Legal Counsel to the Washtenaw County Employees' Retirement System, to take the necessary action to gain approval of the amended plans from the Internal Revenue Service.

**VANOVERBEKE
MICHAUD &
TIMMONY, P.C.**

ATTORNEYS AND COUNSELORS

MICHAEL J. VANOVERBEKE
THOMAS C. MICHAUD
JACK TIMMONY
LESLIE K. HOLMBERG
MICHAEL E. MOCO

79 ALFRED STREET
DETROIT, MI 48201
TEL: 313-578-1200
FAX: 313-578-1201
MPERSLAW@AOL.COM

M E M O R A N D U M

**TO: BOARD OF TRUSTEES OF THE WASHTENAW COUNTY
EMPLOYEES RETIREMENT SYSTEM**

FROM: VANOVERBEKE, MICHAUD & TIMMONY, P.C.

RE: QUALIFIED PLAN COMPLIANCE WITH INTERNAL REVENUE CODE

DATE: NOVEMBER 20, 2001

The Board of Trustees is vested with the fiduciary responsibility for the administration, management and operation of the Retirement System and has the authority to make rules and regulations necessary for the proper conduct of the pension trust fund. The Retirement System is intended to be and has been administered as a qualified governmental pension plan under Section 401 of the Internal Revenue Code, as amended ("IRC" or "Code") and is a tax-exempt organization under IRC § 501.

This "qualified plan" status provides the Retirement System with certain tax advantages, primarily (1) the member does not pay tax on employer contributions to the plan or the earnings and income generated by employer and member contributions until the member receives a distribution from the plan; and (2) certain favorable tax treatment may be available when benefits are actually distributed to members (e.g., rollover). In order to take advantage of these benefits, the Retirement System must satisfy numerous and complex IRC requirements.

Over the years, the qualified plan requirements have been amended by law and regulations. Such amendments include the Tax Reform Act of 1986 (TRA '86); the Technical and Miscellaneous Revenue Act of 1988 (TAMRA); the Unemployment Compensation Amendments of 1992 (UCA); the Omnibus Budget Reconciliation Acts (OBRA); the Uniformed Service Employment and Reemployment Rights Act of 1994 (USERRA); the Uruguay Round Agreements Act of 1994 (GATT); the Small Business Job Protection Act of 1996 (SBJPA '96); the Taxpayer Relief Act of 1997 (TRA '97); the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA '98); the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), and related laws, regulations and administrative authority.

While the Retirement System has operated in accordance with the IRC, the plan document should reflect the changes to the Code. Historically the IRS has extended the deadline for the plan amendments (“remedial amendment period”) with the thought of amending, limiting or eliminating certain requirements for governmental plans. The remedial amendment period for governmental plans was the last day of the first plan year beginning on or after January 1, 2001 (i.e., for calendar year plans - December 31, 2001; for July 1 fiscal year plans - June 30, 2002). However, pursuant to Revenue Procedure 2001-55, the December 31, 2001 has been extended to February 28, 2001. Please note that it is only required that the changes be incorporated into the plan document within the remedial amendment period. The Retirement System is not required to receive a determination letter from the IRS to maintain its qualified status.

The following is presented to provide an overview of the qualification rules applicable to governmental retirement plans under the Internal Revenue Code.

WHAT CONSTITUTES A “PENSION PLAN”?

IRC § 401(a)

- **Held in Trust.** To qualify for the favorable tax treatment, the plan must be governed by a **written** document that requires all contributions to be held in **trust** for the sole purpose of distributing benefits to members and their beneficiaries (IRC § 401(f) permits a custodial account or an annuity account to be used as a funding vehicle in lieu of a trust so long as the requirements of IRC § 401 are otherwise satisfied).

- **Determinable Benefits.** A plan that is established and maintained by an employer to provide systematically for the payment of **definitely determinable benefits** to employees over a period of years after retirement.

- Requires that benefits for each participant can be computed in accordance with an **express formula contained in the plan.** Rev. Rul. 74-385, 1974-2 C.B. 130; Treas. Reg. § 1.401-1(b)(1)(i).

- Requires that whenever the amount of any benefit is to be determined on the basis of actuarial assumptions, such **actuarial assumptions are specified in the plan.** IRC § 401(a)(25); Rev. Rul. 79-90, 1979-1 C.B. 155.

NOTE: Both requirements ensure that there is always a known formula whereby the member's benefits may be calculated at any given time, free from any discretion by the employer or plan administrator.

- **Exclusive Benefit.** IRC § 401(a)(2) requires that the plan be "for the exclusive benefit of the employees or their beneficiaries . . ." Therefore:

- Plan may not benefit a person other than the employee or their beneficiaries. *Rev. Rul. 72-240, 1972-1 C.B. 108.*

- Investments made on behalf of the employees must be for the exclusive benefit of employees and their beneficiaries.

□ No funds may revert back to the employer until the trust is terminated and all liabilities are paid [IRC § 401(a)(2)]. Note that if the surplus is a result of a change in the benefit provisions or in the eligibility requirements of the plan, the surplus may not be transferred back to the employer. Treas. Reg. § 1.401-2(b)(1).

WHAT IS A GOVERNMENTAL PENSION PLAN?

A governmental plan is a plan which is “established and maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing.” IRC § 414(d) Recognition as a governmental plan under IRC § 414(d) exempts the plan from certain IRC requirements and ERISA.

WHAT IS A DEFINED CONTRIBUTION PLAN ?

For purposes of the Internal Revenue Code, a defined contribution plan is defined as **“a plan which provides for an individual account for each participant and for benefits based solely on the amount contributed to the participant’s account, and any income, expenses, gains and losses, and any forfeitures of accounts of other participants which may be allocated to such participant’s account.”**[IRC § 414(i)].

Defined contribution plans require the employer to provide plan **contributions** that **are either discretionary in amount or based on a specified formula**. In contrast to a defined benefit plan, no specific benefits are promised to a participant under a DC plan. The amount of benefits received under a defined contribution plan is determined by the amount of contributions, earnings and forfeitures that are allocated to the participant’s account under the plan. In the event the participant terminates employment before becoming fully vested in the plan, the participant is entitled to a benefit equal to the vested account balance. The nonvested portion is forfeited and may be applied in several ways, including to increase the accounts of remaining participants.

WHAT IS A DEFINED BENEFIT PLAN ?

The Code defines a defined benefit plan as **“any plan other than a defined contribution plan.”** [IRC § 414(j)]. Generally, **defined benefit plans** require the employer to **provide benefits** to plan participants **according to a pre-determined formula** established in the plan. The benefit formula provides for the payment of definitely determinable benefits to participants over a period of years. The amount of employer contributions to the plan depends on actuarial calculations of the amounts necessary to fund the benefits promised under the plan. As with defined contribution plans, a participant in a defined benefit plan is entitled to a benefit equal to the vested amount of his or her employee contributions, provided the particular defined benefit plan provides for such employee contributions. However, forfeitures arising under a defined benefit plan may not be allocated to other participants.

WHO MUST THE PLAN COVER?

The Taxpayer Relief Act of 1997 (“TRA '97”) exempted governmental plans from the required minimum participation standards and coverage requirement tests of IRC § 401(a)(3) and the non-discrimination rules of IRC § 401(a)(4) which previously prohibited contributions, benefits,

optional forms of benefits and other plan features from discriminating in favor of highly compensated employees.

Governmental plans are treated as satisfying Code § § 401(a)(3) [minimum participation rules of IRC 410(b)], 401(a)(4) [general nondiscrimination rules], 401(a)(26) [minimum participation rule], 401(k) [salary reduction nondiscrimination rules], 401(m) [matching employer contribution nondiscrimination rules], 403(b)(1)(D) and 403(b)(12) [403(b) nondiscrimination rules], and 410 [minimum participation rules] for all taxable years beginning before enactment of TRA '97.

WHEN MUST PENSION BENEFITS “VEST”?

“VESTING” commonly refers to the period of time after which a participant is entitled to a benefit (i.e., accrued benefits become nonforfeitable). The vesting requirements are established in the Plan. However, government plans must at a minimum satisfy the vesting requirements “resulting from the application of Sections 401(a)(4) and 401(a)(7) as in effect on September 1, 1974.” IRC § 411(e). This requires that a governmental plan provide for:

- 100% vesting of accrued benefits when a member reaches the plan’s normal retirement age. *Rev. Rul. 66-11, 1966-1 C.B. 71.*
- 100% vesting if there is a partial or complete termination of the plan, or complete discontinuation of contributions, but in either situation, vesting is required only to the extent the benefits are funded. IRC § 401(a)(7) (1974).

ARE THERE LIMITATIONS ON COMPENSATION FOR PENSION PURPOSES?

IRC § 401(a)(17) limits the maximum amount of annual compensation that may be taken into account for a participant in a qualified retirement plan.

For the year 2002, this limit is \$200,000. The prohibition on taking more than \$ 200,000 into account means that:

- Compensation in excess of \$200,000 may not be used when computing a pension benefit.
- Employee contributions may not be computed on more than \$200,000.

The limit may be adjusted for inflation, based in part on the adjustment made under IRC § 415(d). Treas. Reg. § 1.401(a)(17)-1(a)(3)(ii). Annual adjustments to the revised limit under IRC § 401(a)(17) are made in increments of \$5,000. Treas. Reg. § 1.401(a)(17)-1(a)(3)(iii).

ARE THERE LIMITATIONS ON CONTRIBUTIONS OR BENEFITS?

IRC § 401(a)(16) requires a qualified plan to abide by IRC § 415, which imposes annual limits on the amount of contributions and benefits.

IRC § 415 limits must be met by all plan members. If even one member accrues an annual benefit greater than IRC § 415 allows, or contributes more than IRC § 415 allows, the penalty provided is that the entire plan will be disqualified.

Definition of Compensation.

"Compensation" for IRC § 415 purposes includes the compensation actually paid to the employee during the limitation year. Treas. Reg. § § 1.415-2(d) and 1.415-3(a)(3). Treas. Reg. § 1.415-2(d)(2)(i) contains the basic definition of compensation for IRC § 415 purposes:

The employee's wages, salaries, fees for professional services, and other amounts received (without regard to whether or not an amount is paid in cash) for personal services actually rendered in the course of employment with the employer maintaining the plan to the extent that the amounts are includible in gross income (including, but not limited to, commissions paid salesmen, compensation for services on the basis of a percentage of profits, commissions on insurance premiums, tips, bonuses, fringe benefits, and reimbursements or other expense allowances under a nonaccountable plan (as described in § 1.62-2(c)).

Effective for years beginning after December 31, 1997, § 1434(a) of the SBJPA amended the definition of compensation for purposes of applying the IRC § 415 percentage of compensation limits on contributions to, and benefits from, qualified plans to include:

- (i) any elective deferral (as defined in § 402(g)(3)), and
- (ii) any amount which is contributed or deferred by the employer at the election of the employee and which is not includible in the gross income of the employee by reason of § 125 or 457 (i.e., 457 Plan contributions).

Please note that there is no requirement that the definition of compensation used for IRC § 415 purposes be the same definition as is used for benefit or contribution calculations, so long as both definitions independently satisfy IRC § 414(s), and the eventual benefit satisfies IRC § 415.

Limits for Defined Benefit Plans.

One of the requirements for a defined benefit plan to remain qualified is that the total amount of annual pension benefits provided to each member cannot exceed the amount specified in IRC § 415(b). The "Dollar Limit" in the year 2002 is \$160,000.

The SBJPA repealed the 100% salary limitation for governmental plans.

Adjustments to the Dollar Limit.

Certain adjustments must be made to the Dollar Limit.

1. The Dollar Limit is indexed for inflation. (Adjusted in increments of \$5,000).
2. The Dollar Limit is raised if an individual retires later than age 65, and lowered if an individual retires before age 62 or retires with fewer than ten years of participation in the plan. Code § § 415(b)(2)(D); 415(b)(5). The reductions for fewer than ten years of service or

participation (as applicable) are made on a pro rata basis (i.e., reductions for fewer than ten years of service are reduced in proportion to ten years) See also Treas. Reg. § 1.415-3(g)(1). These rules do not apply to (a) income received as a pension, annuity, or similar allowance as a result of personal injuries or sickness, or (b) amounts received as a result of an employee's death by the employee's beneficiaries, survivors, or estate. § 1444(c) of the SBJPA.

4. **Special Limits for Governmental Plans.** Certain adjustments were made to the Dollar Limit for governmental pension plans, so in cases of early retirement, members of governmental plans were subject to a Dollar Limit that was more generous than for members of private plans. However, as part of EGTRRA, the special adjustment rules contained in IRC § 415(b)(2)(F) have been deleted. Therefore, the Dollar Limit may now be reduced below \$75,000 if the employee retires at or after age 55. Notwithstanding, the rules provided for in TRA '97 which allow early retirement for police and fire personnel without a reduction in the Dollar Limit still apply (i.e., IRC § 415(b)(2)(G) provides that **reductions for early retirement** under IRC § 415(b)(2)(C) **do not apply to police and fire personnel** (including emergency medical services) who retire before the Social Security retirement age, **so long as at least 15 years of service is required to receive a full benefit under the plan**).

Defined Contribution Limits.

Prior to EGTRRA, if a member participated in a defined contribution plan, the annual amount that may be added to the member's account was limited to the lesser of \$35,000 or 25% of the member's compensation for the year. IRC § 415(c). The \$35,000 limit for year 2001 was indexed for inflation in increments of \$5,000. Effective for plan years beginning after December 31, 2001, the IRC § 415(c) limitation on contributions to defined contribution plans will be increased to the lesser of \$40,000 or 100% of Compensation. The \$40,000 dollar limit will be subject to more rapid indexing with annual cost of living adjustments in \$1,000 increments, instead of the current \$5,000 increments.

“Compensation” to which the 100% limit is applied includes wages received, as well as any amount which are contributed or deferred by the employer at the election of the employee and which is not includible in the gross income of the employee by reason of IRC § 457.

This test is applied on an annual basis.

"Annual Addition" is defined by Treas. Reg. § 1.415-6(b)(1) as the sum, credited to a participant's account for any limitation year, of:

1. Employer contributions;
2. Employee contributions; and
3. Forfeitures.

Nondeductible employee contributions (both mandatory and voluntary) to a defined benefit plan are treated as a separate defined contribution plan of the employer and must be taken into consideration in computing the annual additions defined contributions plans of the employer. Rev. Rul. 78-57; 1978-CB 128.

"Annual Additions" do not include:

1. The restoration of an employee's accrued benefit by the employer in accordance with § 411(a)(3)(D) or § 411(a)(7)(C) will not be considered an annual addition for the limitation year in which the restoration occurs. (See § 1.411(a)-7(d)(6)(iii)(B).)
2. The transfer of funds from one qualified plan to another will not be considered an annual addition for the limitation year in which the transfer occurs.
3. Rollover contributions.
4. Repayments of loans made to a participant from the plan,
5. Repayments of amounts described in § 411(a)(7)(B) (in accordance with § 411(a)(7)(C)) and § 411(a)(3)(D) (see § 1.411(a)-7(d)(6)(iii)(B)), and
6. The direct transfer of employee contributions from one qualified plan to another.
7. Employee contributions "picked-up" pursuant to IRC § 414(h)(2) are not considered employee contributions to a separate defined contribution plan. IRS Letter § 1 Q&A-8. However, the current IRS position is that the resulting benefit must be tested under IRC § 415(b).

Note that there is no longer a combined test of both defined benefit and defined contribution amounts pursuant to IRC § 415(e).

WHEN IS A PLAN REQUIRED TO MAKE DISTRIBUTIONS?

IRC § 401 (a)(9) includes several rules governing distributions from “qualified” plans.

- Distributions must begin to be paid by the later of April 1 of the calendar year after member attains age 70 ½ or April 1 of the calendar year after the member actually retires.
- Proposed Regulations under § 401(a)(9) were published in 2001-11 I.R.B. 865 on March 12, 2001 (the 2001 Proposed Regulations) which significantly simplified the rules for required minimum distributions.
- The 2001 Proposed Regulations provide a simple, uniform table that most employees can use to determine minimum distributions during their life. If an employee's sole beneficiary is the employee's spouse and the spouse is more than 10 years younger than the employee, the employee can use the longer distribution period of the joint life and last survivor life expectancy of the employee and spouse.
- When the employee dies after the required beginning date with a designated beneficiary, the distribution period is the beneficiary's life expectancy for the year after death reduced by one for each subsequent year. When an employee dies after the required beginning date without a designated beneficiary, the distribution period is the employee's life expectancy for the year of death reduced by one for each subsequent year.
- The Proposed Regulations change the default rule in the case of death before the employee's required beginning date from the five-year rule to the life expectancy of the designated beneficiary.
- The 2001 Proposed Regulations would be effective for distributions for calendar years beginning on or after January 1, 2002. But effective immediately, taxpayers may rely on the 2001 Proposed Regulations for determining minimum required distributions for calendar year 2001, or they may rely on the regulations under § 401(a)(9) that were proposed in 1987 (the 1987 Proposed Regulations) for determining minimum required distributions for calendar year 2001.
- In addition to meeting the minimum distribution requirements, all distributions to beneficiaries or survivors must meet the incidental benefit requirements.

- The general incidental death benefit tests for pre-retirement death benefits require that the cost of providing such a death benefit cannot exceed 25% of the cost of all of the member's benefits or that the death benefit not exceed 100 times the expected monthly amount that would have been paid to the member. This rule applies only to benefits paid from "qualified" trusts. Distributions from federally or state funded line of duty death benefit programs can be set up separately to avoid a problem in this regard.
 - The plan must be operated in a manner that complies with each of the rules under IRC §401(a)(9) and the plan document must specifically include a statement that distributions will be made in accordance with these rules and that any contradictory provisions in the plan are expressly overridden.
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WHAT IS A ROLLOVER?

IRC § 401(a)(31) requires a plan to permit its members to elect to have an otherwise taxable distribution paid directly to an eligible retirement plan.

Eligible Rollover Distributions.

IRC § 402(c) provides that any "eligible rollover distribution" from a qualified trust described in IRC § 401(a) may be rolled over to an "eligible retirement plan" within 60 days.

The amount of any distribution that is actually rolled over to an eligible retirement plan is not included in the recipient's taxable income. IRC § 402(c)(1).

An "**eligible rollover distribution**" means any distribution to an employee or surviving spouse of an employee of all or any portion of the balance to the credit of the employee in a qualified plan, **except for the following:**

- Any distribution that is one of a series of substantially equal periodic payments made (not less frequently than annually) over any one of the following periods: the life of the employee (or the joint lives of the employee and the employee's designated beneficiary), the life expectancy of the employee (or the joint life and last survivor expectancy of the employee and the employee's designated beneficiary), or a specified period of ten years or more;
- Any distribution to the extent the distribution is required by the minimum distribution requirements of IRC § 401(a)(9);
- The portion of any distribution that is not includible in gross income (i.e., the employee's post tax investment in contract (basis)); and
- Additional items designated by the Commissioner in revenue rulings, notices, and other guidance of general applicability. Those that already have been designated include dividends on employer securities, plan loans, taxable cost of life insurance coverage, and corrective distributions for 401(k) plans.

Eligible Retirement Plan.

IRC § 402(c) allow a member and a member's surviving spouse to execute a rollover to an "eligible retirement plan."

Regular Rollovers

A **regular rollover** occurs when a recipient of an eligible rollover distribution elects to personally receive the distribution (rather than have the distribution paid directly to an eligible retirement plan) and subsequently transfers all or part of the distributed amount to an eligible retirement plan within 60 days after receiving the distribution.

Under the regular rollover rules, an **eligible retirement plan** includes an individual retirement plan or a qualified plan. IRC § 402(c)(8)(B); Treas. Reg. § 1.402(c)-2 Q&A-2. With the adoption of EGTRRA, an eligible retirement plan includes an individual retirement account ("IRA") described in IRC § 408(a), an individual retirement annuity described in IRC § 408(b), an annuity plan or contract described in IRC § 403(a) and (b), an eligible plan under IRC § 457 which is maintained by a state, political subdivision of a state and which agrees to separately account for amounts transferred into such plan, or a qualified trust described in IRC § 401(a), that accepts the distributee's eligible rollover distribution. The definition of eligible retirement plan shall also apply in the case of a distribution to a surviving spouse or to a spouse or former spouse who is the alternate payee under a domestic relations order.

For purposes of the direct rollover provision, a portion of a distribution shall not fail to be an eligible rollover distribution merely because the portion consists of after-tax employee contributions which are not includible in gross income. However, such portion may be paid only to an individual retirement account or annuity described in IRC § 408(a) or (b), or to a qualified plan described in IRC § 401(a) or 403(b) that agrees to separately account for amounts so transferred, including separately accounting for the portion of such distribution which is includible in gross income and the portion of such distribution which is not so includible.

Direct Rollovers.

A direct rollover occurs whenever a participant or the participant's spouse elects to have an eligible rollover distribution paid directly to an eligible retirement plan. Direct rollovers may now be made to a defined contribution plan, an individual retirement account or annuity (IRC § 401(a)(31)(D)), to a defined benefit plan Treas. Reg. § 1.401(a)(31)-1 Q&A-2 or to a governmental 457 Plan.

A defined benefit plan is not required to accept rollovers.

ARE THERE IRC PROVISIONS WHICH GOVERNMENTAL PLANS ARE EXEMPT?

Code § 401(a)(3)

- Requires minimum participation standards and coverage requirement tests to be met.

Code § 401(a)(4)

- Prohibits contributions, benefits, optional forms of benefits and other plan features from discriminating in favor of highly compensated employees.

Code § 401(a)(10) & 416

- Top-Heavy Provisions

Code § 401(a)(11) & 417

- Joint and Survivor Annuities. Requires qualified joint and survivor annuity benefits to be payable at retirement and preretirement survivor annuity benefits to become payable upon death prior to retirement.

Code § 401(a)(12) & 414(l)

- Requires accrued benefits to be preserved when there is a plan merger, consolidation or transfer of assets.

Code § 401(a)(13)

- Prohibits assignment or alienation of benefits.

Code § 401(a)(14)

- Requires commencement of benefits to be no later than 60 days after the close of the plan year in which normal retirement (or age 65, if earlier), 10th anniversary of participation or termination occurs, whichever occurs later.

Code § 401(a)(15)

- Prohibits the reduction of retiree benefits due to increases in Social Security benefits after retirement.

Code § 401(a)(19)

- Prohibits accrued benefits derived from employer contributions to be forfeited as a result of withdrawal of employee contribution when such employee is at least 50% vested.

Code § 401(a)(20)

- Allows qualified total distributions to be made with appropriate notice to PBGC when a plan is terminating.

Code § 401(a)(26)

- Code § 401(a)(26) generally requires that for each day of the plan year, the plan must benefit the lesser of 50 employees or 40% or more of all of the employer's employees.

- This requirement is deemed satisfied by governmental plans for plan years beginning before the later of January 1, 1999, or 90 days after the opening of the first legislative session beginning on or after January 1, 1999, of the governing body with authority to amend the plan, if that body does not meet continuously.

Code § 401(m)

- Code § 401(m) includes special nondiscrimination tests that apply to employer matching contributions to defined contribution plans. This would generally not apply for public safety plans.

Code § 403(b)(12)(A)(i)

- Code § 403(b)(12)(A)(i) set forth nondiscrimination requirements for those plans which received contributions not made pursuant to a salary reduction agreement.

Code § 410

- Requires governmental plans to meet pre-ERISA requirements of § 401(a)(3).

Code § 411

- Requires minimum vesting requirements to be met which stipulate that a plan may not discriminate in favor of officers, shareholders, supervisors, or highly compensated employees (401(a)(4)), and 100% vesting upon plan or discontinuance of employer contributions (401(a)(7)).

Code § 412

- Requires plans to be 100% vested upon the plan's termination or discontinuance of employer contributions.

Code § 4980A

- Code § 4980A imposes a 15% excise tax to the extent the aggregate amount of distributions paid to an individual from qualified retirement plans, tax sheltered annuities, and individual retirement accounts exceeds the greater of: (1) \$150,000 or (2) \$112,500 as indexed for inflation, which for 1994 is \$148,500.

- Death benefits, payments pursuant to qualified domestic relations orders, and rollovers are not taken into account for purposes of the excess distribution tax.

It is recommended that the Board incorporate the necessary IRC provisions by the adoption of the attached resolution prior to the expiration of the remedial amendment period.

As always, if you have any questions, please do not hesitate to contact this office. Thank you.

AN ORDINANCE AMENDING SECTION 65 OF THE WASHTENAW COUNTY EMPLOYEES RETIREMENT SYSTEM TO COMPLY WITH THE INTERNAL REVENUE CODE AND RELATED AUTHORITY TO MAINTAIN THE QUALIFIED STATUS OF THE DEFINED BENEFIT PLAN.

Be it ordained by the Board of Commissioners of the County of Washtenaw that Section 65 of the Washtenaw County Employees Retirement System is hereby amended to read as follows:

Internal Revenue Code Qualifications.

Section 65. ~~(a) The County intends the Retirement System to be a qualified pension plan under Section 401 of the Internal Revenue Code, as amended, or successor provisions of law, and that the trust be an exempt organization under Section 501 of the Internal Revenue Code. The Retirement Commission shall recommend for adoption by the County board of Commissioners such additional provisions to the Retirement System as are necessary to fulfill this intent.~~

(a) The Retirement System is intended and has been administered to be a qualified pension plan under § 401 of the Internal Revenue Code, as amended (“IRC” or “Code”), or successor provisions of law, including the Tax Reform Act of 1986 (TRA ‘86); the Technical and Miscellaneous Revenue Act of 1988 (TAMRA); the Unemployment Compensation Amendments of 1992 (UCA); the Omnibus Budget Reconciliation Acts (OBRA); the Uniformed Service Employment and Reemployment Rights Act of 1994 (USERRA); the Uruguay Round Agreements Act of 1994 (GATT); the Small Business Job Protection Act of 1996 (SBJPA ‘96); the Taxpayer Relief Act of 1997 (TRA ‘97); the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA ‘98); the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), and other applicable laws, regulations and administrative authority. The Retirement System is a governmental plan under IRC § 414(d) and is administered for the exclusive benefit of the plan’s participants and their beneficiaries. The Retirement System trust is an exempt organization under IRC § 501.

(b) Prohibition Against Reversion. The Retirement System and trust have been created for the exclusive benefit of the members and beneficiaries as set forth herein. The funds thereof have been established for the benefit of the members and for the operation of the Retirement System. No part of the principal and income of any of the funds of the system and trust shall revert to or be returned to the County prior to the satisfaction of all liabilities hereunder to all members, beneficiaries and anyone claiming by or through them.

(c) Actuarial Valuation Assumptions. Actuarial Valuation Assumptions may be changed by the Retirement Commission after consulting with the actuary. Actuarial equivalence will be determined on the basis of the interest rate and mortality tables adopted by the Retirement Commission. Actuarial assumptions that will be used to determine the amount or level of any optional benefit forms will be the actuarial equivalent of the normal retirement benefit. Optional benefits provided under the plan shall be actuarial adjusted in relation to the straight life annuity. For purposes determining the IRC § 415 limitations, the interest rate assumption will not be less than the greater of five (5%) percent or the rate specified in the plan for determining actuarial equivalence for the particular form of retirement benefit. The actuarial early retirement reduction and reduction of the Dollar Limit if the Employee has less than ten (10) years of participation under

IRC § 415 do not apply to income received as a pension or annuity as a result of an employee's personal injury, sickness or death and shall be administered in accordance with IRC § 415(b)(2), as amended.

(d) **Termination.** In the event of termination of this plan, a member's interest under the plan as of such date is nonforfeitable on the attainment of his/her normal retirement age, as defined in IRC § 411(d)(3), to the extent funded in conformity with applicable sections of the Internal Revenue Code and Regulations. Upon a member's termination date, the value of any forfeitable accrued benefit shall be forfeited by the member as of the termination date. The value of such forfeitures shall be used to reduce the employer's future contributions under the Plan in accordance with IRC § 401(a)(8). No forfeitures under the Plan shall be applied to increase the benefits that any member or beneficiary would otherwise receive at any time prior to the time when the Plan may be terminated. If a member whose employment has terminated does not retain a vested benefit under the Plan, he/she shall no longer be a member or retain or earn credited service under the Plan unless and until he/she again becomes an employee.

(e) **Merger, Consolidation or Transfer.** In conformity with Section 414(1) of the Internal Revenue Code, in the case of any transfer of assets or liabilities of this plan to any other plan, each plan participant would (if the plan then terminated) receive a benefit immediately after the transfer that is equal to or greater than the benefit the participant would have been entitled to receive immediately before the transfer (if the plan had then terminated).

(f) **Limitations of Benefits.** The Retirement System shall not pay any benefit that would exceed the benefit limitations for governmental plans as set forth in Section 415 of the Internal Revenue Code and regulations, as amended. For this purpose, compensation shall be determined in accordance with Code section 415(e)(3). In the event it should become necessary to reduce or restrict a benefit in order to comply with section 415(e), the employer-provided portion of the benefit payable under this Retirement System shall be reduced or restricted to the extent necessary.

The amount of annual benefits and contributions credited a member in any given year shall be subject to the following limitations:

(A) **Defined Benefit Plans.** The maximum permissible Annual Pension Benefit with respect to any member shall be in accordance with IRC § 415(b) which provides that such Annual Pension Benefit shall not exceed \$90,000, as adjusted for inflation, which for 2002 is \$160,000 (the "Dollar Limit").

(i) **Special Dollar Limitations.** If the benefit is payable prior to age 62, the dollar limitation shall be reduced to the actuarial equivalent of a benefit commencing at age 62. In the case of any full-time police or fire employee, who is a Qualified Participant as defined in IRC § 415(b)(2)(G), there is no reduction in the dollar limitation. If the benefit is not payable until after age 65, the dollar limitation shall be increased to the actuarial equivalent of a benefit commencing at age 65.

(ii) In the case of an employee who has less than ten (10) years of participation in the Plan, the Dollar Limitation shall be reduced 1/10 for each year of participation in accordance with IRC § 415(b)(5).

(B) **Defined Contribution Plans.**

(1) For limitation years beginning after December 31, 1986 the term "annual addition" means, for purposes of this section, the sum, credited to a participant's account for any limitation year, of:

- (A) Employer contributions;
- (B) Employee contributions; and
- (C) Forfeitures.

(2) Annual additions that may be contributed or allocated to a participant's account for a limitation year will not exceed the lesser of:

- (A) 100% percent of participant's compensation, within the meaning of IRC § 415(c)(3), or
- (B) \$40,000, as adjusted for increases in the cost of living pursuant to IRC § 415(d).

(c) **Excess Benefit Payment.** The Retirement System shall not pay any benefit that would exceed the benefit limitations for governmental plans as set forth in IRC § 415 and regulations, as amended.

(d) **Compensation.** As defined by IRC § 415(c)(3)(D) and Treas. Reg. § 1.415-2(d)(2)(i), compensation means amounts actually paid to the employee during the Limitation Year, including: wages, salary, professional fees, percentage of profits, commissions, tips and bonuses paid or made available to the member during the Limitation Year for personal services actually rendered in the course of employment, any elective deferral, and any amount which is contributed or deferred by the employer at the election of the employee and which is not includible in the gross income of the employee by reason of IRC §§ 125 or 457.

(g) Distributions from the Retirement System will comply with the requirements of Code section 401(a)(9) and the regulations thereunder, including the following specific requirements. With respect to distributions under the Plan made for calendar years beginning on or after January 1, 2001, the Plan will apply the minimum distribution requirements of IRC § 401(a)(9) in accordance with the regulations under IRC § 401(a)(9) that were proposed in January 2001, notwithstanding any provision in the Plan to the contrary. This amendment shall continue in effect until the end of the last calendar year beginning before the effective date of final regulations under section 401(a)(9) or such other date as may be specified in guidance published by the Internal Revenue Service. Pursuant to IRC § 401(a)(9)(A)(ii), distribution of a member's benefits will begin not later than April 1 of the calendar year following the later of the calendar year in which the employee attains age 70-1/2 and the calendar year in which the employee retires.

~~If distribution of a member's benefits commenced prior to the member's death, any remaining benefits will be distributed at least as rapidly as under the method of distribution used as the date of the member's death.~~

~~If distribution of a member's benefits had not commenced prior to the member's death, any portion of his or her benefits payable after the member's death shall:~~

~~(i) if payable to the member's surviving spouse, begin no later than the end of the calendar year following the calendar year in which the member would have attained age 70 1/2; or~~

~~(ii) if payable to the member's designated beneficiary, begin no later than the end of the calendar year following the calendar year in which the member died and extend over a period not extending beyond the life expectancy of the beneficiary; or~~

~~(iii) otherwise, be distributed within 5 years of the member's death.~~

(h) This subsection applies to distributions made on or after January 1, 1993. Notwithstanding any provision of the plan to the contrary that would otherwise limit a distributee's election under this subsection, a distributee may elect, at the time and in the manner prescribed by the Retirement Commission, to have any portion of an eligible rollover distribution paid directly to an eligible retirement plan specified by the distributee as a direct rollover. The following definitions shall apply with regard to this subsection.

(i) **Eligible rollover distribution:** An eligible rollover distribution is any distribution of all or any portion of the balance to the credit of the distributee, except that an eligible rollover distribution does not include: any distribution that is one of series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the distributee or the joint live (or joint life expectancies) of the distributee and the distributee's designated beneficiary, or for a specified period of ten years or more, and any distribution to the extent such distribution is required under section 401(a)(9) of the Code ~~and the portion of any distribution that is not includable in gross income.~~ For purposes of the direct rollover provision, a portion of a distribution shall not fail to be an eligible rollover distribution merely because the portion consists of after-tax employee contributions which are not includible in gross income. However, such portion may be paid only to an individual retirement account or annuity described in IRC § 408(a) or (b), or to a qualified plan described in IRC § 401(a) or 403(b) that agrees to separately account for amounts so transferred, including separately accounting for the portion of such distribution which is includible in gross income and the portion of such distribution which is not so includible.

(ii) **Eligible retirement plan:** An eligible retirement plan is an individual retirement account described in section 408(a) of the Code, an individual retirement annuity described in section 408(a) of the Code, an annuity plan described in section 403(a) of the Code, an annuity contract described in IRC § 403(b), an eligible plan under IRC § 457 which is maintained by a state, political subdivision of a state and which agrees to separately account for amounts transferred into such plan or a qualified trust described in section 401(a) of the Code, that accepts the distributee's eligible rollover distribution. ~~However, in the case of an eligible rollover distribution to the surviving spouse, an eligible retirement plan is an individual retirement account or individual retirement annuity.~~ The definition of eligible retirement plan shall also apply in the case of a distribution to a surviving spouse or to a spouse or former spouse who is the alternate payee under a domestic relations order.

(iii) **Distributee:** A distributee includes an employee or former employee. In addition, the employee's or former employee's surviving spouse is a distributee with regard to the interest of the surviving spouse.

(iv) **Direct Rollover:** A direct rollover is a payment by the Retirement System to the eligible retirement plan specified by the distributee.

(i) **Maximum Annual Earnings.** For Plan years beginning on or after January 1, 1989 and before July 1, 1996, the annual compensation of each Participant taken into account for determining all benefits provided under the Plan for any determination period shall not include any amounts in excess of the annual compensation limit (originally \$200,000) provided for in IRC § 401(a)(17) prior to the Omnibus Budget Reconciliation Act of 1993 ("OBRA '93") and adjusted for inflation in the manner provided by IRC § 401(a)(17). For Plan years beginning on or after July 1, 1996, the annual compensation of each employee taken into account shall not exceed the annual compensation limit provided for in IRC § 401(a)(17), as amended by the Omnibus Budget Reconciliation Act of 1993 ("OBRA '93") (\$200,000 in 2002). This limit may be adjusted as required by federal law for qualified government plans and shall be further adjusted for inflation in the manner provided by IRC § 401(a)(17). Annual compensation means compensation during the plan year or such other consecutive 12 month period over which compensation is otherwise determined under the plan.

(j) **Military Service.** Notwithstanding any provision of the Plan to the contrary, contributions, benefits and service credit with respect to qualified military service will be provided in accordance with IRC § 414(u) and Regulations.

(k) **Vesting.** Pursuant to IRC § 411(e) as in effect in 1974, a member shall be 100% vested in his/her accrued benefit when he or she attains Normal Retirement Age.

(l) **Plan Year.** The plan year shall be the 12 consecutive month period commencing on January 1 and each anniversary thereafter.

Chair, Washtenaw County Board of Commissioners Date

Attested to by Date

Approved as to Form Date

AN ORDINANCE AMENDING SECTION 65 OF THE WASHTENAW COUNTY EMPLOYEES RETIREMENT SYSTEM TO AUTHORIZE THE RETIREMENT COMMISSION TO AMEND THE RETIREMENT SYSTEM TO COMPLY WITH THE INTERNAL REVENUE CODE AND RELATED AUTHORITY TO MAINTAIN THE QUALIFIED STATUS OF THE DEFINED BENEFIT PLAN.

Be it ordained by the Board of Commissioners of the County of Washtenaw that Section 65 of the Washtenaw County Employees Retirement System is hereby amended to read as follows:

Section 65(m) shall be added to read as follows:

The Retirement Commission may adopt by resolution such additional provisions to the Retirement System as are necessary to comply with the Internal Revenue Code and related authority to maintain the qualified status of the defined benefit plan.

Chair, Washtenaw County Board of Commissioners

Date

Attested to by

Date

Approved as to Form

Date