

OPINION NO. 91-005**Syllabus:**

1. Pursuant to R.C. 145.73, the Ohio Public Employees Deferred Compensation Board is authorized to promulgate and offer a program for deferral of compensation under any available federal statute, provided that the required approval of the Internal Revenue Service is obtained and the desired tax treatment is assured; the Board may act pursuant to 26 U.S.C. §457 or pursuant to any other available provisions.

2. The Ohio Public Employees Deferred Compensation Board is not precluded by R.C. 145.73 from offering employee benefit programs for which certain eligible employees are not qualified under federal law; the Board is, however, required to assure that the program for deferral of compensation as a whole provides each eligible employee with a reasonable number of options for which the employee is legally qualified.

3. Under current federal law, state and local governments are not eligible to adopt plans under 26 U.S.C. §401(k) and may not offer such plans unless they adopted them before May 6, 1986; thus, the Ohio Public Employees Deferred Compensation Board may not currently offer a program for the deferral of compensation under 26 U.S.C. §401(k) unless it adopted a plan under that provision before May 6, 1986.
4. The Ohio Public Employees Deferred Compensation Board may offer employee benefit programs under 26 U.S.C. §403(b), provided that the Board complies with federal law and that the appropriate approval of the Internal Revenue Service is obtained.
5. Under current federal law, the Ohio Public Employees Deferred Compensation Board may not offer a program for the deferral of compensation under 26 U.S.C. §407.

To: Richard J. Rehmer, Chairman, Ohio Public Employees Deferred Compensation Program, Columbus, Ohio
By: Anthony J. Celebrezze, Jr., Attorney General, January 11, 1991

I have before me your request for an opinion concerning the authority of the Ohio Public Employees Deferred Compensation Board to offer various types of employee benefit programs. R.C. 145.73 grants the Board the following authority:

(A) The Ohio public employees deferred compensation board shall initiate, plan, expedite, and, subject to an appropriate assurance of the approval of the internal revenue service, *promulgate and offer to all eligible employees*, and thereafter administer on behalf of all participating employees and continuing members, and alter as required, *a program for deferral of compensation*, including a reasonable number of options to the employee for the investment of deferred funds, including life insurance, annuities, variable annuities, regulated investment trusts, pooled investment funds managed by the board, or other forms of investment approved by the board, always in such form as will assure the desired tax treatment of such funds. (Emphasis added.)

Your letter asks the following questions:

- (1) Whether the Ohio Public Employees Deferred Compensation Program possesses the statutory authority to offer employee benefit programs under [the provisions of 26 U.S.C. 403(b), 401(k) and 407] as a "program of deferred compensation..." in accordance with R.C. 145.73; and
- (2) Whether all employee benefit programs offered by the Ohio Public Employees Deferred Compensation Program must, in accordance with R.C. 145.73(A), be equally available to all "eligible employees," or whether the Ohio Public Employees Deferred Compensation Program may offer employee benefit programs for which only certain eligible employees legally qualify.

Your first question asks about the authority of the Board to offer employee benefit programs under particular federal provisions – i.e., sections 403(b), 401(k) and 407. See 26 U.S.C. §§401(k), 403(b), 407 (1988). This question arises from the fact that another federal provision – section 457 – is addressed specifically to deferred compensation plans of state and local governments and tax-exempt organizations. See 26 U.S.C. §457 (1988). The Board has offered programs under section 457, and such programs clearly come within the language of R.C. 145.73(A). Your question is whether R.C. 145.73(A) encompasses programs under sections 401(k), 403(b), and 407, as well as programs under section 457.

R.C. 145.73(A) does not by its terms restrict its applicability to any particular type of deferred compensation program. Rather, the language of R.C. 145.73(A) indicates that, if the appropriate assurance of the approval of the Internal Revenue Service ("IRS") is obtained and if a reasonable number of options are provided, the Board may promulgate and offer to all eligible employees *any* program for deferral of compensation that is in such form as will assure the desired tax treatment of such funds. R.C. 145.73(A) grants the Board general authority to provide a program for deferral of compensation, subject to the condition that IRS approval be obtained and the desired tax treatment be assured; R.C. 145.73 does not specify that only certain federal statutes may be implemented. I conclude, accordingly, that the language of R.C. 145.73(A) does not preclude the Board from offering programs under federal provisions other than section 457, if all relevant requirements are satisfied.

The conclusion that the words "program for deferral of compensation," as used in R.C. 145.73(A), refer generally to programs under whatever federal statutes may permit such deferral is supported by the use of similar language in R.C. 145.73(E), as follows:

This section does not limit the authority of any municipal corporation, county, township, park district, conservancy district, sanitary district, health district, public library, county law library, public institution of higher education, or school district to provide separate authorized plans or programs for deferring compensation of their officers and employees in addition to the program for the deferral of compensation offered by the board. Any municipal corporation, public institution of higher education, or school district that offers such plans or programs shall include a reasonable number of options to its officers or employees for the investment of the deferred funds, including annuities, variable annuities, regulated investment trusts, or other forms of investment approved by the municipal corporation, institution of higher education, or school district, that will assure the desired tax treatment of the funds. (Emphasis added.)

This provision leaves open the possibility that certain public employers will provide plans or programs for deferring compensation of their officers or employees, in addition to the program offered by the Board. The language is general, including any plan or program that will assure the desired tax treatment of the funds, rather than being restricted to particular federal statutory provisions.

Similar broad usage of the term "deferred compensation" appears in R.C. 9.90. R.C. 9.90(A)(1) and (2) authorize the governing boards of public institutions of higher education and the boards of education of school districts to procure various benefits for their employees, including life insurance, annuity benefits, and other insurance coverage and benefits, and to "[m]ake payments to a custodial account for investment in regulated investment company stock for the purpose of providing retirement benefits as described in section 403(b)(7) of the Internal Revenue Code of 1954, as amended." R.C. 9.90 goes on to state:

Any income of an employee deferred under divisions (A)(1) and (2) of this section in a deferred compensation program eligible for favorable tax treatment under the Internal Revenue Code of 1954, as amended, shall continue to be included as regular compensation for the purpose of computing the contributions to and benefits from the retirement system of such employee. Any sum so deferred shall not be included in the computation of any federal and state income taxes withheld on behalf of any such employee.

It is, thus, clear that the General Assembly has used the term "deferred compensation program" generally, to include programs under section 403(b)(7) and other programs under which such benefits as annuities and life insurance are used for the deferral of compensation under federal tax law. It follows that the language used in R.C. 145.73(A) is not restricted to programs under section 457, but extends to other federal provisions that may be available to the Board.

I have, thus, concluded that the Board has statutory authority to offer employee benefit programs under provisions other than section 457, provided that the programs meet the criteria set forth in R.C. 145.73. You have inquired specifically about programs under sections 403(b), 401(k), and 407. See 26 U.S.C. §§403(b), 401(k), 407 (1988). I note that I am not able to opine authoritatively on matters of federal law, see, e.g., 1985 Op. Att'y Gen. No. 85-007, and, further, that R.C. 145.73 expressly requires that the Board obtain "an appropriate assurance of the approval of the internal revenue service." I shall, therefore, address these federal provisions only briefly to consider matters in the federal law that may affect the authority of the Board to act pursuant to the various provisions.

I consider, first, whether the Board has authority to offer employee benefit programs under section 401(k). Plans established under section 401(k) provide, in general, that employees may make an election between receiving current compensation and having a portion of their compensation contributed to a qualified profit-sharing or stock bonus plan, a pre-ERISA money purchase plan, or a rural cooperative plan. Section 401(k) plans are, thus, arrangements for the deferral of compensation. Current federal statutory provisions exclude state and local governments and tax-exempt organizations from the entities that may adopt plans under section 401(k). See 26 U.S.C. §401(k)(4)(B) (1988). The federal statute states expressly:

(B) State and local governments and tax-exempt organizations not eligible

A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement if it is part of a plan maintained by—

(i) a State or local government or political subdivision thereof, or any agency or instrumentality thereof, or

(ii) any organization exempt from tax under this subtitle.

This subparagraph shall not apply to a rural cooperative plan.

26 U.S.C. §401(k)(4)(B) (1988) (emphasis added). Thus, pursuant to existing federal law, governmental and tax-exempt entities are not eligible to adopt plans under section 401(k).

Provisions governing the effective date of section 401(k)(4)(B) appear in section 1116(f) of the Tax Reform Act of 1986, Pub. L. 99-514, 100 Stat. 2457 (1986), as amended by Pub. L. 100-647, title I, §1011(k)(8), (10), 102 Stat. 3470 (1988), as follows:

TRANSITION RULES FOR CERTAIN GOVERNMENTAL AND TAX-EXEMPT PLANS. — Subparagraph (B) of section 401(k)(4) of the Internal Revenue Code of 1986 (relating to governments and tax-exempt organizations not eligible for cash or deferred arrangements), as added by this section, shall not apply to any cash or deferred arrangement adopted by —

(i) a State or local government or political subdivision thereof, or any agency or instrumentality thereof, before May 6, 1986, or

(ii) a tax-exempt organization before July 2, 1986.

In the case of an arrangement described in clause (i), the amendments made by subsections (a), (b)(4), and (d) shall apply to years beginning after December 31, 1988. If clause (i) or (ii) applies to any arrangement adopted by a governmental unit, then any cash or deferred arrangement adopted by such unit on or after the date referred to in the applicable clause shall be treated as adopted before such date.

26 U.S.C. at 729 (1988) (note discussing effective date of 1986 amendments to §401). It thus appears that, prior to the Tax Reform Act of 1986, it was possible for a state or local government to adopt a plan under section 401(k). See 26 U.S.C. §401(k) (1982 & Supp. III 1985); [1990] 6 Stand. Fed. Tax Rep. (CCH) ¶12899M.017. It follows that a state or local government that adopted a section 401(k) plan before May 6, 1986, may continue to offer such a plan. A state or local government that

did not adopt a 401(k) plan before May 6, 1986, may not now adopt or offer such a plan.

It is clear that the Board is a governmental entity and, accordingly, that it may not offer a plan under section 401(k) unless it adopted that plan before May 6, 1986. The facts that you have presented do not indicate whether the Board adopted such a plan prior to May 6, 1986.

I turn now to the question whether the Board may offer employee benefit programs under section 403(b). As discussed above, the General Assembly has, in R.C. 9.90, indicated that a program under section 403(b) may be a program for the deferral of compensation. It follows that the Board may implement such a program under R.C. 145.73 if it is permitted to do so under federal law, and if such implementation is consistent with the Board's authority under R.C. 145.73. I note that section 403(b) provides for the purchase of an annuity with amounts that an employee elects to defer pursuant to a salary reduction agreement. See 26 U.S.C. §403(b)(1)(E) (1988). R.C. 145.73 requires that the employer of an eligible employee contract with the employee upon application for his participation in a deferred compensation program offered by the Board.

Your second question asks whether all employee benefit programs offered by the Board must be equally available to all eligible employees, or whether the Board may offer programs for which only certain eligible employees legally qualify. It is important to consider this issue in connection with programs under section 403(b).

R.C. 145.71 was recently amended to change the definition of the term "eligible employee," as used in R.C. 145.73. See Sub. S.B. 240, 118th Gen. A. (1990) (eff. July 24, 1990). R.C. 145.71 now states:

(A) "Eligible employee" includes any public employees as defined in division (A) of section 145.01 [Public Employees Retirement System], any person eligible to become a member under section 145.20 [elective officials], any employee as defined in division (C) of section 742.01 [Police and Firemen's Disability and Pension Fund], any employee as defined in division (B) of section 3309.01 [Public School Employees Retirement System], any employee as defined in division (A) of section 5505.01 of the Revised Code [Highway Patrol Retirement System], and any member of the state teachers retirement system.

R.C. 145.71 thus includes as "eligible employees" all members of the State Teachers Retirement System ("STRS"). Prior to its amendment, R.C. 145.71 included as "eligible employees" only certain of such members - *i.e.*, employees of the State School for the Deaf and the State School for the Blind and appointees of the State Board of Education or the Superintendent of Public Instruction.

Section 403(b) is relevant in light of this amendment, since programs under section 403(b) are, pursuant to federal law, available only to employees of tax-exempt organizations and public schools. Section 403(b) provides for the deferral of compensation, *inter alia*, in certain circumstances in which an annuity contract is purchased "for an employee...who performs services for an educational organization described in section 170(b)(1)(A)(ii), by an employer which is a State, a political subdivision of a State, or an agency or instrumentality of any one or more of the foregoing." 26 U.S.C. §403(b)(1)(A)(ii) (1988). The Board is, thus, asking, in light of the fact that all STRS members are now eligible for deferred compensation programs under R.C. 145.73, whether it may provide programs that are available to school employees under section 403(b), but are not available to other public employees.

It is clear under R.C. 145.73 that the Board must "offer to all eligible employees...a program for deferral of compensation, including a reasonable number of options to the employee for the investment of deferred funds." It might be argued on the basis of this language that a single program must be offered to all eligible employees and, thus, that all employees must be able to qualify for each option that is available under the program. R.C. 145.73 does not, however, directly address the question whether each option must be available to every eligible employee. Since no

such requirement is directly imposed, it appears that the Board may use its discretion in determining whether to provide options for which some of the eligible employees may not be qualified under federal law. *See generally, e.g., State ex rel. Hunt v. Hildebrant*, 93 Ohio St. 1, 12, 112 N.E. 138, 141 (1915) (where an officer has been given no clear direction on a particular matter, the officer "has implied authority to determine, in the exercise of a fair and impartial official discretion, the manner and method" of performing his duties), *aff'd*, 241 U.S. 565 (1916); *Jewett v. Valley Railway Co.*, 34 Ohio St. 601 (1878); 1986 Op. Att'y Gen. No. 86-076; Op. No. 85-007. The language of R.C. 145.73 does not appear to preclude the Board from offering an option for which certain eligible employees are not qualified under federal law.¹ Such an option may be part of the program that is offered to all eligible employees, even though certain employees are precluded by federal law from participating in the option. It is, however, necessary under R.C. 145.73 for the Board to assure that the program as a whole provides each employee with a reasonable number of options for which the employee is legally qualified.

I conclude, accordingly, that R.C. 145.73 does not preclude the Board from offering a plan for the deferral of compensation on the sole basis that federal law does not permit certain eligible employees to participate in the plan. With respect to plans under section 403(b), it follows that the Board may offer such plans if it can comply with federal requirements. It should be noted that various federal statutes impose nondiscrimination requirements. *See, e.g., 26 U.S.C. §403(b)(1?)* (1988). Federal law, does, however, permit the exclusion of persons who participate in other deferred compensation plans or arrangements, *see, e.g., 26 U.S.C. §403(b)(12)*, and does impose limitations on total amounts that an employee may elect to defer, *see, e.g., 26 U.S.C. §§402(g), 457* (1988). In particular section 457(c)(2) states expressly that, in computing the maximum amount of compensation of an individual that may be deferred under 26 U.S.C. §457(a) in any taxable year, any amount excluded from gross income under section 403(b) shall be treated as an amount deferred under section 457(a). 26 U.S.C. §457(c)(2) (1988).

I turn now to the question whether the Board may offer employee benefit programs under section 407. Section 407 provides that, for purposes of certain employee benefits, employees of domestic subsidiaries engaged in business outside the United States may be treated as employees of the domestic parent corporation. By its terms, section 407 relates to pension, profit-sharing, or stock bonus plans described in sections 401(a) and to annuity plans described in section 403(a); it does not relate to plans described in section 403(b). It does not appear that section 407 and related provisions are applicable to governmental entities, and it follows that a program under section 407 is not available to the Board.

It is, therefore, my opinion, and you are hereby advised, as follows:

1. Pursuant to R.C. 145.73, the Ohio Public Employees Deferred Compensation Board is authorized to promulgate and offer a program for deferral of compensation under any available federal statute, provided that the required approval of the Internal Revenue Service is obtained and the desired tax treatment is assured; the Board may act pursuant to 26 U.S.C. §457 or pursuant to any other available provisions.
2. The Ohio Public Employees Deferred Compensation Board is not precluded by R.C. 145.73 from offering employee benefit programs for which certain eligible employees are not qualified under federal law; the Board is, however, required to assure that the program for deferral of compensation as a whole provides each eligible employee with a reasonable number of options for which the employee is legally qualified.

¹ I am not considering whether the Board may offer options that are not available to some eligible employees for reasons other than their failure to qualify for such options under federal law.

3. Under current federal law, state and local governments are not eligible to adopt plans under 26 U.S.C. §401(k) and may not offer such plans unless they adopted them before May 6, 1986; thus, the Ohio Public Employees Deferred Compensation Board may not currently offer a program for the deferral of compensation under 26 U.S.C. §401(k) unless it adopted a plan under that provision before May 6, 1986.
4. The Ohio Public Employees Deferred Compensation Board may offer employee benefit programs under 26 U.S.C. §403(b), provided that the Board complies with federal law and that the appropriate approval of the Internal Revenue Service is obtained.
5. Under current federal law, the Ohio Public Employees Deferred Compensation Board may not offer a program for the deferral of compensation under 26 U.S.C. §407.