

IRS issues Annualization Pay Rules For School Employees

In general, most rules under Section 409A of the Code are already currently effective. However, there are special transition rules that apply with the school year that begins in 2008.

If the District(s) offers employees the opportunity to choose to be paid throughout the entire 12 month period or over the school year (i.e. typically 9 months), there is a potential problem with deferral elections that the employees may make for that school year.

Assuming a School Year starts on September 1 and ends on May 31 each year. There are only 4 months in the first calendar year and 5 months in the second calendar year of the School Year. If an employee chooses to be paid in 9 months instead of 12 months, he/she will be paid approximately 44% of his/her pay the first calendar year and 56% of his/her pay the second calendar year.

However, if the employee chooses to be paid over a 12 month period, he/she will be paid approximately 33% of his/her pay during the first calendar year of the School Year and 67% of his/her pay the second calendar year.

Section 409A of the Code governs the deferral of compensation. This "election" that the employees typically have with school districts is—by virtue of its being—an election to defer compensation over a longer period of time.

There is a special rule in the Section relating to this quandary. Generally, the rule states that in order to satisfy Code Section 409A, the following must be satisfied:

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- Employees must make a written election
- The election must be made before the school year starts
- The election must be irrevocable for 12 months
- The employees must state how they want the pay to be given to them (i.e. ratably over the 12 months beginning on the first day of the school year)
- The District must pay the salary, in full, before the last day of the 13th month following the first day the election is effective.

You have another unique marketing opportunity to showcase your knowledge of the industry by contacting your local districts to help with the compliance of these new rules. The following are steps that the Districts must take in order to comply with the new rules:

- Do nothing, but change policies so the District dictates when pay is made to employees (as a unit—not on an individual basis)
- Review current written policies to ensure that there is a process in place that complies with the new requirements
- Create written election forms describing the election policies in compliance with the new IRS Rules.



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