



**Medina  
City Schools**

Recognizing Potential—Maximizing Achievement

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To: All Employees

From: Wally Gordon, Treasurer

Date: November 18, 2008

Re: Tax-Sheltered Annuity Contributions

On January 1, 2009<sup>4</sup>, the IRS is changing some of the rules relating to “tax-sheltered annuities” (“TSA’s”). TSAs are designed to be tax-qualified under Section 403(b) of the federal tax law.

To comply with the new IRS rules, we are providing you with the attached Employee Summary. It is designed to help explain the tax law rules and School District rules that relate to TSAs. In that regard, the most important things you need to know are:

Please contact Terri Lattimer (330.636.3054) or Jill Young (330.636.3055) in the Treasurer’s office if you have questions.

**EMPLOYEE SUMMARY  
OF THE  
MEDINA CITY SCHOOL DISTRICT  
SECTION 403(B) PLAN**

As an employee of the Medina City School District, you are eligible to participate in the Medina City School District Section 403(b) Plan (the "Plan"). The Plan permits you to elect to defer a portion of your salary or wages on a pre-tax basis.

This summary provides an overview of the terms of the Plan. The Plan is being adopted by the School District on January 1, 2009 to comply with certain requirements of the federal income tax law (e.g., IRS Regulations).

Contact the Treasurer's office if you would like to defer compensation under the Plan, or if you have any questions about the Plan. The Treasurer's office also can provide you with a copy of the Plan document.

**In General**

The amounts that you elect to defer under the Plan are called "Elective Contributions". Your Elective Contributions are not currently subject to federal or state income taxes. Your Elective Contributions go into an annuity contract or custodial account contract that meets certain requirements of the federal income tax law - Section 403(b) of the Internal Revenue Code ("IRC").

The annuity contracts are provided by insurance companies and the custodial accounts are designed to invest in mutual funds. In this summary, those contracts are called "Plan Contracts", and the companies that offer them are called "Providers". Attached is the current list of all of the Providers who are permitted to offer Plan Contracts to eligible employees under the Plan. The Treasurer's office will periodically update the list. In the future, you can contact the Treasurer's office for an updated Provider list.

The remainder of this summary reviews the following points:

- Electing to Defer Compensation Under the Plan
- Salary Reduction Agreements
- Federal Tax Law Contribution Limits
- Plan Contracts
- Prior Contracts
- Distributions From Plan Contracts and Prior Contracts
- Transfers and Exchanges From Plan Contracts and Prior Contracts
- Selecting a Plan Contract
- Other Tax and Benefit Matters

### **Electing to Defer Compensation Under the Plan**

All employees of the School District are eligible to defer compensation under the Plan.

In general, to defer compensation under the Plan you have to:

- Sign a "Salary Reduction Agreement", and
- Establish a "Plan Contract" to receive your salary reduction contributions.

If you made salary reduction contributions to Providers prior to January 1, 2009, you may already have one or more annuity contracts or custodial accounts in place that are now "Plan Contracts" under this Plan. See the discussion of "Plan Contracts" below.

### **Salary Reduction Agreements**

A Salary Reduction Agreement will require you to specify an amount that is to be taken out of each paycheck and paid over to a Plan Contract. The amounts taken out of your pay are called "Elective Contributions" under the Plan.

The Treasurer's office can provide you with a Salary Reduction Agreement. Your Salary Reduction Agreement can be effective for any payroll date that is at least 15 days after you turn it into the Treasurer's office.

Unless you specify otherwise, deductions will be taken out of your regular payroll checks, and not out of special pays, like supplemental pay. Your Salary Reduction Agreement will stay in effect until you change it. You may change or end your Salary Reduction Agreement at any time. However, if you elect to receive a distribution from a Plan Contract on account of hardship, the tax law requires that for 6 months, you must be prohibited from making salary reduction contributions under the Plan or under any other deferred compensation plan of the School District.

If you have a Salary Reduction Agreement currently in effect, that Salary Reduction Agreement will not be continued on January 1, 2009. If you wish to continue making salary deferrals to a TSA on January 1, 2009, you will need to complete a new Salary Reduction Agreement that is provided by the Treasurer's office, and file it with the Treasurer's office by December 15, 2009.

### **Federal Tax Law Contribution Limits**

The federal income tax law limits the maximum amount that you can defer under this Plan in any calendar year.

In general, the calendar year limit is a specific dollar amount. The limit for 2008 is \$15,500.

Beginning in the calendar year that includes your 50<sup>th</sup> birthday, you are eligible to make additional salary reduction contributions ("Age 50 Contributions"). In 2008, the limit on Age 50 Contributions is \$5,000.

In future calendar years, the \$15,500 and \$5,000 limits may be increased because of inflation indexing. You will be advised if those limits do increase.

### **Plan Contracts**

Before you can defer compensation under the Plan, you will also have to establish a "Plan Contract" to receive your Salary Reduction Contributions. Your Salary Reduction Agreement will have to state which Plan Contract you will be using.

In general, in order for you to establish a Plan Contract, you will need to sign some type of legal documents with the Provider. This is something that you must do yourself. You will be the owner of the Plan Contract.

If you are making Salary Reduction Agreement contributions under this Plan as of December 31, 2008, your current annuity contract or custodial account contract will continue to qualify as a "Plan Contract" under the Plan on January 1, 2009 if it is on the attached Contract Provider list.

If your current contract continues as a "Plan Contract", you can elect in your new Salary Reduction Agreement to continue making your salary reduction contributions to that Contract. However, if your current contract does not qualify as a Plan Contract, you will have to select a different contract that is a Plan Contract to continue making Salary Reduction Agreement contributions on and after January 1, 2009.

### **Prior Contracts**

In addition, to comply with the federal tax law, you are also required to notify the Treasurer's office of any "Prior Contracts" you may have. A Prior Contract is a Section 403(b) annuity contract or custodial account that you made contributions to before January 1, 2009 as an employee of this School District, but are no longer contributing to.

To comply with the tax law, you also need to advise the Treasurer's office of any contract exchanges that you made before January 1, 2009 if you transferred your salary reduction contributions to another Section 403(b) contract. To comply with the federal tax law, the School District must enter into an "Information Sharing Agreement" with the Provider of a Prior Contract. Under the Information Sharing Agreement, the Provider will agree to only make distributions to you as is allowed under the federal tax law.

If the Provider of a Prior Contract will not enter into an Information Sharing Agreement with the School District, beginning January 1, 2009, you will not be permitted to make any additional salary reduction contributions under the Plan unless you either (a) transfer your interest under that Prior Contract to a "Plan Contract" or another Prior Contract where there is an

Information Sharing Agreement with the Provider, or (b) if you are permitted to do so under the tax law, receive a complete distribution under that Prior Contract.

### **Distributions From Plan Contracts and Prior Contracts**

To meet the requirements of the federal tax law, the Plan and the Plan Contracts and Prior Contracts are only permitted to allow you to receive a distribution in certain circumstances.

In general, the Plan will permit a Plan Contract or Prior Contract to make a distribution to you in the following circumstances:

- severance from employment with the School District
- attainment of age 59-1/2
- total and permanent disability
- death
- financial hardship

Upon death, payments will be made to your designated beneficiary. You must contact the Provider and use the Provider's designation of beneficiary forms to name a beneficiary.

You should review the terms of the Plan Contract or Prior Contract to determine if it allows for hardship distributions. If so, a distribution of your Elective Contributions is permitted if certain requirements of the federal income tax law are met. However, as a general matter, hardship distributions can be allowed to pay for uninsured medical expenses, college tuition, purchasing your own home, preventing eviction from or foreclosure on your home, funeral expenses and uninsured casualty losses to your home (e.g. by a tornado).

Applications for hardship distributions must be made directly with the Provider and will be determined solely by the Provider. If you do obtain a hardship withdrawal from a Plan Contract or Prior Contract, you will not be permitted to make Elective Contributions under this Plan for 6 months.

### **Loans From Plan Contracts and Prior Contracts**

You should review the terms of a Plan Contract or Prior Contract to determine if it allows for loans. If so, loan provisions in Plan Contracts and Prior Contracts also must meet certain requirements of the federal income tax law.

As a general matter, loans under all of your Plan Contracts and Prior Contracts may not exceed the lesser of (i) 50% of your interest in the Plan Contracts and Prior Contracts, or (ii) \$50,000 (including all outstanding loans under this Plan). Your interest rate on a loan will be a market rate of interest. Repayments will have to be made in five years, unless you are purchasing a residence. If you default on the loan, you will have to pay taxes, and possibly a 10% tax penalty, on the outstanding balance of the loan.

Applications for loans must be made directly with the Provider and will be determined solely by the Provider. When you apply for a loan, you will be required to tell the Provider if you have any outstanding loans under any other Plan Contracts or Prior Contracts; and the Providers are required to notify the Treasurer's office of any outstanding loans under Plan Contracts and Prior Contracts. However, you can ask the Treasurer's office to deduct the loan payments from your salary or wages.

### **Transfers and Exchanges From Plan Contracts and Prior Contracts**

You should review the terms of a Plan Contract or Prior Contract to determine if it allows for transfers or exchanges.

A Plan Contract or Prior Contract is also permitted to have terms that will allow you to transfer or exchange all or part of your interest in that contract to either (i) another contract that is Plan Contract under this Plan, or (ii) a Prior Contract, if the Provider has an Information Sharing Agreement with the School District.

In addition, in certain circumstances you also are allowed to transfer all or part of your interest in a Plan Contract or Prior Contract to purchase additional service credit under a state retirement system (e.g. STRS or SERS).

### **Selecting a Plan Contract**

The Treasurer's office has a list of all of the Providers that offer Plan Contracts, and contact information for the Providers.

Contact the Treasurer's office if you would like to use a Provider that is not on the approved list. In general, in order for a Provider to be made available under the Plan, at least five employees must make a request to use that Provider. In addition, before a Provider can be approved, the Provider will have to agree to follow the terms of the Plan and to provide other documentation to the Treasurer's office.

We encourage you to carefully review the prospectus and any other information that a Provider gives you to describe the terms of its Plan Contracts, especially the information regarding the investments that are available, and the charges and fees that apply under the Provider Contract.

Although the Provider Contracts must meet certain requirements of the federal tax law to be offered under the Plan, neither the Board, nor the Treasurer's office, nor the Plan Administrator has reviewed, or is responsible for reviewing, the investment options and charges and fees that are offered under the Plan Contracts. Selection of a Plan Contract from the approved Provider list is something that is completely up to you. Neither the Board, nor the Treasurer's office, nor the Plan Administrator is in any way recommending to you, or in any way responsible for, the investments and/or the charges and fees that apply under any Plan Contracts.

### Other Tax and Benefit Matters

Your Elective Contributions under the Plan are tax deferred for federal and state of Ohio income tax purposes. However, your Elective Contributions will remain subject to the federal Medicare tax (if that tax applies to you) and will also be subject to municipal income tax.

Your Elective Contributions will also continue to be considered as compensation for purposes of determining contributions to and benefits under the State Teachers Retirement System or School Employees Retirement System. Your Elective Contributions will also continue to be counted for other compensation and benefit purposes (e.g. calculation of your per diem rate of pay).

Any interest or earnings in the Plan Contracts and Prior Contracts is also tax deferred. You will pay federal income taxes when you actually receive payments from a Plan Contract. The Provider will issue a Form 1099 to report the payments. Whether you will pay state income taxes will depend on where you live at the time you receive a distribution.

Under the federal income tax law, there also is a 10% excise tax that is imposed on "early distributions" from Plan Contracts and Prior Contracts prior to age 59-1/2. There is an exception from the 10% penalty tax if your separation from service or retirement is in or after the calendar year that includes your 55<sup>th</sup> birthday. There are other exceptions from the 10% penalty tax that may apply, including (i) the distribution is being made after your death, (ii) you elect to receive distributions in substantially equal periodic payments over you life or life expectancy, (iii) the distribution is attributable to uninsured medical expenses, or (iv) the distribution is being made to an "alternate payee" pursuant to a domestic relations order (e.g., on account of divorce or child support order).

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Please contact the Treasurer's office if you would like to defer compensation under the Plan or if you have any questions about the Plan. The Treasurer's office can provide you with a list of the approved Providers under the Plan, a Salary Reduction Agreement, and a copy of the Plan document. Information regarding Plan Contracts must be obtained directly from the Plan Contract Provider.