

DATE: April 1, 1987

TO: Cruz Gonzalez, Risk Management Director via
Jack McGrory
FROM: City Attorney
SUBJECT: Supplemental Pension Savings Plans Withdrawal
Calculation Method

By memorandum dated March 16, 1987, you requested that this office review a recommendation by the Wyatt Company that The City of San Diego amend article VI, section 6.01 of both the Supplemental Pensions Savings Plan and the Supplemental Savings Plan M (Medicare) which describe the sequence of the withdrawal of funds from the Plans by employees. As you are aware, on October 6, 1986, the City Council adopted Resolution No. R-266724 to comply with the requirements imposed upon the Plans by the Internal Revenue Service (IRS) in their July 14, 1986 Determination Letter. That letter indicated, in part, that The City of San Diego could not permit employees to withdraw any employer contributions in either Plan or the Plans would lose their qualified status. After the City Council adopted Resolution No. R-266724, negotiations with employer organizations were undertaken and resulted in an agreement to support an amendment to the Plans which would allow withdrawal of employee mandatory contributions. That amendment was subsequently submitted to a vote of the active participants and was overwhelmingly approved. The new article VI, section 6.01 provided for the following order of withdrawal:

- (a) First, from principal amounts of all employee voluntary contributions;
- (b) Second, from earnings on employee voluntary contributions;
- (c) Third, from principal amounts of all employee mandatory contributions; and
- (d) Fourth, from earnings on employee mandatory contributions.

On January 12, 1987, the City Council authorized the City Manager to amend both SPSP Plans to implement the withdrawal sequence described above. It was generally believed at that time that the recommended withdrawal sequence was in compliance with the Tax Reform Act of 1986. PL 99-514. However, on January 26, 1987, the IRS published Internal Revenue Bulletin No. 1987-4 which provided initial guidance on the employee plan provisions of the Tax Reform Act of 1986. The City's tax consultant, the Wyatt Company, after consultation with their Washington, D.C.

office and representatives from the IRS, notified The City of San Diego that in order to maintain the qualified status of the Plans, the withdrawal sequence must be as follows:

- (a) First, from pre-1987 principal amounts of employee voluntary contributions;
- (b) Second, from pre-1987 principal amounts of employee mandatory contributions;
- (c) Third, from post-1986 principal and prorated interest amount of employee voluntary contributions;
- (d) Fourth, from post-1986 principal and prorated interest amount of employee mandatory contributions;
- (e) Fifth, from remaining interest earnings on employee voluntary contributions; and
- (f) Sixth, from remaining interest earnings on employee mandatory contributions.

Article XI, section 11.01 of both Plan Documents authorizes The City of San Diego to amend the Plan Documents at any time, without an election, in order to comply with federal or state laws necessary to maintain the qualified status of the Plans. We have reviewed Internal Revenue Bulletin No. 1987-4 and the applicable provisions of the Tax Reform Act of 1986 and believe that the withdrawal sequence recommended by both the IRS and the Wyatt Company is consistent with the provisions of the Act and the examples set forth in Internal Revenue Bulletin No. 1987-4. However, we must advise you that Internal Revenue Bulletin No. 1987-4 contains the usual IRS disclaimer that the guidance provided in the bulletin may only be used until further guidance is published. If new guidance is published and it is more restrictive than that contained in Internal Revenue Bulletin No. 1987-4, the IRS states that it will only apply it prospectively. No doubt the IRS will publish additional guidance sometime in the future; however, the City must comply with the current guidance or the IRS may challenge the qualified status of the Plans.

In summary, if The City of San Diego desires to maintain the current qualified status of the Plans, it is advisable to immediately adopt the recommended withdrawal sequence approved by the IRS. To do otherwise will put the qualified status of both Plans at risk.

JOHN W. WITT, City Attorney

By

John M. Kaheny

Deputy City Attorney

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