

Ottosen Britz Kelly Cooper & Gilbert, Ltd.

# Legal Insights

Vol. 15, No. 1

for School Districts

Winter 2008

## **New 403(b) regulations create greater responsibility for school districts**

**by David Zafiratos**

On July 26, 2007, the IRS issued the first new regulations covering 403(b) tax-sheltered annuities in over four decades. Since the last time the IRS published 403(b) regulations, numerous changes have occurred through case law and IRS policy that had yet to be officially recognized by Treasury Department regulations. These new regulations mark an official recognition of some existing IRS positions and also create new requirements in the area of 403(b) plans. A key theme of the new regulations is an increased role for school districts in administering 403(b) plans. As the regulations take effect it will become important for school districts to understand the part they must play in the world of 403(b) tax-sheltered annuities.

### **Effective dates**

The regulations generally take effect in an employee's taxable year beginning after December 31, 2008. As most individual's tax year begins January 1, most of the regulations' requirements take effect on January 1, 2009. The regulations also contain the following exceptions to that general effective date:

- For school districts with 403(b) plans provided according to a collective bargaining agreement in effect on July 26, 2007, the regulations will take effect upon the termination of that collective bargaining agreement, including any extensions, or July 26, 2010, whichever date is earlier.
- Under the regulations, school districts may not prevent any of their full time employees from taking elective deferrals under salary reduction agreements. However, if 403(b) plans in place on July 26, 2007 exclude cer-

*Continued on page 2*

## **School employee dismissals: A Primer**

**by Maureen Anichini Lemon**

As your school board considers its staffing needs for the 2008-2009 school year, it must soon decide whether to release any employees prior to the end of the current school year. In general, non-tenured teachers must be notified of a dismissal at least 45 days before the last day of the current school term. Notice of a reduction in force of teachers must occur at least 60 days before the last day of the school term. Educational support personnel employees, by contrast, must receive notice of a reduction in force at least 30 days before they are dismissed. This article fully describes the statutory requirements pertaining to each type of dismissal.

### **Full time teachers completing fourth consecutive year of service**

Any teacher first employed on a full time basis on or after January 1, 1998, must complete a probationary period of four consecutive school terms to attain tenure. Those teachers who will not attain tenure must receive written notice of dismissal stating the specific reason for the dismissal, by certified mail, return receipt requested, at least 45 days before the end of this school term. Failure by the school board to fully comply with this requirement will result in the attainment of tenure by teachers completing the last year of their probationary period.

### **Full time teachers not completing the last year of the probationary period**

Any full-time teacher who is not completing the last year of the probationary period must also receive written notice from the school board at least 45 days before the end of the school term whether or not he or she will be re-employed for the following school term. The written notice of non-renewal to such employees does not need to include a reason for the non-renewal. If the school board does not give timely notice the non-tenured teachers will be deemed reemployed, and the school board must issue a regular contract to them for the following school year.

### **Reduction in force (RIF)**

If the school board decides to decrease the number of teachers employed by it or to discontinue some particular type of teaching service, the school board must follow the RIF requirements contained in Section 24-12 of the School Code. The school board must first remove or dismiss all non-tenured teachers before removing or dismissing any tenured teacher who is legally qualified to

*Continued on page 2*

## **New 403(b) regulations**

*Continued from page 1*

tain categories of employees from taking elective deferrals, that plan will still satisfy the regulations until the taxable year beginning on or after January 1, 2010.

- While the regulations place greater restrictions on in-service distributions, those new restrictions will not apply to annuity contracts issued before January 1, 2009.
- The regulations prohibit 403(b) annuities from including incidental life insurance contracts. This rule does not apply to annuity contracts issued before September 24, 2007.
- Regulations that place further restrictions on annuity plan-to-plan transfers do not apply to such transfers that were made before September 24, 2007.

### ***Written plan required***

Once the regulations take effect, school districts will need to play a greater role in administering employees' 403(b) tax-sheltered annuities. School districts must be aware of the regulations' requirement to establish a written 403(b) plan. Each school district's written 403(b) plan must satisfy the new regulations and 403(b) plan requirements in both form and operation. Written plans must contain "all the material terms and conditions for eligibility, benefits, applicable limitations, the contracts available under the plan, and the time and form under which benefits distributions would be made." (26 C.F.R. 1.403(b)-3(b)(3)) In addition to those required items, each school district's plan may include various optional features, including information regarding transfers and exchanges of annuity contracts.

The IRS recently issued Revenue Procedure 2007-71, which includes model language that should prove useful in formulating these written plans. This information can be found at <http://www.irs.gov/pub/irs-drop/rp-07-71.pdf>. According to a November 30, 2007 alert provided by the IRS, school districts that adopt the model language as their written plan will be in compliance with the regulations. School districts should, however, be wary of simply

*Continued on page 3*

## **School employee dismissals**

*Continued from page 1*

hold a position currently held by a non-tenured teacher. Among tenured teachers, the teacher(s) with the shorter length of continuing service with the school district shall be dismissed first, unless an alternative method of determining the sequence of dismissal is set forth in a collective bargaining agreement.

Tenured teachers dismissed pursuant to a RIF must receive written notice by regular mail and either by certified mail, return receipt requested or personal delivery, at least 60 days before the end of the school term. Included with the notice must be a statement of honorable dismissal and the reason for the dismissal. All teachers dismissed as a result of a RIF must be paid all earned compensation on or before the third business day following the last day of pupil attendance in the regular school term.

### ***Post-RIF vacancies***

Each year, the school board shall, in consultation with the teachers' union, establish a list categorized by position, showing the length of continuing service of each teacher who is qualified to hold such positions. Copies of this list should be distributed to the teacher's union on or before February 1 of each year. The school board should refer to this list when vacancies arise after a RIF.

If the school board has any vacancies for the following school term or within one calendar year from the beginning of the following school term (i.e. through August 24<sup>th</sup>, 2009), the vacant positions shall be offered to the RIF'd teacher(s) by seniority as far as they are legally qualified to hold such positions. If the number of honorable dismissals based on economic necessity exceeds 15% of the number of full-time equivalent positions filled by certified employees (excluding principals and other administrators) during the preceding school year, then the school board must offer to the qualified RIF'd teachers any vacant position for the following school term or within two calendar years from the beginning of the following school term (i.e., through August 23, 2010).

Whenever the number of honorable dismissals based upon economic necessity exceeds five or 150% of the average number of teachers honorably discharged in the preceding three years, whichever is more, then the school board must hold a public hearing on the question of the dismissals. A majority of the full board (four members) must vote in favor of the reduction following the hearing and board review.

### ***Educational support personnel***

A school board has a longer period of time to decide its educational support staffing needs. If an educational support personnel employee is dismissed as a result of a school board decision to decrease the number of educational support personnel employees or to discontinue some particular type of educational support service, the board must give written notice to the employee, received at least 30 days before the employee is removed or dismissed.

*Continued on page 3*

## School employee dismissals

*Continued from page 2*

The exception to this rule occurs when the employer is going to sub-contract the work previously performed by the educational support personnel. The sub-contracting scenario warrants a 90 day written notice and is subject to onerous requirements enacted into law in August, 2007.

In the non sub-contracting scenario, the notice must be sent by mail and either by certified mail return receipt requested or by personal delivery. A statement of honorable dismissal and the reason for the dismissal shall accompany the notice. Such a dismissal can occur at any time with at least 30 days notice; it is not tied to the last day of the school term as is a teacher RIF. The employee with the least seniority within a particular category of position shall be dismissed first unless a collective bargaining agreement establishes an alternative method of determining the sequence of dismissal. RIF'd educational support personnel employees shall be offered any vacancies within the category of position from which they were dismissed by seniority and so far as they are qualified to hold such positions, for the following school term or within one calendar year from the beginning of the following school term (i.e. through August 24, 2009).

As with teachers, the school board shall, in consultation with any exclusive employee representative or bargaining agent, establish an annual list, categorized by position, showing the length of continuing service of each full time educational support personnel who is qualified to hold such positions. Copies of this list shall be distributed to the exclusive employee representative bargaining agent on or before February 1 of each year. All RIF'd educational support personnel employees shall be paid all their earned compensation on or before the third business day following their last day of employment.

### Conclusion

Your school board must count back 60 days and 45 days from the last day of the school term to ensure that teachers receive RIF and/or dismissal notices in a timely manner. Likewise, the school board must count back 30 days from the date of an educational support personnel employee's desired termination date to ensure that the employee receives timely notice of the dismissal. For further information, please contact Maureen Anichini Lemon at (630) 682-0085 or [mlemon@obkcg.com](mailto:mlemon@obkcg.com). ■

### Attorney Notes

- **OBKC&G, Ltd.** is pleased to announce that **Joseph Miller III** has become a partner with the firm. Joe joined the firm in November 2000 and has focused his practice in municipal and education law. He graduated from the University of Illinois in 1991 with a bachelor's degree in Speech Communication and English. He attended Washington University School of Law and received his J.D. in 1994. Joe practices in our Naperville office.

*Continued on page 4*

## New 403(b) regulations

*Continued from page 2*

using the IRS's model written plan without knowing what the provisions of the model plan entail. It is essential that administrators of a school district's 403(b) plan fully understand its written content and how it affects the district and its employees.

### Transfers and exchanges

In addition, the new regulations restrict in-plan exchanges and plan-to-plan transfers of annuity contracts. Previously, Revenue Ruling 90-94 allowed the transfer and exchange of annuities without employer involvement. Now, employees may only exchange one annuity contract for another if certain conditions are satisfied. The same is true for employees wishing to transfer from a contract offered under one employer's plan to a contract offered under another employer's plan.

If seeking to exchange one annuity contract for another within the same employer's 403(b) plan, the following requirements must be met:

- The written plan must permit such transfers.
- The benefits of the new annuity contract must not be diminished compared to those of the old contract.
- The distribution restrictions of the new contract must be at least as strict as those of the old contract.
- The employer and contract provider must enter into an information sharing agreement.

If seeking to transfer from a contract offered under one employer's plan to a contract offered under another employer's plan, the following requirements must be met:

- The participant must be an employee or former employee of the school district for the receiving plan;
- Both the transferring and receiving plans must permit such transfers;
- The benefits of the new annuity contract must not be diminished compared to those of the old contract; and

*Continued on page 4*

## New 403(b) regulations

Continued from page 3

- The distribution restrictions of the new contract must be at least as strict as those of the old contract.

### Practical considerations

The employer involvement necessary for administering 403(b) tax-sheltered annuities is a significant responsibility. In addition to the new rules on written plans and contract exchanges discussed in this article, the regulations affect catch-up contribution limits, hardship distribution rules, the purchase of incidental life insurance, and other important aspects of 403(b) tax-sheltered annuities. Gaining familiarity with the regulations will be essential to understanding the new responsibilities facing school districts.

The IRS has allowed school districts until January 1, 2009 to comply with the new regulations. Nonetheless, it is critical that school district administrators consider the terms and conditions that will be included in their written 403(b) plans. They should also consider entering into information sharing agreements with current contract providers so employees can continue to complete contract exchanges. For further information, please contact David Zafiratos at (630) 682-0085 or [dzafiratos@obkcg.com](mailto:dzafiratos@obkcg.com). ■

### The firm's Wheaton office has moved to:

1804 North Naper Boulevard, Suite 350  
Naperville, Illinois 60563  
Phone: 630-682-0085 Fax: 630-682-0788

[www.obkcg.com](http://www.obkcg.com)

## Attorney notes

Continued from page 3

- The firm is also pleased to announce that **William R. Thomas** joined the firm as an associate in December 2007. Bill focuses his practice in a variety of areas including municipal law, real estate, eminent domain, family law, as well as wills and estate planning. He attended Valparaiso University School of Law and received his J.D. in 1991. Bill practices in our Elburn office.
- Effective December 2007, the firm welcomes **David T. Zafiratos** as an associate. David graduated from Northern Illinois University in 2004 with a bachelor's degree in Political Science and received his J.D. in 2007 from Chicago-Kent College of Law. His practice will focus on municipal law, with an emphasis on fire protection districts and school districts. David will practice in the firm's Naperville and Joliet offices.
- For the third consecutive year, *Illinois Super Lawyers* Magazine recognized **Karl Ottosen** as a 2008 Illinois Super Lawyer in the area of Government Law. *Law & Politics* conducts a rigorous review, research, and selection process of nominated attorneys. Only five percent of attorneys in Illinois are recognized as Super Lawyers by their peers for their outstanding professional achievement.
- Congratulations to **Shawn Flaherty** on being selected as a "Rising Star" in the areas of Government/City/Municipal Law in the 2008 issue of *Illinois Super Lawyers* Magazine. This designation is awarded to the top 2.5% of Illinois attorneys who are under the age of 40 or have been practicing ten years or less.
- This year, as in the past two years, **Karl Ottosen** was listed as a leading lawyer in the areas of Governmental, Municipal, Lobbying & Administrative Law in the Leading Lawyers Network section of *Chicago Lawyer* Magazine. Karl was recognized by his peers in a statewide survey to be among the top government-related attorneys in Illinois. ■

Ottosen Britz Kelly Cooper & Gilbert, Ltd.'s newsletter, *Legal Insights for School Districts*, is issued periodically to keep its clients and other interested parties informed of legal developments that may affect or otherwise be of interest to its readers. Due to the general nature of its contents, the comments herein do not constitute legal advice and should not be regarded as a substitute for detailed advice regarding a specific set of facts. Questions regarding any items should be directed to:

### OTTOSEN BRITZ KELLY COOPER & GILBERT, LTD.

1804 North Naper Boulevard, Suite 350  
Naperville, Illinois 60563  
(630) 682-0085 FAX (630) 682-0788  
Maureen Anichini Lemon, Editor  
[mlemon@obkcg.com](mailto:mlemon@obkcg.com)

Copyright 2008 by OTTOSEN BRITZ KELLY COOPER & GILBERT, LTD.

All rights reserved.

Pursuant to Rules 7.2-7.4 of the Illinois Rules of Professional Conduct, this publication may constitute advertising material.

