

BATH COUNTY SCHOOL BOARD

AGENDA ITEM: INFORMATION { } ACTION { X } CLOSED MEETING { }

SUBJECT: SUPERINTENDENT’S REPORT - ACTION

D. Employer-Sponsored Hybrid 403(b) Plan Election

BACKGROUND: Recent legislation (Senate Bill 1162 and House Bill 2178) allows school divisions to elect to allow eligible employees to use an employer-sponsored hybrid 403(b) plan for employee voluntary contributions to the Hybrid Retirement Plan. The two resolutions are as follows:

- Allow eligible employees the option to elect to direct hybrid voluntary contributions to an employer-sponsored hybrid 403(b) plan, instead of the VRS Hybrid 457 Deferred Compensation Plan.
- Not to offer this option, so that hybrid voluntary contributions will continue to be directed into the VRS Hybrid 457 Deferred Compensation Plan only.

RECOMMENDATION: Not to offer this option, so that hybrid voluntary contributions will continue to be directed into the VRS Hybrid 457 Deferred Compensation Plan only. By not allowing the option, VRS (not Bath County School Board) is responsible for the fiduciary and administrative duties associated with sponsorship of such a plan, including the development and maintenance of plan documents, compliance with applicable state and federal laws, investment selection and oversight, and acting in the best interest of a plan’s members and beneficiaries, among other responsibilities.



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July 10, 2015

Dear Employer,

Recent legislation (Senate Bill 1162 and House Bill 2178) allows school divisions to elect to allow eligible employees to use an employer-sponsored hybrid 403(b) plan for employee voluntary contributions to the Hybrid Retirement Plan. The employer match on these contributions will go into the 403(b) or the employer's cash match plan pursuant to the Internal Revenue Code 401(a).

Two resolutions are enclosed. Your local school board must elect by October 30 to either:

- Allow eligible employees the option to elect to direct hybrid voluntary contributions to an employer-sponsored hybrid 403(b) plan, instead of the VRS Hybrid 457 Deferred Compensation Plan; or
- Not to offer this option, so that hybrid voluntary contributions will continue to be directed into the VRS Hybrid 457 Deferred Compensation Plan only.

The formal signed resolution to either elect or decline to allow eligible employees to direct voluntary contributions to the employer-sponsored hybrid 403(b) plan must be postmarked **on or before November 2, 2015** (Attn: ZaeAnne Allen, employer coverage coordinator, P.O. Box 2500, Richmond, VA 23218-2500).

Enclosed you will find the following resources:

- Your Guide to the Employer-Sponsored Hybrid 403(b) Plan Election, which outlines considerations you will want to address before making this decision
- Resolution to Allow Eligible Employees to Direct Hybrid Voluntary Contributions to an Employer-Sponsored Hybrid 403(b) Retirement Plan
- Resolution to NOT Allow Eligible Employees to Direct Hybrid Voluntary Contributions to an Employer-Sponsored Hybrid 403(b) Retirement Plan
- Senate Bill 1162 and House Bill 2178 from the 2015 General Assembly Session
- Fiscal Impact Statement for the legislation
- Sample language for an employee election form

If you elect to offer this option, your Hybrid Retirement Plan employees will have from November 1 – 30 to elect to direct their voluntary contributions to either the VRS Hybrid 457 Deferred Compensation Plan or the employer-sponsored hybrid 403(b) plan that you offer. Employee elections made on or before November 30, 2015, will be effective January 1, 2016.

If you have any questions about the election process, contact ZaeAnne Allen, employer coverage coordinator, at zallen@varetire.org or (804) 775-3514. If you have other questions about the legislation, please contact your employer representative: Gwyn Ciemniecki at gciemniecki@varetire.org, (804) 771-7765, or Carolyn Newton at cnewton@varetire.org, (804) 344-3196.

Sincerely,

Patricia S. Bishop
VRS Director

Enclosures



Your Guide to the Employer-Sponsored Hybrid 403(b) Plan Election

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Your Guide to the Employer-Sponsored Hybrid 403(b) Plan Election

Following a 2015 legislative change (Senate Bill 1162 and House Bill 2178), school divisions will have the option to elect to allow their employees to use an employer-sponsored hybrid 403(b) plan for Hybrid Retirement Plan voluntary contributions. This document provides an overview of the employer's administrative responsibilities and a summary of key points you will need to convey to employees. If an employer elects to allow this option, it will go into effect January 1, 2016.

Considerations for Employers

Employer Elections

Your school board must elect by October 30 to either:

- Allow eligible employees the option to elect to direct hybrid voluntary contributions to an employer-sponsored hybrid 403(b) plan instead of the VRS Hybrid 457 Deferred Compensation Plan; or
- Not to offer this option, so that hybrid voluntary contributions will continue to be directed into the VRS Hybrid 457 Deferred Compensation Plan only.

School divisions will continue to be required to contribute a corresponding employer match to either:

- The VRS Hybrid 401(a) Cash Match Plan, if the voluntary contributions are being directed to the VRS Hybrid 457 Deferred Compensation Plan, or
- The employer-sponsored plan, which can be a 403(b) plan or a 401(a) plan.

Eligible employees include 4 code (teaching and administrative) and 5 code (non-administrative) Hybrid Retirement Plan employees. Make your election using one of the two resolutions enclosed in your resolution packet. The *Code of Virginia* states that the school board must make an election by November 1. Since that date falls on a Sunday in 2015, your school board must make an election by Friday, October 30. Resolutions must be postmarked on or before November 2 and returned to VRS. This is an annual election for school divisions.

If a school board fails to make an election before October 30, 2015, the default is that all employee hybrid voluntary contributions will be directed to the VRS Hybrid 457 Deferred Compensation Plan and the associated matching contributions will be directed to the VRS Hybrid 401(a) Cash Match Plan. In future years, if a school board fails to make an election, the default is the prior year's election (or, if there has never been an election, the VRS Hybrid 457 Deferred Compensation Plan and VRS Hybrid 401(a) Cash Match Plan remain the default).

If a school board elects to offer an employer-sponsored plan, hybrid plan employees within the school division will elect to make voluntary contributions to the employer-sponsored hybrid 403(b) plan or to the VRS Hybrid 457 Deferred Compensation Plan during an election period from November 1- 30. Employee elections will be effective January 1, 2016. This is also an annual election for employees (see Employee Elections).

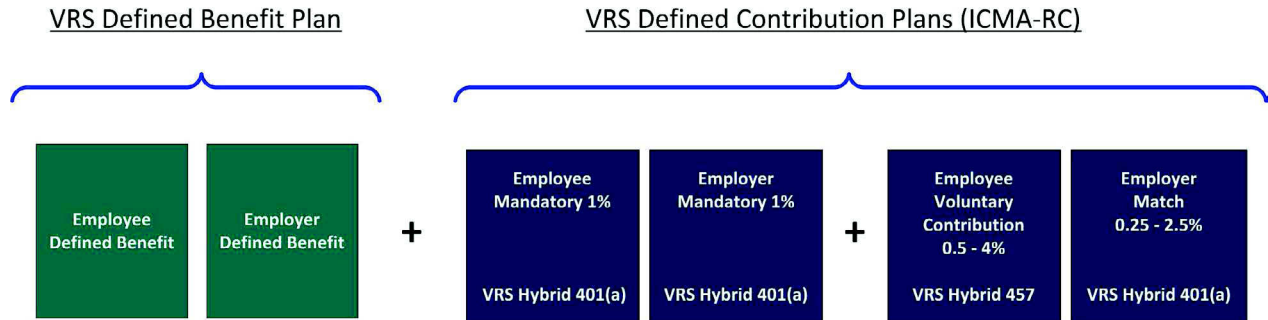
Please note that you will need to indicate in *myVRS* Navigator which employees have elected to use the employer-sponsored hybrid 403(b) plan. The system will only allow these entries from November 1 to December 10.

What the Election Will Mean to the Current Structure

Under the existing structure, VRS is the plan fiduciary for all defined contribution plans it administers including the VRS Hybrid 401(a) Cash Match Plan and the VRS Hybrid 457 Deferred Compensation Plan.

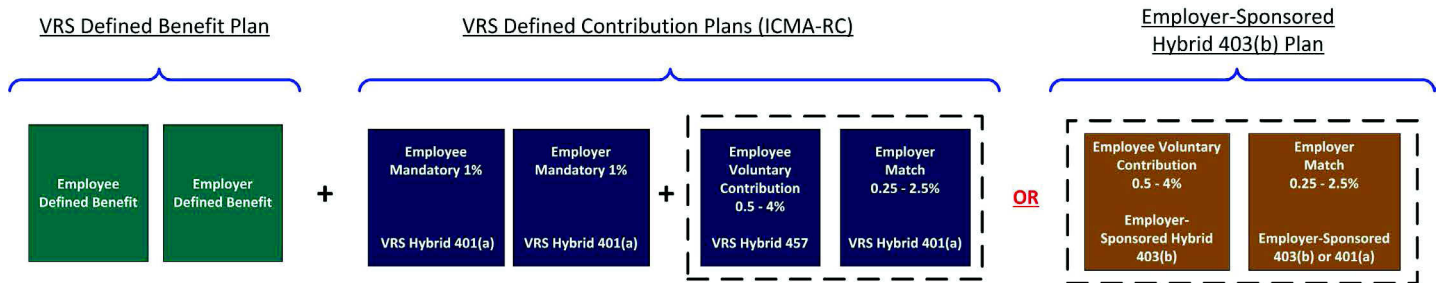
If you do not elect the employer-sponsored hybrid 403(b) plan option

Under the current hybrid plan structure, voluntary contributions are directed to the VRS Hybrid 457 Deferred Compensation Plan and the employer match is directed to the VRS Hybrid 401(a) Cash Match Plan as shown below.



If you elect to offer the employer-sponsored hybrid 403(b) plan option

If your school board makes an election to allow employees to contribute to an employer-sponsored hybrid 403(b) plan, you will be allowing employees the option to direct hybrid plan voluntary contributions to an employer-sponsored hybrid 403(b) plan instead of the VRS Hybrid 457 Deferred Compensation Plan. The corresponding employer match will be redirected to the employer-sponsored hybrid 403(b) plan or locally established 401(a) cash match plan, if applicable, instead of the VRS Hybrid 401(a) Cash Match Plan. Your school division will be the responsible fiduciary for the employer-sponsored hybrid 403(b) plan and any locally established 401(a) cash match plan, not VRS.



Note: If you elect to use an employer-sponsored 403(b) plan for hybrid voluntary contributions, the mandatory employee and employer contributions must still be made to the VRS Hybrid 401(a) Cash Match Plan with ICMA-RC as the record keeper.

Before Making an Election

Generally, a retirement plan sponsor is responsible for the fiduciary and administrative duties associated with sponsorship of such a plan, including the development and maintenance of plan documents, compliance with applicable state and federal laws, investment selection and oversight, and acting in the best interest of a plan's members and beneficiaries, among other responsibilities. VRS is unable to provide an electing employer with specific advice regarding the legal responsibilities of a retirement plan fiduciary. VRS recommends seeking legal counsel before making an election. The discussion below is general in nature and not intended as specific advice.

Fiduciary Responsibilities

If your school board elects to allow its Hybrid Retirement Plan employees to make voluntary contributions to an employer-sponsored hybrid 403(b) plan, then the school division will take on a number of fiduciary duties and responsibilities. The school division should become familiar with the “exclusive benefit rule” applicable to 403(b) plans and plans established under Section 401(a) of the Internal Revenue Code as well as with state law requirements.

The “exclusive benefit rule” has broad application and prohibits “all objects or aims not solely designed for the proper satisfaction of all liabilities to employees or their beneficiaries.” Thus, a fiduciary of a 403(b) plan or 401(a) plan must act solely in the interests of plan participants and beneficiaries and for the exclusive purpose of providing benefits to those participants and beneficiaries. The Internal Revenue Service (IRS) provides guidance on what it means to be a retirement plan fiduciary. While the IRS guidance is directed at private sector plans, subject to ERISA, it provides good information applicable to the “exclusive benefit rule.” You can learn more on the IRS website: <http://www.irs.gov/Retirement-Plans/Retirement-Plan-Fiduciary-Responsibilities>.

Section 51.1-169 (G) of the *Code of Virginia*, under which the school board plans may be established, generally requires compliance with the standards of Section 51.1-803 A of the *Code of Virginia*. That section provides that funds “shall be invested with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with the same aims.” This standard is identical to that set forth in ERISA and more fully explained on the IRS website.

Administrative Responsibilities

If your school division elects to allow its Hybrid Retirement Plan employees to make hybrid voluntary contributions to an employer-sponsored hybrid 403(b) plan, then the school division will take on a number of administrative duties and responsibilities. You will administer the employer-sponsored hybrid 403(b) plan you offer. This responsibility includes, but is not limited to, the following tasks:

Enforcing Hybrid Retirement Plan Provisions

As provided in Section 51.1-169 (G) (1) of the *Code of Virginia*, you will be responsible for developing policies and procedures to ensure enforcement of Hybrid Retirement Plan provisions. This includes:

- Administration of vesting provisions
- Establishment and use of a forfeiture account
- Automatic voluntary contribution escalation

Employee loans and hardship withdrawals are not permitted from the plans.

Vesting and Forfeiture

You will be responsible for establishing a forfeiture account to hold employer matching contributions from separated employees who take a distribution from the employer-sponsored hybrid 403(b) or 401(a) plan before being fully vested. Because vesting considers all VRS creditable service, you will need to contact VRS to determine the appropriate vesting percentage that should be applied to employer contributions before approving distributions from an employer-sponsored hybrid 403(b) plan or 401(a). A distribution from employer matching contributions is considered a plan-level forfeiture and only requires that the employer determine the correct vesting percentage and direct the record keeper to forfeit any non-vested employer funds prior to the distribution occurring.

Non-vested employer contributions in the defined contribution component of the Hybrid Retirement Plan would forfeit at the earlier of the time:

- The member requests a distribution from the employee mandatory or employer mandatory contributions in the defined contribution component of the hybrid plan

- The member requests a refund of his or her Member Contribution Account under the defined benefit component of the hybrid plan
- The member's death

These events initiate a global forfeiture of all non-vested employer contributions, which include both employer mandatory contributions and employer matching contributions. As such, VRS will notify you when one of these events occur. You will be responsible for notifying the record keeper(s) for your employer-sponsored hybrid 403(b) plan when a global forfeiture event occurs.

Auto Escalation

You will be required to administer automatic escalation provisions as required by Section 51.1 – 169 (C) (3) of the *Code of Virginia*. You will need to provide direction to your record keeper(s) for any employees participating in your employer-sponsored hybrid 403(b) plan for hybrid voluntary contributions. Additionally, you will need to communicate auto escalation information to your Hybrid Retirement Plan employees who participate in an employer-sponsored hybrid 403(b) plan and administer internal record-keeping procedures for those who opt out of the auto escalation.

Payroll Systems

Additional payroll modifications may be necessary to administer the various contribution types for the Hybrid Retirement Plan.

Adjustments

You will be responsible for working with your 403(b) provider to correct any contribution errors and adjust member records. You should continue to reconcile your mandatory contributions against your Snapshot.

Overseeing Participant IRS Limits

Similar to contributions to the VRS Hybrid 457 Deferred Compensation Plan, you are responsible for overseeing annual participant Internal Revenue Service (IRS) limits that pertain to both contributions and compensation.

Even if you administer multiple 403(b) plans, you are responsible for tracking the IRS annual contribution limits for your employees. This includes any voluntary contributions to an employer-sponsored hybrid 403(b) plan.

Annual Disclosures

Section 51.1 – 169 (G) of the *Code of Virginia* requires the sponsor to make certain disclosures relating to plan investments. You are responsible for annually disclosing all services, fees, restrictions and surrender penalties associated with an employer-sponsored hybrid 403(b) plan and 401(a) cash match plan. You must also provide a side-by-side comparison of fees and their long-term effects on investments. VRS provides this information to members annually for the VRS Hybrid 457 Deferred Compensation Plan and VRS Hybrid 401(a) Cash Match Plan.

Changes to Voluntary Contribution Percentages

Employees should not be allowed to change their voluntary contribution percentage more frequently than monthly.

Reporting Information

VRS will not maintain the hybrid plan voluntary contribution percentages for members using an employer-sponsored hybrid 403(b) plan for voluntary hybrid contributions. Therefore, *myVRS* Navigator will not provide the amount of voluntary contributions and the employer match in your Snapshot.

Calculations of contributions sent to your employer-sponsored hybrid 403(b) plan must follow the *myVRS* Navigator business rules and guidelines regarding contract employees. This includes calculation of creditable compensation/contribution basis, the allowable voluntary contribution percentages, and the calculation of the employer match on voluntary contributions.

As provided in the *Code of Virginia*, the percentage of voluntary contributions made to an employer-sponsored hybrid 403(b) plan must be based on creditable compensation. Creditable compensation is an employee's annual salary not including overtime pay, payment of a temporary nature or payments for extra duties such as pay for teachers who provide coaching or act as an advisor for special activities, divided by the employee's contract period. Contract periods are 9, 10, 11 or 12 months.

Employees with contracts less than 12 months can be paid over a contract period or 12 months. If an employee with a contract less than 12 months is paid over 12 months rather than over the contract period, contributions to VRS are based on a contribution basis (annual salary/12) rather than creditable compensation (annual salary/contract length). Contributions should also be submitted to your 403(b) provider on a contribution basis.

You will be responsible for correctly calculating the contribution amounts based on elected voluntary contribution percentages and creditable compensation or contribution basis, as applicable. You bear the responsibility for reconciliation of any employee voluntary contributions and employer matching contributions made to an employer-sponsored hybrid 403(b) plan. VRS recommends that you allow employees to change voluntary contribution percentages on a quarterly basis. Because *myVRS* Navigator rules calculate creditable compensation/contribution basis on a monthly basis, employees should not be allowed to change their voluntary contribution percentage more frequently than monthly.

Offset of VRS Employer Defined Benefit Contributions

Since VRS will not maintain the voluntary contribution percentages for members participating in your employer-sponsored hybrid 403(b) plan, the defined benefit plan employer contributions for these members will only be reduced by the 1 percent mandatory employer contribution, and reflected accordingly in your monthly *myVRS* Navigator Snapshot.

You must pay the full employer defined benefit contribution amount calculated in your *myVRS* Navigator Snapshot each month. On a quarterly basis, a credit will be issued to your VRS accounts receivable for the employer matching contributions. To receive the offset to your defined benefit contributions, you will submit data to VRS indicating the employer matching contribution amounts paid to the employer-sponsored hybrid 403(b) plan or 401(a) cash match plan.

The Auditor of Public Accounts will provide testing guidelines to your auditors for your annual audit that will include:

- Calculation of voluntary contributions to the employer-sponsored hybrid 403(b) plan
- The employer match on these voluntary contributions
- The offset of the VRS employer defined benefit contributions that you received

Use of the VRS Logo

Although an employer-sponsored hybrid 403(b) plan is an element of the Hybrid Retirement Plan, VRS does not administer employer-sponsored plans. Therefore, use of the VRS logo and/or other VRS branding is prohibited on forms and documents affiliated with an employer-sponsored plan.

Considerations for Employees

Employee Elections

If you elect to allow it, your Hybrid Retirement Plan employees will have the option to elect to participate in the employer-sponsored hybrid 403(b) plan or the VRS Hybrid 457 Deferred Compensation Plan during an election period from November 1 to 30. You will be responsible for providing the appropriate information regarding the option to your employees, providing an election form using the sample language provided by VRS, tracking elections and recording the employee's election for an employer-sponsored hybrid 403(b) plan in myVRS Navigator. Sample language for an employee election form is enclosed in the resolution packet.

Employee elections will be effective January 1, 2016. You will need to ensure that your employer-sponsored hybrid 403(b) plan is in place before this date.

Employees whose employers have elected to allow this option can elect to participate in the employer-sponsored hybrid 403(b) plan or the VRS Hybrid 457 Deferred Compensation Plan annually. They cannot make contributions to both at the same time. They can elect to participate in the employer-sponsored hybrid 403(b) plan during the annual election period (November 1 – 30) without selecting a contribution percentage. Employees can begin making contributions in a subsequent month or quarter.

Employees cannot make an election to use an employer-sponsored hybrid 403(b) plan or to switch between the VRS Hybrid 457 Deferred Compensation Plan and the employer-sponsored hybrid 403(b) plan outside of the annual election period. For this year only, the default for employees who do not make an election is the VRS Hybrid 457 Deferred Compensation Plan. In subsequent years, the default is the prior year's election (or, if there has never been an election, the VRS Hybrid 457 Deferred Compensation Plan remains the default).

New hybrid plan employees who are hired throughout the year can begin making voluntary contributions at any time. However, if they are hired outside of the annual election period, contributions can only be directed to the VRS Hybrid 457 Deferred Compensation Plan and the associated employer match will be directed to the VRS Hybrid 401(a) Cash Match Plan. Employees can change their election during the next election period.

Examples:

- 1. Sara is a current hybrid plan employee who elects to participate in the employer-sponsored hybrid 403(b) plan during the election period.** She does not select a voluntary contribution percentage at the time of her election in the fall. On June 14 of the following year, she contacts the plan record keeper to begin making a 2 percent hybrid voluntary contribution. Her contributions to the employer-sponsored hybrid 403(b) plan will begin either the beginning of the following month or following quarter depending on plan design.
- 2. Marcus is a new hybrid plan employee hired July 1.** He cannot elect to participate in the employer-sponsored hybrid 403(b) plan until your next annual election window. He has the option to:
 - Begin making hybrid voluntary contributions that will be directed into the VRS Hybrid 457 Deferred Compensation Plan and elect to stay in this plan during the election window
 - Wait until the next election window to begin directing hybrid voluntary contributions to the employer-sponsored hybrid 403(b) plan
 - Begin making hybrid voluntary contributions to the VRS Hybrid 457 Deferred Compensation Plan and switch to the employer-sponsored 403(b) plan during the next election window

Fee Structure

Generally, VRS deferred compensation plans offer lower investment management fees to participants than those in the private sector. It may cost your employees more to participate in an employer-sponsored hybrid 403(b) plan. Advise your employees to compare investment management fees when making a decision about which plan to elect.

ICMA-RC will charge a record-keeping fee of \$2.54 a month, \$30.50 per year, for the mandatory contributions to the VRS Hybrid 401(a) Cash Match Plan. Members pay one plan administration fee regardless of the number of accounts held with ICMA-RC, including the Commonwealth of Virginia 457 Deferred Compensation Plan (if applicable). Employees who elect to participate in an employer-sponsored hybrid 403(b) plan will be subject to the ICMA-RC fees and any fees associated with the employer-sponsored plan.

myVRS Account Balance and Multiple Retirement Plans

VRS can provide a holistic picture of employee Hybrid Retirement Plan accounts under the current structure. VRS will not be able to include contribution information in *myVRS* for an employer-sponsored hybrid 403(b) plan. If your employees elect to participate in an employer-sponsored hybrid 403(b) plan, they will not be able to view their Hybrid Retirement Plan total account balance in *myVRS*.

If employees elect to switch from the VRS Hybrid 457 Deferred Compensation Plan to an employer-sponsored hybrid 403(b) plan, or vice versa, they will have multiple retirement plans under different providers:

- Defined benefit member contribution account with VRS
- VRS Hybrid 401(a) Cash Match Plan (for employer match on the mandatory 1% contribution)
- VRS Hybrid 457 Deferred Compensation Plan
- Employer-sponsored hybrid 403(b) plan
- Employer-sponsored hybrid 401(a) plan if the employer chooses this plan for the employer match on voluntary contributions

Changing Employers

If an employee moves to another VRS-covered employer, the new employer may not have elected to allow employees to make voluntary hybrid contributions to an employer-sponsored hybrid 403(b) plan or may not use the same provider. In that situation, an employee would have to direct his or her voluntary contributions to a different plan and would have multiple retirement plans in place.

Rollovers

Employees cannot roll money out of the VRS Hybrid 457 Deferred Compensation Plan or VRS Hybrid 401(a) Cash Match plan while employed in a VRS-covered position.

Employees can roll over money from other eligible plans to the VRS Hybrid 457 Deferred Compensation Plan. A rollover is a transfer of a pre-tax, lump-sum payment to another qualified plan. A rollover allows employees to continue to defer income taxes until they withdraw money from the plan.

Rollovers are not allowed into the VRS Hybrid 401(a) Cash Match Plan.

Webinar Registration

Sign up for The Employer-Sponsored Hybrid 403(b) Option Resolution Process webinar from 1 to 2 p.m. August 12 at www.varetire.org/hybrid-er.

Questions?

For questions about this legislative change, contact your employer representative:

- Gwyn Ciemniecki at gciemniecki@varetire.org or 804-771-7765
- Carolyn Newton at cnewton@varetire.org or 804-344-3196

For questions about the election process, contact **ZaeAnne Allen**, employer coverage coordinator, at zallen@varetire.org or 804-775-3514.

RESOLUTION TO ALLOW ELIGIBLE EMPLOYEES TO DIRECT HYBRID VOLUNTARY CONTRIBUTIONS TO AN EMPLOYER-SPONSORED HYBRID 403(b) RETIREMENT PLAN

(Pursuant to Chapters 538 and 539 of the 2015 Acts of Assembly)

The language in this resolution has been approved by the VRS Benefits Counsel and is not subject to modification.

Please check this box to indicate that (the “**School Division**”) intends to exercise its election, pursuant to the Code of Virginia § 51.1-169(G), to allow its eligible employees to use an employer-sponsored Hybrid 403(b) plan instead of the Hybrid 457 Deferred Compensation Plan for voluntary contributions and an employer-sponsored Hybrid 403(b) plan or an employer-sponsored 401(a) cash match plan for the associated employer matching contributions described in the Code of Virginia § 51.1-169 (the “Hybrid Retirement Plan”).

WHEREAS, the School Division employs members who participate in the Virginia Retirement System’s (“VRS”) Hybrid Retirement Plan, which consists of a defined benefit component and a defined contribution component; and

WHEREAS, the defined contribution component of the Hybrid Retirement Plan requires a covered employee to make a mandatory contribution of 1% of creditable compensation to the defined contribution component, in addition to a 4% contribution to the defined benefit component; and

WHEREAS, employees of the School Division who participate in the Hybrid Retirement Plan may also make voluntary contributions of up to 4% of creditable compensation to the defined contribution component of the Hybrid Retirement Plan; and

WHEREAS, the Hybrid Retirement Plan requires the School Division to provide a matching contribution on behalf of an employee based on that employee’s Hybrid Retirement Plan voluntary contributions; and

WHEREAS, an employee’s voluntary contributions are deposited in that employee’s Hybrid 457 Deferred Compensation Plan account, and the associated employer match is deposited in that employee’s Hybrid 401(a) Cash Match Plan account; and

WHEREAS, the Hybrid 457 Deferred Compensation Plan and the Hybrid 401(a) Cash Match Plan are administered by VRS and its third-party administrator for members who make contributions under the original framework of the Hybrid Retirement Plan; and

WHEREAS, the Internal Revenue Code permits an eligible employer to establish a supplemental retirement plan pursuant to 26 U.S.C § 403(b); and

WHEREAS, Chapters 538 and 539 of the 2015 Acts of Assembly permit the School Division to elect on an annual basis whether to allow its eligible Hybrid Retirement Plan employees i) to make Hybrid voluntary contributions to an employer-sponsored Hybrid 403(b) plan established by the School Division, as an alternative to the Hybrid 457 Deferred Compensation Plan maintained by VRS and ii) to have the associated employer match deposited in the 403(b) plan or cash match plan established and maintained by the School Division; and

WHEREAS, upon such election of the School Division, each eligible employee will continue to make Hybrid voluntary contributions to the Hybrid 457 Deferred Compensation Plan unless the employee makes an affirmative election between November 1 and November 30 to instead contribute to an employer-sponsored Hybrid 403(b) plan established by the School Division; and

WHEREAS, prior to making the election, the School Division has read “Your Guide to the Employer-Sponsored Hybrid 403(b) Plan Election” and understands and has processes and procedures in place to carry out:

- the fiduciary responsibilities and duties imposed by Code of Virginia § 51.1-803 as applicable through Code of Virginia § 51.1-169(G)(4);
- the administrative duties and responsibilities associated with sponsoring a plan or plans for the Hybrid voluntary contributions and associated employer match under the Code of Virginia § 51.1-169; and
- the administrative duties and responsibilities associated with sponsoring a retirement plan or plans intended to qualify for favorable tax treatment under the Internal Revenue Code.

NOW, THEREFORE, BE IT RESOLVED, that the School Division hereby elects, pursuant to the Code of Virginia § 51.1-169(G), to allow its employees the option to direct i) voluntary contributions to an employer-sponsored Hybrid 403(b) plan established by the School Division, and ii) the associated employer match to such 403(b) plan or to a 401(a) cash match plan established by the School Division; and

BE IT FURTHER RESOLVED, that by making the election, the School Division acknowledges that under no circumstances shall the Commonwealth, the VRS Board of Trustees, VRS employees, the VRS Investment Advisory Committee, or any other advisory committee established by the VRS Board of Trustees bear any liability with respect to any employer-sponsored Hybrid 403(b) plan or individual account established by the School Division, and that VRS has no fiduciary or administrative responsibility with respect to any employer-sponsored Hybrid 403(b) plan or cash match plan established by the School Division; and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to comply with the “prudent person” rule to provide for the investment of the assets of the employer-sponsored Hybrid 403(b) plan and any associated cash match plan with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with the same aims, pursuant to the Code of Virginia § 51.1-803(A); and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to provide for the investment of the assets of the 403(b) plan and any associated cash match plan in a diversified manner so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to operate the 403(b) plan and any associated cash match plan for the exclusive benefit of plan participants and their beneficiaries; and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to ensure that all Hybrid voluntary contributions made by its employees are made on a pre-tax basis and deposited in the applicable plan as soon as administratively possible following the date such contributions would otherwise have been paid in cash; and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to develop policies and procedures for administering the voluntary contributions of employees who make an affirmative election to contribute to an employer-sponsored Hybrid 403(b) plan established by the School Division, and that such policies and procedures shall provide for the enforcement and administration of the vesting provisions of the Code of Virginia § 51.1-169(B)(3), provisions related to the establishment and uses of a forfeiture account as provided in the Code of Virginia § 51.1-169(B)(3), and the automatic escalation provisions of the Code of Virginia § 51.1-169(C)(3); and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees that any employer-sponsored Hybrid 403(b) plan or cash match established by the School Division shall not permit loans or hardship withdrawals from contributions made by the employer; and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to provide each employee the annual option to elect to contribute Hybrid voluntary contributions to an employer-sponsored Hybrid 403(b) plan, so long as the employee election is made between November 1 and November 30; and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to provide, at least annually to each employee who elects to contribute Hybrid voluntary contributions to an employer-sponsored Hybrid 403(b) plan, a disclosure of all services, fees, restrictions, and surrender penalties associated with its 403(b) plan and any associated cash match plan, as well as a side-by-side comparison that demonstrates the long-term impact of expense ratios (fees) on the value of his or her investments over time; and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to monitor and ensure that each employee who elects to contribute Hybrid voluntary contributions to an employer-sponsored Hybrid 403(b) plan does not exceed the annual contribution limits established by the Internal Revenue Code; and

BE IT FURTHER RESOLVED, that by making the election, the School Division agrees to provide to, and in a manner prescribed by, VRS, on at least a quarterly basis, the total amount of employer matching contributions that the School Division made on behalf of its employees who elected to contribute Hybrid voluntary contributions to an employer-sponsored Hybrid 403(b) plan; and

BE IT FURTHER RESOLVED, that this election becomes effective January 1, 2016, and remains irrevocable for at least 12 months, and longer if the School Division does not reverse a prior election in subsequent years pursuant to the Code of Virginia § 51.1-169(G); and

BE IT FURTHER RESOLVED, that in order to reverse a prior election, the School Division shall, on or before November 1 of a subsequent year, pass a resolution to reverse its previous election and submit such resolution to VRS by a date required by VRS, which resolution shall become effective the following January 1.

NOW, THEREFORE, the officers of the School Division are hereby authorized and directed to carry out the provisions of this resolution in compliance with all applicable laws and regulations of the Commonwealth of Virginia and of the United States, and said officers are authorized and directed to communicate a true and certified copy of this resolution to VRS upon its passage.

Signature: _____
School Board Chairman

CERTIFICATE

I, _____ **[name]**, the _____ **[title]** of the School Division, certify that i) the foregoing is a true and accurate copy of a resolution passed at a lawfully organized meeting of the School Division held in _____ **[city/town]**, Virginia, at _____ **[time]** on _____ **[date of meeting]**, 2015, and ii) the terms of the foregoing resolution do not differ from the resolution provided by VRS. Given under my hand and seal of the School Division this _____ **[date of certification]** day of _____ **[month of certification]** 2015.

Signature: _____

Individual of Record in Certification

**RESOLUTION NOT TO ALLOW ELIGIBLE EMPLOYEES TO DIRECT
HYBRID VOLUNTARY CONTRIBUTIONS TO AN EMPLOYER-SPONSORED
HYBRID 403(b) RETIREMENT PLAN**

(Pursuant to Chapters 538 and 539 of the 2015 Acts of Assembly)

The language in this resolution has been approved by the VRS Benefits Counsel and is not subject to modification.

Please check this box to indicate that _____
(the “**School Division**”) does not wish to exercise the election provided in the Code of Virginia § 51.1-169(G) to allow its eligible employees to participate in an employer-sponsored Hybrid 403(b) plan for voluntary contributions to the defined contribution component of the hybrid retirement program described in the Code of Virginia § 51.1-169 (the “Hybrid Retirement Plan”).

WHEREAS, the School Division employs members who participate in the Virginia Retirement System’s (“VRS”) Hybrid Retirement Plan, which consists of a defined benefit and defined contribution component; and

WHEREAS, Chapters 538 and 539 of the 2015 Acts of Assembly permit the School Division to elect, on an annual basis, to allow its Hybrid Retirement Plan employees: i) to make Hybrid voluntary contributions to an employer-sponsored Hybrid 403(b) plan established by the School Division, as an alternative to the Hybrid 457 Deferred Compensation Plan maintained by VRS, and ii) to have the associated employer match deposited in the 403(b) plan or cash match plan established and maintained by the School Division; and

WHEREAS, the School Division understands that it may change its election annually, but that this Resolution will remain in force until the School Division adopts and files a new Resolution with VRS before November 1 to be effective for the following calendar year.

THEREFORE, BE IT RESOLVED, that the School Division elects not to allow eligible employees to direct Hybrid voluntary contributions to an employer-sponsored Hybrid 403(b) plan for the period from January 1, 2016, until a subsequent Resolution is timely adopted and filed with VRS.

NOW, THEREFORE, the officers of the School Division are hereby authorized and directed to communicate a true and certified copy of this resolution to VRS upon its passage.

Signature: _____
School Board Chair

CERTIFICATE

I, _____ [name], the _____ [title] of the School Division, certify that i) the foregoing is a true and accurate copy of a resolution passed at a lawfully organized meeting of the School Division held in _____ [city/town], Virginia, at _____ [time] on _____ [date of meeting], 2015, and ii) the terms of the foregoing resolution do not differ from the resolution provided by VRS. Given under my hand and seal of the School Division this _____ [date of certification] day of _____ [month of certification], 2015.

Signature: _____
Individual of Record in Certification

VIRGINIA ACTS OF ASSEMBLY -- 2015 SESSION

CHAPTER 539

An Act to amend and reenact §§ 51.1-169 and 51.1-610 of the Code of Virginia, relating to hybrid retirement program; school division deferred compensation and cash match plans.

[H 2178]

Approved March 23, 2015

Be it enacted by the General Assembly of Virginia:

1. That §§ 51.1-169 and 51.1-610 of the Code of Virginia are amended and reenacted as follows:

§ 51.1-169. Hybrid retirement program.

A. For purposes of this section, "hybrid retirement program" or "program" means a hybrid retirement program covering any employee in a position covered for retirement purposes under the provisions of Chapter 1 (§ 51.1-124.1 et seq.) for retirement purposes other than the Virginia Retirement System defined benefit retirement plan established under Chapter 1 (§ 51.1-124.1 et seq.). Persons who are participants in, or eligible to be participants in, the retirement plans under the provisions of Chapter 2 (§ 51.1-200 et seq.), Chapter 2.1 (§ 51.1-211 et seq.), the optional retirement plans established under §§ 51.1-126.1, 51.1-126.3, 51.1-126.4, and 51.1-126.7, or a person eligible to earn the benefits permitted by § 51.1-138 shall not be eligible to participate in the hybrid retirement program. Any person who is employed as a firefighter, emergency medical technician, or law-enforcement officer as those terms are defined in § 15.2-1512.2 and whose employing political subdivision has legally adopted an irrevocable resolution as described in subdivision B 4 of § 51.1-153 and subdivision A 3 of § 51.1-155 shall not be eligible to participate in the hybrid retirement program. No member of the Judicial Retirement System under Chapter 3 (§ 51.1-300 et seq.) shall be eligible to participate in the hybrid retirement program described in § 51.1-169 except members appointed to an original term on or after January 1, 2014.

The Board shall maintain the hybrid retirement program established by this section, and any employer is authorized to make contributions under such program for the benefit of its employees participating in such program. Every person who is otherwise eligible to participate in the program but is not a member of a retirement plan administered by the Virginia Retirement System the first time he is hired on or after January 1, 2014, in a covered position, shall participate in the hybrid retirement program established by this section.

A person who participates in the otherwise applicable defined benefit retirement plan established by this title and administered by the Virginia Retirement System under this chapter may make an irrevocable election to participate in the hybrid retirement program maintained under this section. Such election shall be exercised no later than April 30, 2014. If an election is not made by April 30, 2014, such employee shall be deemed to have elected not to participate in the hybrid retirement program and shall continue to participate in his current retirement plan.

B. *Except as otherwise provided in subsection G:*

1. The employer shall make contributions to the defined benefit component of the program in accordance with § 51.1-145.

2. The employer shall make a mandatory contribution to the defined contribution component of the program on behalf of an employee participating in the program in the amount of one percent of creditable compensation, *which shall be made to the appropriate cash match plan established for the employee under § 51.1-608*. In addition, the employer shall make a matching contribution on behalf of the employee based on the employee's voluntary contributions under the defined contribution component of the program to the deferred compensation plan established under § 51.1-602, up to a maximum of 2.5 percent of creditable compensation for the payroll period, as follows: (i) 100 percent of the first one percent of creditable compensation contributed by the employee to the defined contribution component of the program under subdivision C 2 for the payroll period, and (ii) 50 percent of the next three percent of creditable compensation contributed by the employee to the defined contribution component of the program under subdivision C 2 for the payroll period. The matching contribution by the employer shall be made to the appropriate cash match plan established for the employee under § 51.1-608.

3. The total amount contributed by the employer under subdivision 2 shall vest to the employee's benefit according to the following schedule:

- a. Upon completion of two years of active participation, 50 percent.
- b. Upon completion of three years of active participation, 75 percent.
- c. Upon completion of four years of active participation, 100 percent.

For purposes of this subdivision, "active participation" includes creditable service, as defined in § 51.1-124.3, in any retirement plan established by this title and administered by the Retirement System.

If an employee terminates employment with an employer prior to achieving 100 percent vesting, contributions made by an employer on behalf of the employee under subdivision 2 that are not vested,

shall be forfeited. The Board may establish a forfeiture account and may specify the uses of the forfeiture account.

4. An employee may direct the investment of contributions made by an employer under subdivision B 2.

5. No loans or hardship distributions shall be available from contributions made by an employer under subdivision B 2.

C. Except as otherwise provided in subsection G:

1. An employee participating in the hybrid retirement program maintained under this section shall, pursuant to procedures established by the Board, make mandatory contributions on a salary reduction basis in accordance with § 414(h) of the Internal Revenue Code (i) to the defined benefit component of the program in the amount of four percent of creditable compensation in lieu of the amount described in subsection A of § 51.1-144 and (ii) to the defined contribution component of the program in the amount of one percent of creditable compensation, *which shall be made to the appropriate cash match plan established for the employee under § 51.1-608.*

2. An employee participating in the hybrid retirement program may also make voluntary contributions to the defined contribution component of the program of up to four percent of creditable compensation or the limit on elective deferrals pursuant to § 457(b) of the Internal Revenue Code, whichever is less. The contribution by the employee shall be made to the appropriate deferred compensation plan established by the employee under § 51.1-602.

3. If an employee's voluntary contributions under subdivision C 2 are less than four percent of creditable compensation, the contribution will increase by one-half of one percent, beginning on January 1, 2017, and every three years thereafter, until the employee's voluntary contributions under subdivision C 2 reach four percent of creditable compensation. The increase will be effective beginning with the first pay period that begins in such calendar year unless the employee elects not to increase the voluntary contribution in a manner prescribed by the Board.

4. No loans or hardship distributions shall be available from contributions made by an employee under this subsection.

5. Disclosure of all services, fees, restrictions, and surrender penalties associated with employee voluntary contributions under subdivision C 2 shall be provided by the Board on an annual basis to an employee who does not make the election provided in subdivision G 1.

D. 1. The amount of the service retirement allowance under the defined benefit component of the program shall be governed by § 51.1-155 for all creditable service credited prior to the effective date of the member's participation in the program. For all other creditable service, the allowance shall equal one percent of a member's average final compensation multiplied by the amount of his creditable service while in the program. For judges who are participating in the hybrid retirement program, creditable service shall be determined as provided in § 51.1-303 and service retirement eligibility shall be determined as provided in § 51.1-305.

2. No member shall retire for disability under the defined benefit component of the program.

3. Except as provided in subdivision 1, any employee participating in the hybrid retirement program maintained under this section shall be considered to be a person who becomes a member on or after July 1, 2010.

4. In all other respects, administration of the defined benefit component of the program shall be governed by the provisions of Chapter 1 (§ 51.1-124.1 et seq.).

E. With respect to any employee who elects, pursuant to subsection A, to participate in the otherwise applicable defined benefit retirement plan established by this title and administered by the Virginia Retirement System, the employer shall collect and pay all employee and employer contributions to the Virginia Retirement System for retirement and group life insurance in accordance with the provisions of Chapter 1 (§ 51.1-124.1 et seq.) for such employee.

F. 1. The Board shall develop policies and procedures for administering the hybrid retirement program it maintains, including the establishment of guidelines for employee elections and deferrals under the program.

2. No employee who is an active member in the hybrid retirement program maintained under this section shall also be an active member of any other optional retirement plan maintained under the provisions of Chapter 1 (§ 51.1-124.1 et seq.).

3. If a member of the hybrid retirement program maintained under this section is at any time in service as an employee in a position covered for retirement purposes under the provisions of Chapter 1 (§ 51.1-124.1 et seq.), 2 (§ 51.1-200 et seq.), 2.1 (§ 51.1-211 et seq.), or 3 (§ 51.1-300 et seq.), his benefit payments under the hybrid retirement program maintained under this section shall be suspended while so employed; provided, however, reemployment shall have no effect on a payment under the defined contribution component of the program if the benefit is being paid in an annuity form under an annuity contract purchased with the member's account balance.

4. Any administrative fee imposed pursuant to subdivision A 13 of § 51.1-124.22 on any employer for administering and overseeing the hybrid retirement program maintained under this section shall be charged for each employee participating in such program and shall be for costs incurred by the Virginia

Retirement System that are directly related to the administration and oversight of such program. Notwithstanding the foregoing, the Board is authorized to collect all or a portion of such fee directly from the employee.

5. The creditable compensation for any employee on whose behalf employee or employer contributions are made into the hybrid retirement program shall not exceed the limit on compensation as adjusted by the Commissioner of the Internal Revenue Service pursuant to the transition provisions applicable to eligible participants under state and local governmental plans under § 401(a)(17) of the Internal Revenue Code as amended in 1993 and as contained in § 13212(d)(3) of the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66).

6. The Board may contract with private corporations or institutions, subject to the standards set forth in § 51.1-124.30, to provide investment products as well as any other goods and services related to the administration of the hybrid retirement program, *except as provided in subsection G*. The Virginia Retirement System is hereby authorized to perform related services, including but not limited to, providing consolidated billing, individual and collective recordkeeping and accountings, and asset purchase, control, and safekeeping.

G.1. Any political subdivision of the Commonwealth that has established a plan pursuant to § 403(b) of the Internal Revenue Code of 1986, as amended (a "403(b) plan"), may, at its option, elect to allow its employees the option to direct that voluntary contributions to the defined contribution component of the program under subdivision C 2 be made to such 403(b) plan and the corresponding employer matching contributions under subdivision B 2 be made to such 403(b) plan or the appropriate local cash match plan established under § 51.1-610. All such voluntary contributions by an employee to such 403(b) plan shall be made on a pretax basis. Any such political subdivision of the Commonwealth that so directs shall develop policies and procedures for administering such contributions, subject to and in accordance with applicable federal law and regulations. The policies and procedures shall provide for the administration of vesting provisions as provided in subdivision B 3, the establishment of and uses for a forfeiture account as provided in subdivision B 3, and automatic contribution escalation provisions as provided in subdivision C 3, all with regard to employee voluntary contributions and corresponding employer matching contributions.

In all other respects, the political subdivision shall be subject to the provisions of the hybrid retirement program described in this section.

2. The governing body of any political subdivision of the Commonwealth electing to allow its employees to use its 403(b) plan or a local cash match plan as described in subdivision 1 shall adopt a resolution on or before November 1, 2015, and submit such resolution to the Board to notify the Board of its election, which shall be effective January 1, 2016, and shall remain effective for 12 months. Thereafter, the governing body of any political subdivision of the Commonwealth may make or change its election for its employees no more often than annually by adopting a resolution on or before November 1 of each year notifying the Board of a new or changed election, which shall become effective on January 1.

3. A person who participates in the hybrid retirement program maintained under this section may make an election to participate in the 403(b) plan established by his employer under subdivision G 1. Such election shall be exercised no later than November 30, 2015, and shall be effective January 1, 2016. If an election is not made by November 30, 2015, such employee shall be deemed to have elected not to participate in the 403(b) plan established by his employer under subdivision G 1. Thereafter, such employee may make or change his election on or before November 30 of each year by notifying his employer of a new or changed election, which shall become effective the following January 1. If an election is not made or changed by November 30, such employee shall be deemed to have elected not to change the prior year's election.

4. In the case of a 403(b) plan or local cash match plan administered by a political subdivision of the Commonwealth that provides individual accounts permitting an employee or beneficiary to exercise discretion over assets in his account, the political subdivision shall not be liable for any loss resulting from such employee's or beneficiary's (i) investment of voluntary contributions in the political subdivision's 403(b) plan or matching contributions in the political subdivision's 403(b) plan or local cash match plan, (ii) exercise of discretion over the assets in any of his accounts, or (iii) inaction with respect to the assets in any of his accounts that results in such assets being placed in a default investment option selected by the political subdivision, provided that the investment options for the affected individual account and the particular default investment option for such individual account are selected in accordance with subsection A of § 51.1-803, applied mutatis mutandis. Under no circumstances shall the Commonwealth, the Board, employees of the Retirement System, the Investment Advisory Committee of the Retirement System, or any other advisory committee established by the Board bear any liability with respect to any plan or individual account described in this subsection.

5. The provisions of this subsection shall not apply to any political subdivision of the Commonwealth that has entered into an agreement with the Retirement System pursuant to § 51.1-603.1 or 51.1-611 except with regard to a 403(b) plan.

6. Disclosure of all services, fees, restrictions, and surrender penalties associated with employee

voluntary contributions under subsection G shall be provided by the political subdivision of the Commonwealth on an annual basis to an employee who makes the election provided in subdivision G 1. Such employee shall also be provided with a side-by-side comparison of the long-term effects of generic expense ratios on his investments.

7. The Board shall not be responsible for administration of or recordkeeping related to voluntary contributions to the defined contribution component of the program made to a 403(b) plan or the corresponding employer matching contributions made to a 403(b) plan or the appropriate local cash match plan established under § 51.1-610 that are authorized by subdivision G 1.

8. The Board shall develop policies and procedures for administering the provisions of this subsection.

§ 51.1-610. Local cash match plans.

A. Any county, municipality, authority, or other political subdivision of the Commonwealth may by ordinance or resolution adopt and establish for itself and its employees a cash match plan. Any such cash match plan may include constitutional officers and their employees. The ordinance or resolution adopting or establishing such plan shall create or designate an appropriate board or officer to administer the plan, and shall confer upon such board or officer the authority to do all things by way of supervision, administration, and implementation of the plan, including the power to contract with private corporations or institutions for services in connection therewith.

B. If it deems it advisable, any county, municipality, authority, or other political subdivision of the Commonwealth, which by ordinance or resolution adopts and establishes for itself and its employees a cash match plan, may create a trust or other special fund for the segregation of the funds or assets resulting from contributions.

~~C. No amount shall be credited pursuant to any cash match plan created pursuant to this section on behalf of a qualified participant who is participating in the hybrid retirement program described in § 51.1-169 if the qualified participant has not contributed the maximum amount of voluntary contributions under subdivision C 2 of § 51.1-169.~~

2. That the provisions of this act shall become effective on January 1, 2016, except the provisions of subdivision G 2 of § 51.1-169 of the Code of Virginia, as created by this act, which shall become effective in due course.

Virginia Retirement System 2015 Fiscal Impact Statement

1. **Bill Number:** HB2178

House of Origin Introduced Substitute Engrossed
Second House In Committee Substitute Enrolled

2. **Patron:** Patron Prior to Substitute- Poindexter

3. **Committee:** Passed both Houses

4. **Title:** Hybrid retirement program; school division deferred compensation and cash match plans.

5. **Summary:** Allows school divisions the option of establishing and administering their own deferred compensation and cash match plans for the hybrid retirement program. Employees of such school divisions would have the option of participating in such programs. The bill has a delayed effective date of January 1, 2016.

6. **Budget Amendment Necessary:** Yes. VRS and its third-party record keeper will incur implementation costs of approximately \$440,000 related to this change in the hybrid retirement plan.

7. **Fiscal Impact Estimates:** Final; The VRS costs to implement the changes required by this bill are estimated at \$370,000, and include internal VRS system changes and testing to accommodate annual reporting of decentralized (local) hybrid contributions, as well as additional positions in the finance, employer reporting and defined contribution areas to collect contribution information from employers and to recalculate employer contributions and credit amounts related to the employer match. This amount also includes VRS' costs for revisions to plan documents. Employers that elect to administer employee voluntary contributions and corresponding matching employer contributions locally will have similar expenses for revising their plan documents. VRS' third-party record keeper's implementation costs of approximately \$70,000 include programming to track employers that elect to allow 403(b) contributions and to prevent members who elect a 403(b) provider from using ICMA-RC for voluntary contributions, changes to member communications, and testing, documentation and administration of changes. Ongoing VRS costs are estimated at approximately \$110,000 per year for the new positions.

8. **Fiscal Implications:** See Fiscal Impact Estimates above.

9. **Specific Agency or Political Subdivisions Affected:** VRS, participating school divisions that choose to administer their own 403(b) plans for purposes of the voluntary employer and employee contributions to the hybrid retirement plan, and hybrid employees of school divisions who elect to use local 403(b) plans for voluntary hybrid contributions.

10. Technical Amendment Necessary: No.

11. Other Comments:

Overview of Changes

This legislation authorizes the decentralization of voluntary employee and employer matching contributions under the defined contribution component of the hybrid retirement program that went into effect on January 1, 2014. Under the legislation, each local school division will determine on an annual basis whether their employees will be permitted to elect to contribute their voluntary Hybrid contributions (and the corresponding employer match) to a local 403(b) plan (or plans, as many school divisions have multiple 403(b) providers) or the VRS Hybrid 457 and VRS Hybrid 401(a) Cash Match plans. The initial decision by each school division must be made by November 1, 2015, with an effective date of January 1, 2016. Thereafter, school divisions will need to make or change their decision and notify VRS by November 1, beginning in 2016, as to whether their employees will be provided an election to participate in a local 403(b) plan or the VRS Hybrid 457 plan for voluntary hybrid contributions. Each eligible employee in a political subdivision that has elected to allow the use of a local 403(b) plan for voluntary Hybrid contributions must make an annual election, by November 30, to contribute his voluntary Hybrid contributions to one or more of the local 403(b) plans the employer offers or to the VRS Hybrid 457 and VRS Hybrid 401(a) Cash Match plans. An employee who does not change his annual election by November 30 of each year will be deemed not to have made a change from the prior year. Elections by either the local school division or employees made by November 1 or 30, respectively, will be effective January 1 of the following year.

Amounts currently invested in the VRS Hybrid 457 plan may not be transferred to 403(b) plans. This could result in multiple low balance accounts that could be adversely affected by fees.

This legislation also removes the requirement that a local employee must contribute the maximum amount of voluntary contributions to the hybrid retirement program before being eligible for a local cash match on supplementary contributions to a 403(b) or 457 account.

The enrolled bill deletes the provision that would have allowed loans and hardship distributions from the voluntary employee hybrid contributions and matching employer contributions made to local 403(b) accounts administered by a school division.

The enrolled bill also requires employers that allow their employees to use locally administered 403(b) accounts for voluntary hybrid contributions to provide those employees who elect to use the 403(b) accounts with a side-by-side comparison of the long-term effects of generic expense ratios on investments.

The bill also provides that school divisions and VRS, its officers, directors and employees, have no liability for contributions made to local 403(b) accounts. School divisions, as fiduciaries of the Hybrid funds contributed to 403(b) accounts, must select such funds under the standard of care set out in § 51.1-803.

As currently structured, the hybrid retirement plan requires that all participating localities use the VRS Hybrid 457 Deferred Compensation Plan and Hybrid 401(a) Cash Match Plan for all contributions—mandatory and voluntary—for the hybrid defined contribution component. The hybrid plan requires mandatory contributions from both employer and employee of 1%, and under this legislation these mandatory contributions will continue to be made to the Commonwealth’s Hybrid 401(a) cash match plan. As is the case under the current legislation, no loans or hardship distributions will be allowed from the mandatory employee and employer contributions made to the VRS Hybrid 401(a) Cash Match Plan. All political subdivisions, with the exception of school divisions, which will have an option under this legislation, will continue to use the VRS Hybrid 457 and the associated Hybrid 401(a) cash match plan for both mandatory and voluntary hybrid defined contribution amounts.

Under the hybrid retirement program, additional contributions may be made by the employee on a voluntary basis up to an additional 4%, with a matching component by the employer up to an additional 2.5%. As currently structured, all mandatory hybrid contributions, including the employer match to voluntary contributions, are made to the VRS Hybrid 401(a) Cash Match Plan. Under the current structure, only the employee voluntary contributions go into the VRS Hybrid 457 plan, which frees up as much of the 457 annual Internal Revenue Service (IRS) limit (currently \$18,000 for all employees, with additional amounts possible for those over 50 and those close to retirement) as possible for any supplemental contributions an employee may be eligible to make in addition to the hybrid contributions.

This legislation would provide that a school division has the option to use its own 403(b) plan(s) and 401(a) cash match plan for the voluntary employee and employer matching contributions to the Hybrid plan. If a school division does not establish a 401(a) cash match plan, then both the employer and the employee contributions will be made to the 403(b) plan and will count toward the IRS maximum annual contribution limit. School division employees will likely be required to pay additional administrative costs as well as different investment fees for these separate accounts, and will not be able to view their complete retirement benefits in a holistic manner in one location.

Forfeiture accounts

School divisions that choose to administer their own plans for purposes of this legislation may want to consider adding a 401(a) account for the employer contributions if they do not already have one. This will facilitate the school division’s administration of the forfeiture provisions of the hybrid retirement plan, which they will be required to oversee if they opt out of the VRS accounts. Employees who terminate employment prior to vesting in the employer contributions to the hybrid retirement plan (full vesting in the defined contribution component takes four years) forfeit a portion of those employer contributions and any earnings thereon. If the employer and employee contributions are commingled, this will create administrative complexity for the employer. Under the legislation, school divisions that elect to allow employees to use 403(b) accounts for voluntary contributions will need to establish a forfeiture account for those employees and specify the uses of the account. Additionally, consideration needs to be given to the forfeiture guidelines as an employee moves between different employers during the initial four-year vesting period as the

employee's total time in the hybrid plan, and not just service with a single employer, will need to be tracked. School divisions that allow their employees to use 403(b) accounts will need to work with VRS and their 403(b) provider(s) to ensure that all non-vested employer sources are forfeited when a forfeiture event occurs. For example, if a terminated employee takes a distribution from non-vested employer match funds with a 403(b) provider, non-vested employer mandatory funds should also be forfeited at the same time. Employees can end up with multiple employer match buckets as they move between employers before being fully vested. Vesting is based on total creditable service at the time of distribution, not service with an individual employer.

Auto-escalation

In order to encourage employees to contribute the maximum voluntary amount, the hybrid retirement program includes an auto-escalation feature that automatically increases the voluntary contributions by 0.50% every three years until the employee is contributing the maximum amount of voluntary contributions. The auto-escalation requirements of the hybrid retirement plan will be much easier for the school divisions that allow their employees to use 403(b) plans to administer if the employer and employee contributions are segregated, as the auto-escalation provisions will require these school divisions to determine the percentage of voluntary contributions of each employee to administer the auto escalation schedule every three years.

Plan documents

School divisions that allow their employees to use 403(b) plans will need to ensure that the plan documents for their local plans (403(b) and 401(a)) are revised to include the additional provisions of the hybrid retirement plan, such as the schedule for employer matching contributions and the vesting schedule, forfeiture accounts, as well as auto escalation of employee voluntary contributions every three years. Additionally, due to the relationship between the blended employer rate and the employer match, which may vary, employers will need to ensure that their plan documents consider VRS business rules related to when Hybrid participation and contributions should start and stop, as well as the definition of "creditable compensation," which all Hybrid contributions are based on. This will be especially important for employees that choose to move into and out of the Commonwealth's Hybrid 457 plan.

IRS Annual Account Limits

Opt-out school divisions or their record keepers will also need to monitor IRS annual account contribution limits for 403(b) accounts to ensure that those limits are not exceeded, as VRS will not have access to the information necessary to do this. School divisions will also be required to monitor the IRC Section 401(a)(17) annual compensation limit and the IRC Section 415 annual contribution limit. School divisions that opt out will need to be able to correct errors in the voluntary contributions and the related employer match to ensure compliance with IRS requirements related to errors in contributions. Employers may also be subject to liability for failure to comply with those requirements.

Election Periods

This bill provides both the employer and the employee the option to elect to use a local 403(b) plan or plans in addition to the VRS Hybrid 457 plan for voluntary hybrid contributions and the associated employer match. However, an employee of a school division that has not elected to allow the use of local 403(b) plans cannot elect to use a 403(b) plan in lieu of the VRS Hybrid 457 and 401(a) plans. On an annual basis, each school division will have the opportunity to elect to give its employees the option to direct hybrid voluntary contributions to local 403(b) plans. The initial election period at the employer level will expire on November 1, 2015. Each year thereafter, the bill provides that a decision must be made by each school division by November 1, to become effective the subsequent January 1.

A school division's election to permit its employees to use local 403(b) plans for voluntary hybrid contributions does not automatically require every employee to contribute to a local 403(b). If a school division makes the election to allow a 403(b) option, each employee will have the opportunity to decide whether to remain with VRS for their voluntary contributions and employer match or to use a local 403(b) plan. These plans would be established separately from the VRS Hybrid 401(a) Cash match Plan, which will still be used for all mandatory contributions. This substitute bill incorporates an amendment for an annual employee election period. Each employee of a local school division that provides a 403(b) plan or plans will have the opportunity to choose whether to use the VRS Hybrid 457 plan, or a local 403(b) account for voluntary hybrid contributions. The initial employee election period will expire on November 30, 2015.

Each year thereafter, the bill provides that each employee of a local school division that offers a 403(b) plan or plans must make an election by November 30, to become effective the subsequent January 1, to direct their contributions to the VRS Hybrid 457 Plan, or to the school division's 403(b) plan(s). The bill also provides that if no change is made, the employee continues in the plan elected for the previous year.

Reporting and Contributions

Because VRS will not have access to voluntary hybrid contribution information for school divisions that decide to administer the voluntary contributions locally, it will not be possible for VRS to provide members in school divisions that elect to allow employees to use local 403(b) plans for hybrid voluntary contributions with consolidated information about their retirement benefits. For state employees, judges and political subdivisions other than school divisions that elect to offer a 403(b) option, the employee will have access to a member benefit profile that consolidates all VRS-administered benefits to provide the member with a complete snapshot of his or her retirement benefit. For school divisions that elect to allow a 403(b) option, the members who choose to use a local 403(b) account for voluntary hybrid contributions will not have access to a consolidated view of his or her primary retirement benefit. In addition, for counseling purposes, VRS will not be in a position to provide information concerning the locally administered portion of the benefit. As school district employees that choose to utilize the 403(b) option move between employers, they will likely end up with multiple accounts over various providers, which may make this process more difficult.

VRS anticipates that school divisions that choose to offer 403(b) options to their employees in addition to the VRS Hybrid 457 plan will need to report to VRS annually and potentially more often on the amount of voluntary contributions and the employer match on those contributions. This is necessary because the employer contribution rate is a blended rate, based on the defined benefit actuarially determined rate, and incorporates an estimate of the employer match for hybrid employees. For employers that use only VRS accounts, there is a monthly accounting for the employer match on the employee's voluntary contributions and the billing for the defined benefit component of the hybrid plan is reduced accordingly. For employers that elect to offer a 403(b) option, VRS will use the annual employer report of the employer matching contributions on the employee's voluntary contributions (or a similar method) and provide the school division an adjustment for that amount against future VRS contributions. This will allow school divisions that elect to offer a 403(b) option to have the same contribution allocation result as employers who remain with the VRS administered plan, although not on a monthly basis.

Transferring Hybrid Funds

It will not be easy for a member who elects to make Hybrid voluntary contributions to a 403(b) plan pursuant to this bill to consolidate funds already deposited into his or her Hybrid 457 Deferred Compensation account, where Hybrid voluntary contributions are currently deposited. Additionally, plan to plan transfers between 457 plans and 403(b) plans are not permissible, as the rules governing each respective type of account are slightly different. A member would have to meet break in service requirements prior to being eligible to take a distribution from the VRS Hybrid 457 Plan.

Provisions of the Hybrid that are Unchanged

The mandatory employee and employer contributions to the defined benefit component of the hybrid plan would not be affected by this legislation. This legislation would also not change any of the provisions related to state employees and judges participating in the hybrid. No loans or hardship distributions will be available for state employees, judges, or employees of political subdivisions in the hybrid retirement plan. SPORS, VaLORS, and local hazardous duty employees with enhanced benefits are not eligible to participate in the hybrid.

Delayed Effective Date

This bill contains an enactment clause with a delayed effective date of January 1, 2016. This additional time will allow for system modifications and testing. Further, it will give VRS time to provide educational materials to school divisions that wish to allow employees to use local 403(b) plans. School divisions that make this election will need to make themselves familiar with information on the rules of the Hybrid plan, including how to manage the forfeiture of unvested employer contributions, and how to monitor IRS annual limits, auto-escalation requirements, the separation of employee and employer contributions, and maintaining coordination with other aspects of the Hybrid plan.

This bill, as amended by the Senate Finance Committee, is identical to SB 1162, as amended.

Date: 2-27-2015

Document: HB2178ER.DOC

Sample Language for Employee Election Form

Note to Employers: If you elect to offer Hybrid Retirement Plan employees the opportunity to direct voluntary contributions and associated employer match to a 403(b) retirement plan and/or cash match plan that you sponsor, employees must elect between November 1 and November 30 if they wish to use the plan provided by the school division. You are encouraged to use the language included below in any election form you create for this purpose of tracking employee elections. Employee election forms will not be collected by VRS and are for the employer's purposes only.

Employee Election Form: By making this election, future voluntary hybrid contributions will be made to the employer-sponsored 403(b) plan and not to the plan administered by the Virginia Retirement System. If you want to participate in the school division plan, complete this form and give it to your human resource office between November 1 and November 30. If you take no action, you will continue to make voluntary hybrid contributions to the VRS-administered plan. The election becomes effective January 1, _____. You have an opportunity to change your election annually between November 1 and November 30 of each year.

<p>1. Employee Name (First, Middle Initial, Last)</p>
<p>2. Employee Statement</p> <p>I elect to direct my Hybrid Retirement Plan voluntary contributions to a 403(b) retirement plan established by my school division, rather than the plan administered by the Virginia Retirement System. I understand that this election means that the associated employer matching contributions will be made to the same 403(b) retirement plan or local cash match plan established by the school division.</p> <p>By making this election, I understand that:</p> <ul style="list-style-type: none">• The election cannot be changed until the election window, between November 1 and November 30 the following year.• My voluntary contributions in the Hybrid Retirement Plan and associated employer matching contributions will be directed to the school division plan and not to the plan administered by VRS or its third-party administrator, and that I will be responsible for any related fees.• Mandatory contributions will continue to be deposited in the VRS Hybrid 401(a) Cash Match Plan and that I will be responsible for associated fees.• The school division bears full responsibility for plans it administers and is the fiduciary of these plans. VRS has no responsibility for plans administered by the school division.• I have reviewed the plan information provided and carefully considered the decision to use the plan(s) administered by the school division.• VRS will provide me retirement counseling and benefit information only for plans it administers and cannot provide me counseling on contributions made to the school division plan or elsewhere.• The rules governing distributions and transfers of funds may vary among the different types of retirement plans. <p>_____</p> <p>Employee Signature</p> <p>_____</p> <p>Date</p>

Please contact the human resource office for details.