

CLEVELAND PUBLIC LIBRARY

Human Resources Committee Report

June 18, 2009

**Resolutions Relating to the Cleveland Public Library
Section 403(b) Tax-Sheltered Annuity Plans**

WHEREAS, the Library currently maintains two plans for employees under Internal Revenue Code Section 403(b) (the "403(b) Plans"); and

WHEREAS, due to the implementation of more stringent Treasury regulations, and, on advice of outside employee benefits counsel, based upon the discovery that the Library is no longer eligible to continue contributions to any 403(b) Plans, it is necessary for the Library to close the 403(b) Plans to new contributions; and

WHEREAS, in order to preserve the tax deferrals under the 403(b) Plans while providing appropriate advanced notice to employees of these changes, the Library will close the 403(b) Plans as of August 31, 2009 and take steps to conform the 403(b) Plans to meet the Treasury regulation requirements and other applicable tax requirements; and

WHEREAS, in order to reduce the administrative burdens and exposures associated with the 403(b) Plans, the Library hereby amends the 403(b) Plans to prohibit new loans after August 31, 2009 and terminates the 403(b) Plans effective in 2011; and

THEREFORE, BE IT RESOLVED by the Board of Trustees of the Cleveland Public Library as follows:

RESOLVED, the current 403(b) Plans will be frozen to new contributions as of August 31, 2009;

RESOLVED, loans under the 403(b) Plans shall be prohibited after August 31, 2009;

RESOLVED, THE 403(B) Plans will be terminated during 2011, with an effective date no later than December 31, 2011.

RESOLVED, the Library Director is hereby authorized to work with outside employee benefits counsel to take all steps necessary to preserve the tax deferrals under the 403(b) Plans and **THEREFORE BE IT;**

FURTHER RESOLVED, that the appropriate officers of the Library be, and each of them hereby is, authorized and empowered in the name and on behalf of the Library to take or cause to be taken any and all such further actions, to execute and deliver or cause to be executed and delivered all documents, instruments and agreements, and to make such filings, in the name and on behalf of the Library, to incur and pay all such fees and expenses and to engage such advisors as they shall in their judgment determine to be necessary, desirable or advisable to carry out fully the intent and purposes of the foregoing resolutions and the execution by such officers of any such document, instrument or agreement or the payment of any such expenses or the doing by them of any act in connection with the foregoing matters shall conclusively establish their authority therefore and the approval of the documents, instruments or agreements so executed, the expenses so paid, the filings so made and the actions so taken.

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Background and Strategies Regarding 403(b) Plan

- **Background.**
 - CPL currently offers three 403(b) retirement savings arrangements (salary deferral and accumulated leave) through two vendors: ING and Isquick Annuities. IRS Regulations becoming effective in 2009 impose new requirements on, and require a complete overhaul of, all 403(b) arrangements. As a result, Isquick Annuities has permanently frozen its arrangements to new contributions.
 - In the course of reviewing the CPL 403(b) arrangements, it was determined that, at some point in the past, CPL ceased being eligible to sponsor any on-going 403(b) arrangements. The IRS offers a program to fix this problem through its Voluntary Correction Program (requiring a filing with the IRS, the freezing of the arrangements to new contributions and the payment of an \$8,000 compliance fee).
 - The frozen 403(b) arrangements must be updated to comply with the new IRS Regulations, even if they are terminated at some point in the future.
 - The complexity of the new regulations imposes new burdens on CPL for regulatory compliance (requiring more administrative effort and creating opportunities for greater liability exposure).
 - CPL also offers tax-deferred voluntary retirement savings through a 457 plan maintained under the Ohio Public Employees Deferred Compensation Plan. A 457 plan can be used as a substitute retirement saving vehicle, but the maximum amounts that may be contributed are somewhat lower than under the combination of 403(b) and 457 arrangements.
- **Required Steps.**
 - The 403(b) arrangements must be frozen and submitted to the IRS under its correction program.
 - The 403(b) arrangement must be updated to reflect the new Regulations.
- **Strategies and Other Considerations.**
 - Due to the expanded regulatory obligations and exposure to potential liability, it appears to be in the best interest of CPL to terminate the 403(b) arrangements at some point in time.
 - However, immediate termination could cause some disruption to certain employees and retirees because:

- Participant loans (apparently by ten individuals) are outstanding under the ING annuities which would need to be repaid to avoid tax consequences;
 - Certain investments under the existing arrangements contain early surrender charges which, through further investigation and structuring, could be avoidable;
 - An additional tax on distributions prior to age 59-1/2 can likely be avoided through further structuring; and
 - A delay in the termination would afford individuals eligible (or nearly eligible) for early retirement the opportunity to retire and take advantage of the higher limits that exist under the combined 403(b) and 457 arrangements.
- In part, minimizing or reducing these disruptive effects would likely involve the use of a “fully supported” ING 457 plan (to supplement the existing plan) which will not be available until later in 2009 or early in 2010.

- **Current Recommendations.**

- It is recommended that the Board freezes the existing 403(b) arrangements to new contributions and authorizes the necessary updating of these arrangements as well as the taking of corrective steps under the IRS VCP filing (see the attached proposed Resolutions). The freeze date of August 31, 2009 is proposed to allow the employees eligible for, or soon to be eligible for, early retirement to make use of the higher deferral limits if they choose to retire within this timeframe. The Resolutions also prohibit new loans after the freeze date. Employees, retirees and the unions would be informed of these steps in the manner set forth in the attached Notices.
- At some point in the near future (preferably not later than December 31, 2011), management recommends 403(b) arrangements be terminated altogether. The proposed Resolutions call for the termination, effective not later than December 31, 2011. Between now and this future date, CPL will work with its vendors to reduce the disruptions mentioned above.

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Notice to All Active Employees Regarding Change in Retirement Arrangements

For many years, CPL employees have been permitted to make tax-deferred retirement contributions under tax-sheltered annuities created under Section 403(b) of the Internal Revenue Code ("IRC"). Also, since 2005, CPL has made accumulated vacation and sick leave contributions (for employees retiring) under its Accumulated Leave Plan, also a tax-sheltered annuity arrangement governed by IRC Section 403(b).

In 2007, the IRS issued a comprehensive set of new regulations on Section 403(b) plans, dramatically changing the level of the employer involvement required under these plans. Among other things, these new regulations, which became effective this year, require employers to become deeply involved in the personal affairs of the employees as they relate distributions, loans and hardship withdrawals under the employee 403(b) accounts. In addition, an employer sponsoring a 403(b) plan is now required to take additional steps to operationally comply with and document the tax requirements associated with the 403(b) accounts. In the process of updating CPL 403(b) plans to bring them into compliance with the new rules, it was also discovered that, while CPL may have been in the past eligible to sponsor a 403(b) plan, it is no longer eligible to be a 403(b) sponsor. Under the IRS rules, this means that the library must take steps to close the CPL 403(b) plans to new contributions.

Accordingly, this means that no new contributions (both voluntary deferrals and accumulated leave contributions) will be permitted under these plans after August 31, 2009. Also, no loans will be permitted under the CPL 403(b) plans after August 31, 2009. One or more 457 deferred compensation plans will be the going forward vehicle for contributions, commencing September 1, 2009. Finally, the CPL 403(b) plans will be terminated at a future date (currently expected to be in 2011).

For the time being, however, the amounts you may have accumulated under the existing 403(b) arrangements will continue to be held, invested (subject to your direction) and distributed in the same manner as is currently the case. When CPL terminates the 403(b) arrangements, you will be advised of the distribution options and option for rolling the amount over into an individual retirement account or other tax-deferred vehicle.

Notice to 403(b) Participants who have Separated from Service

[Same notice as above]

Notice to Union Regarding 403(b) Changes and New 457 Plan

As indicated in the attached Notices, CPL has been advised that it must suspend contributions to its existing 403(b) tax-sheltered annuity arrangements. CPL intends to implement this suspension at the end of August. Also, no new loans may be made from the 403(b) arrangements after August. Finally, the 403(b) arrangements will be terminated at some point in the future (currently expected to be during 2011).

In place of these arrangements, deferral opportunities will be available under one or more CPL sponsored tax-deferred compensation plans governed by Internal Revenue Code section 457.

In the near future, CPL will provide the Union with further details on the 457 deferral opportunities and the steps it plans to take to transition from the existing 403(b) arrangements to the 457 approach.