



HANDBOOK

Ohio County Commissioners

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CHAPTER 69

DEFERRED COMPENSATION

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69.01 INTRODUCTION

Public employee deferred compensation plans are governed by Section 457 of the Internal Revenue Code. All counties offer one or more deferred compensation plans to their employees. Very simply, a plan consists of an agreement between the county and the individual employee where the employee voluntarily reduces their salary for state and federal tax purposes. The county agrees to pay these deferred amounts, plus earnings, to the employee when they qualify for distribution.

Municipal income taxes and Public Employee Retirement System (PERS) contributions are computed on the gross salary, before the reduction. Thus, there is no impact on future PERS benefits which have been calculated on gross salary.

The amount of salary deferred is invested in one or more of the options available under the plan chosen by the employee. Legally these monies remain the property of the county until the employee qualifies for distribution at separation of service. Access to these deferred funds by the employee while still employed is limited to a severe financial emergency as defined in U.S. Department of the Treasury regulations. There are no 59½ age requirements or penalties for early withdrawal attendant to public employee deferred compensation plans.

Since the deferred monies are held in the county's name, the investment earnings are not taxable until withdrawn by the employee. The funds are held in trust by the

counties. They are a legal asset of the county in county's financial report, not the employee. The county shows the obligation to the employee as a future liability, offsetting the current asset.

69.02 HISTORY OF PUBLIC EMPLOYEE DEFERRED COMPENSATION

In 1960, the Internal Revenue Service (IRS) issued a Revenue Ruling 60-31 which became known as the "Doctrine of Constructive Receipt." Basically, it stated that monies earned by an individual cannot be taxed until paid to the individual.

Private sector corporations immediately initiated a form of deferred compensation for certain high-level, highly paid executives wherein they received a reduced salary, with the deferred amount being retained as a corporate asset until some future date. This was particularly common among professional sports organizations, where highly paid athletes received only a portion of their contractual salaries, with the remainder to be paid when their active playing careers were over. The shortcoming of this process and the reason it was limited to a select few was that these retained dollars were subject to corporate taxes on the assets and their investment earnings.

Local government units in California soon realized they could initiate a similar type of arrangement for their employees without being concerned about taxation on the assets or earnings because they were tax-exempt employers. The IRS could find no fault with this interpretation, but plans could only be activated if the state permitted the practice through passage of enabling legislation.

Ohio passed enabling legislation for public employee deferred compensation in 1976, establishing the "Ohio Public Employees Deferred Compensation Plan." The legislation, as introduced, dictated that all public employees in the state would be limited to participation in the "state plan" and its attendant investment vehicles. Immediately, the Ohio Municipal League pointed out that charter cities were not subject to such an edict from the state because of municipal home rule. The legislation was amended, granting autonomy to municipal corporations to establish and operate their own plans, separate from the "state plan." County government, through the CCAO, requested the same freedom of choice, but was informed that legally, counties were a statutory arm of the state government and were therefore, directly subject to the legislature. Counties had no option other than the "state plan."

During the early 1980's, CCAO received numerous complaints from individual counties regarding the operations of the "state plan." A strong lobbying effort took place over the next few years, culminating in a 1984 Act permitting counties to establish and operate their own deferred compensation plans.

69.03 STATE STATUTORY FRAMEWORK

ORC Chapter 148 contains the primary body of law concerning deferred compensation. The "state plan" is administered by a state deferred compensation board whose

members include the members of the public employee's retirement board and one member of the Ohio Senate and Ohio House of Representatives.

69.04 ADDITIONAL DEFERRED COMPENSATION PLANS FOR COUNTIES

As mentioned above, a change in the law in 1984 allowed counties to offer plans in addition to the "state plan." The law now provides that a county must offer the "state plan" to its employees. In addition to the "state plan" however, a county may offer up to two additional plans, but not more than a total of three plans.

69.05 AMOUNT OF DEFERRAL

The limit on elective deferrals into 401(k), 403(b) and 457(b) plans for 2014 remains at **\$17,500 for participants under the age of 50, while participants aged 50 and above will be able to contribute an additional \$5,500.**

Under the formula, the limitation does not increase until the inflation rate causes the index to increase by at least \$500. The contribution limit will only be increased in \$500 increments, no more often than annually. Thus, the rate of inflation will dictate how soon the cost-of-living index will result in a \$500 increase.

There is one major exception to this general rule on the maximum deferral. Employees who are eligible to participate in a 457 plan after 1978 and who did not make maximum deferrals during those years of service, may take advantage of a "Regular Catch Up Provision." In one or more of three years ending prior to Normal Retirement Age, an employee may "catch-up" underutilized contributions. The maximum special 457 catch-up amount for 2014 is \$35,000 (twice the basic §457(b) contribution limit). (§457(b)(3)). Participants may use greater of the age 50 catch-up or special §457 catch-up, but not both in same calendar year. (§457(e)(18)).

69.06 INVESTMENT OPTIONS UNDER DEFERRED COMPENSATION PLANS

Ohio law is fairly broad in describing the types of investments allowable under public employee deferred compensation plans. It allows annuity contracts, savings accounts, mutual funds and other "suitable" types of investment for long-term, retirement planning, including life insurance policies.

Both nationally and in Ohio, most successful plans offer some combination of the above investments. Each participating employee is free to choose which of the investments available best suits his or her personal needs.

69.07 WITHDRAWAL OF DEFERRED COMPENSATION FUNDS-TAXATION

Participants must meet a qualifying event in order to withdraw funds from their deferred compensation account. Qualifying distribution events are as follows:

1. Retirement.
2. Unforeseeable emergency within the Plan guidelines (as defined by the Internal Revenue Code and if allowed by your Plan's provisions).
3. Severance of employment (as defined by the Internal Revenue Code provisions).
4. Attainment of age 70½ (whether or not still employed).
5. Death (the beneficiary receives the benefits).
6. Transfer to purchase service credit.

Each distribution is subject to ordinary income tax except for an in-service transfer to purchase service credit. The current federal tax amount is 20%. Distributions from deferred compensation plans are taxable as regular income in the calendar year in which they are withdrawn.

The methods of withdrawal include lump-sum withdrawals, periodic payments, annuity payments or roll over to an eligible governmental 457(b), 401(k), 403(b) or 401(a) plan or IRA.

69.08 DEFERRED COMPENSATION ENROLLMENT/NON-SOLICITATION POLICIES

Most counties have in place stringent non-solicitation policies, intended to limit access to employees by outside vendors, organizers, etc.

Legal counsel has advised CCAO that these policies do not apply to deferred compensation enrollment or participant service procedures. The basis for this exception is that deferred compensation is a legislated benefit, adopted and installed by formal resolution of the county commissioners.

It thus falls into the same category as periodic health insurance enrollments; PERS seminars; or other benefits offered to county employees as a condition of their employment.

69.09 ATTACHMENT OF DEFERRED COMPENSATION PARTICIPANT ACCOUNTS

ORC Section 148.09 generally provides that an account of a participant in a deferred compensation program is not subject to execution, garnishment, attachment, or sale to satisfy a judgment or order. Likewise, a deferred compensation account is not subject to bankruptcy or insolvency laws.

There are, however, certain exceptions to this general rule. Often a divorce settlement determines that all or a portion of a participant's deferred compensation account should

be split and paid to an alternate payee—defined by the IRS as a spouse, former spouse, child or other dependent of a participant.

Under Ohio law, deferred compensation accounts of a participant are considered as marital property under ORC 3105.171 and can included in a separation agreement in a divorce or disillusionment of marriage under ORC 3105.63. Likewise some attachment is possible related to child support under ORC Chapters 3119, 3121, 3123, and 3125.

In order for the deferred compensation account of a participant to be attached or divided it must qualify as a Qualified Domestic Relations Order (QDRO), which is really a court order issued as a part of a divorce or can be included in a divorce or disillusionment decree. It must be reviewed and approved by the deferred compensation plan administrator to assure compliance with both state and federal law.

69.10 ATTACHMENT OF DEFERRED COMPENSATION PARTICIPANT ACCOUNTS FOR RESTITUTION ORDERED BY A COURT

Another exception to the general rule that deferred compensation accounts of participants are not subject to attachment is in cases where for certain crimes, courts order the use of the funds in the account to be used to pay court ordered financial sanctions or restitution to victims, including political subdivisions in cases involving theft in office by a public official or employee.

ORC Section 148.10 provides that the account of a deferred compensation participant is subject to a withholding order issued by a court for certain offenses. The withholding orders may be issued either under ORC Section 2907.15 or Division (C)(2)(b) of ORC Section 2921.41.

More specifically, if a deferred compensation program receives a notice that a person who is a participant in the plan has been charged with a violation of section 2907.02, 2907.03, 2907.04, 2907.05, or 2921.41 of the Revised Code, no payment from that participant's account can be made before one of the following occurs, whichever is applicable:

1. If the person is convicted of or pleads guilty to the violation and a motion for a withholding order for purposes of restitution has not been filed, 30 days after the day on which the person is sentenced for the violation;
2. If the person is convicted of or pleads guilty to the violation and a motion for a withholding order for purposes of restitution has been filed, the day on which the court decides the motion;
3. If the charge is dismissed or the person is found not guilty or not guilty by reason of insanity, the day on which the dismissal of the charge or the verdict is entered in the journal of the court.

69.11 CCAO DEFERRED COMPENSATION PROGRAM

After the enactment of legislation in 1984 authorizing counties to participate in deferred compensation programs other than the “state plan,” CCAO made the decision to establish a statewide deferred compensation plan exclusively for county governments. It was the intent of the CCAO Board of Directors that:

1. Operation of the deferred compensation program would be under the direct control of the counties, through the CCAO Board of Directors.
2. The collective financial leverage of numerous counties, through CCAO, would result in obtaining highly competitive investment options for county employees choosing to participate.

The CCAO program is totally controlled by the CCAO Board of Directors and each individual county. A separate CCAO Deferred Compensation Committee consisting of commissioners has been established to monitor operation of the program and act in an advisory capacity to the Directors.

Investment options are selected through a national competitive-bid process overseen by the CCAO Deferred Compensation Committee. This process is repeated annually to guarantee that the program contains the most competitive and up to date types of investments for county employees.

The CCAO program is offered by all 88 counties. Over 24,000 active and inactive participants have accumulated over \$550 million in retirement assets since the first enrollments began in mid-1985.

For more information and program details click on the following link to go to the CCAO Deferred Compensation Program website <https://ccao457.qwrs.com/login.do>