KLAUSNER KAUFMAN JENSEN & LEVINSON

A PARTNERSHIP OF PROFESSIONAL ASSOCIATIONS
ATTORNEYS AT LAW

May 13, 2016

VIA E-MAIL Pbrosamer@wpb.org
Patricia Brosamer
City of West Palm Beach City Hall
401 Clematis Street, 1st floor
West Palm Beach, FL 33401

Re: West Palm Beach Police Pension Fund
Accumulated Sick and Vacation Leave
Transfer
Our File No.: 150100

Dear Patricia:

Following up with you in regards to our last Board meeting on the topic of accumulated sick time and vacation leave transfers. There are no limits as to the accumulated sick and vacation transfer. See attached letter from Gary Robinson which details the tax opinion regarding these transfers with out limit.

If you have any questions, please do not hesitate to contact my office.

Sincerely yours,

Bonni S. Jensen

BSJ/dze
Encloseure
Chairman & Secretary
E-copy to Administrator

7080 NORTHWEST 4TH STREET, PLANTATION, FLORIDA 33317

PHONE: (954) 916-1202 • FAX: (954) 916-1232
www.robertdklausner.com

GRAY | ROBINSON
ATTORNEYS AT LAW

301 EAST PINE STREET
SUITE 1400
POST OFFICE BOX 3068 (32802-3068)
ORLANDO, FLORIDA 32801
TEL 407-843-8880
FAX 407-244-5690
gray-robinson.com

BOCA RATON
FORT LAUDERDALE
FORT MYERS
GAINESVILLE
JACKSONVILLE
KEY WEST
LAKELAND
MELBOURNE
MIAMI
NAPLES
ORLANDO
TALLAHASSEE
TAMPA

Richard E. Burke, Esq.
Chairman - Employee Benefits Practice Group
407-244-5603
RICK.BURKE@GRAY-ROBINSON.COM

April 12, 2016

Bonni S. Jensen
Klausner, Kaufman, Jensen & Levinson
7080 N.W. 4th Street
Plantation, Florida 33317

Re: West Palm Beach Police Pension Fund ("Plan")/Tax Advice
Client-Matter No. 211580-1

Dear Bonni:

You have requested advice as to whether the contributions of accumulated leave amounts to member DROP or Share Accounts in the Plan are subject to the limitations on "annual additions" set forth in IRC § 415(c). Based on administrative guidelines issued by the IRS National Office in December, 2014, we do not believe these contributions are subject to the IRC § 415(c) limits. Thus, we believe these amounts are added to other benefits provided by the Plan and are subject to the IRC § 415(b) limitations. However, it is possible the IRS could adopt future guidance altering these conclusions.

The Plan is a governmental defined benefit plan intended to satisfy the so-called "qualification" requirements of IRC § 401(a). Pursuant to the terms of the Plan, members otherwise eligible to receive cash payments of accumulated sick leave, accumulated vacation leave, or any other accumulated leave upon separation of employment shall have such leave transferred to the Pension Fund up to the amount permitted by law. These accumulated leave contributions will be transferred to a member's DROP Account or to his/her Share Account.

Under the Internal Revenue Code, defined benefit plans (like the Plan) are subject to the benefit limitations of IRC § 415(b) and defined contribution plans are subject to the annual contribution limits set forth in IRC § 415(c). Pursuant to IRC § 414(i), a defined contribution plan is a plan which provides for an individual account for each participant and for benefits based solely on the amount contributed to the participant's account, and any income, expenses, gains and losses and any forfeiture of accounts of other participants which may be allocated to such participant's account. Conversely, a defined benefit plan is defined as any plan which is not a defined contribution plan. See IRC § 414(j). With respect to retirement programs having elements of both types of plans, IRC § 414(k) provides that a defined benefit plan which provides a benefit derived from employer contributions which is based partly on the balance of the separate account of a participant shall, for purposes of IRC § 415, be treated as a defined contribution plan to the extent benefits are based on the separate account of a participant and as a defined benefit plan with respect to the remaining portion of benefits under the plan.

Arguably, the accumulated leave contribution provisions of the Plan could be viewed as a separate account within the defined benefit plan that is subject to the IRC § 415(c) limits because of the requirements of IRC § 414(k). However on December 8, 2014, the IRS National Office issued a memorandum ("Memorandum") that supports the opposite conclusion. In other words, based on the

analysis set forth in the Memorandum, the accumulated leave contributions under the Plan do not appear to be subject to the IRC § 415(c) limitations.

The Memorandum was issued to provide IRS Employee Plans personnel reviewing governmental defined benefit plans with DROP features guidelines for applying the benefit and contribution limits of IRC § 415 to such plans. The Memorandum describes a typical DROP arrangement (which would include the DROP program set forth in the Plan) and simply concludes that DROP benefit amounts[1] are not subject to IRC § 415(c) limits on "annual additions". However, the Memorandum also notes that many DROP arrangements permit other employee or employer contributions to be made to the DROP, which are in addition to the DROP benefit amounts. The Memorandum refers to these types of contributions as "Additional Contributions" and indicates that such contributions will only be treated as annual additions subject to the IRC § 415(c) limits in very limited situations.

According to the Memorandum, if a governmental defined benefit plan permits Additional Contributions to a DROP, the IRC § 415(c) limits will **only** apply to these contributions if **all** of the following three conditions are satisfied:

(1) The DROP consists of **"segregated accounts"** for each participant;

(2) Earnings on the amounts in the DROP are based **solely** on actual investment earnings (i.e., the DROP does not provide for a fixed or guaranteed rate of return on funds in the DROP); and

(3) The DROP does not provide for the cessation of the accrual of earnings in the DROP at any time.

Based on the terms of the Plan, the DROP and Share Accounts do not satisfy two of the above-referenced conditions (i.e., (1) and (2) above). First, the DROP and Share Accounts do not appear to be "segregated accounts". According to the Memorandum, a DROP only constitutes a segregated account if all DROP benefits payable to a participant are paid **only** from the assets in that participant's DROP account. Conversely, if a participant's DROP benefits are payable from the general assets of the trust fund (or from the assets of the DROP accounts of all DROP participants), the DROP accounts are not segregated accounts. Pursuant to the terms of the Plan, the DROP and Share Accounts do not appear to be segregated accounts because DROP benefits are payable from the general assets of the Pension Fund (because the DROP Accounts are commingled with Pension Fund assets) and benefits from the Share Accounts are payable from general Pension Fund assets (or from the assets of the Share Accounts of all Share participants, if the Pension Board dedicates a separate investment portfolio for Share Accounts).

In addition, the earnings on DROP and Share Accounts are not based **solely** on actual investment earnings (as defined in the Memorandum). According to the Memorandum, if a DROP participant has a choice between investment options **and one of those options provides for a fixed or guaranteed rate of return** (which for this purpose includes the rate of return on general trust fund assets), earnings are **not** based **solely** on actual investment earnings. Therefore, since at least one of the investment options

[1] DROP benefit amounts are the amounts credited to a participant's DROP account that he/she would have received if she/she actually retired.

available for DROP and Share Accounts under the Plan includes a fixed or guaranteed rate of return, earnings are not based **solely** on actual investment earnings.

As indicated above, according to the analysis set forth in the Memorandum, we believe that accumulated leave contributions to the DROP and Share Accounts are not subject to the annual additions limitation of IRC § 415(c) because the terms of the Plan that apply to both types of Accounts fail to satisfy two of the requirements contained in the Memorandum.[2] In this regard, we recognize that the language of the Memorandum refers to "Additional Contributions" made to **DROP accounts** and does not specifically address "Share accounts". However, we believe this is a distinction without substance and that the logic and conclusions enunciated in the Memorandum also apply to accumulated leave contributions to member Share Accounts. This is due to the fact that there is no substantive difference between the DROP and Share Accounts in the Plan. Both constitute separate benefit structures which provide supplemental benefits based on the value of such Accounts. In this sense they are the same type of account and we believe the IRC 415 limits should apply in the same manner to both Accounts.

Before closing, we would like to note that the contents of the Memorandum are not law and it specifically states that it is not subject to use, citation or reliance as such. However, notwithstanding this disclaimer, the Memorandum apparently represents the IRS National Office's current informal position on the issues referenced therein.

As indicated above, based on the terms of the Memorandum, we believe the accumulated leave contributions made to DROP and Share Accounts are not subject to the limitations on "annual additions" set forth in IRC 415(c). Thus, we believe these amounts are added to other benefits provided by the Plan and are subject to the IRC 415(b) limits. However, it is possible the IRS could issue future guidance altering these conclusions.

Very truly yours,

Richard E. Burke

Richard E. Burke, Esq.

REB/er

[2] Please note that the DROP Accounts actually fail all three of the requirements of the Memorandum because earnings on such Accounts cease to accrue if the applicable police officer fails to terminate employment by the end of the DROP participation period.