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SENATE GOVERNMENT AFFAIRS COMMITTEE
TESTIMONY ON AB 225 BY FRED HINNERS
MAY 9, 2003

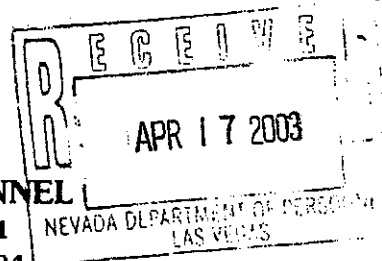
Senators, for the record my name is Fred Hinnners, I am a state employee, but today I am testifying as a private citizen. I am a former member of the State Deferred Compensation Committee, and I have an idea that will save the State of Nevada more than \$6 million over the next biennium.

State agencies and the university system pay into Social Security for their part-time and seasonal employees. The reason they do this is because employees who are less than half-time are not eligible for Public Employees Retirement System, yet they are required to be covered by some sort of retirement program. Under Social Security, employees pay 7.5 percent, and the state, as employer, is required to make a 6.2 percent match. These matching funds add up to \$3 million per year for the University and Community College System alone. The university and colleges in northern Nevada paid \$1.336 million last year; in southern Nevada it was \$1.645 million. In a recent year, general fund agencies paid out \$366,000 as the employer's share of Social Security; Nevada Department of Transportation paid out approximately \$50,000 last year.

Instead of contributing to Social Security, I propose Nevada require its part-time and seasonal employees to contribute to the state's deferred compensation program. Deferred compensation is a qualified retirement program under Chapter 26 of the United States Code, and there would be no problem switching from Social Security to deferred compensation. This is already being done in local jurisdictions, Reno, Washoe County and Carson City, and the states of Illinois and Florida. The only requirement to make this proposal a reality is a change to state statutes and requiring part-time and seasonal employees to contribute a minimum of 7.5 percent.

The benefits to the state are obvious. I feel this change will also benefit employees. We can start part-time and seasonal employees on perhaps a long-term retirement program. If the employee leaves the state system, the deferred comp proceeds can be rolled over into an Independent Retirement Account. Other benefits are that deferred compensation contributions are pre-tax, and take home pay is greater.

For your reference I have attached a memo quoting the attorney general's position stating this change cannot be made administratively; a change of statutes is required. Also attached are a series of questions and answers provided by Nevada's deferred compensation administrator Hartford on the practicality and legality of shifting part-time employees from Social Security to deferred compensation.

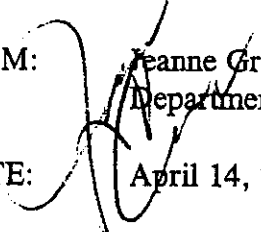


DEPARTMENT OF PERSONNEL

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MEMORANDUM

TO: Pat Ullom, Secretary
Merit Award Board

FROM:  Jeanne Greene, Director
Department of Personnel

DATE: April 14, 2003

SUBJECT: MERIT AWARD SUGGESTION

I have evaluated the suggestion from Fred Hinner regarding changing contributions for part-time and seasonal employees from Social Security to the Deferred Compensation Program. In reviewing this suggestion with Senior Deputy Attorney General Jim Spencer, it appears that changes to Chapter 287 of the NRS would be required before this suggestion could be implemented. Therefore, a decision must be made by the Governor, Director of Administration and the Board of Regents to pursue the required statutory changes before the Merit Award Board can consider Mr. Hinner's suggestion.

I have attached the evaluation completed through this office as well as Mr. Hinner's suggestion for the Board's review.

JG:dd

Attachments

Cc: Keith Munro, General Counsel, Office of the Governor
John P. Comeaux, Director, Department of Administration
Jane Nichols, Chancellor, University and Community College System of Nevada

CHAPTER III

457 PLANS AS A FICA ALTERNATIVE

III.1 *Are employees of state or local governments subject to FICA tax?*

The Omnibus Budget Reconciliation Act of 1990 (OBRA) amended the Internal Revenue Code and the Social Security Act by changing the definition of employment for FICA tax purposes. Since July 1, 1991 employment, for FICA purposes, includes services performed by an employee of a state or local government entity unless that employee is a member of a retirement system of that entity.

III.2 *Is there any way a government employee can still be exempted from FICA tax?*

An employee will not be subject to FICA tax if the following two requirements are met: First, the state or local government entity must provide a retirement plan with a specified minimum benefit or contribution. Second, the employee must be a qualified participant in the retirement system.

III.3 *Can government employees be exempt from the Medicare tax?*

No. As was always the case, employees hired after April 1, 1986 must still pay Medicare

taxes. The employee is only exempt from the Old Age Security and Disability Insurance (OASDI) portion of FICA, commonly known as Social Security taxes.

III.4 What is a retirement system?

As defined by the IRS, a retirement system is any plan or system that provides a specified minimum retirement benefit or contribution. The plan need not be a qualified retirement plan. Therefore, eligible deferred compensation plans may meet the requirements.

III.5 What are the specified minimum benefits?

First, the benefits or contributions must be retirement income benefits. In the case of a defined contribution plan, the minimum contribution must be at least 7.5 percent of compensation as defined for FICA tax purposes. Base pay cannot be used to calculate the minimum contribution and the amount of wages over the FICA tax wage base can be ignored in calculating the 7.5 percent contribution. An employee's contribution may be considered in determining if the minimum benefit is met. Therefore, a state or local government employee contributing 7.5 percent of his salary to a section 457 deferred compensation plan may avoid FICA tax, if all the other requirements are met.

III.6 Who is a qualified participant?

A qualified participant is any employee who participates in a retirement system and for that year actually receives an allocation or benefit equal to the minimum benefit

requirement.

III.7 Are there any vesting requirements?

There are no special vesting requirements for ordinary full-time employees. However, in order for part-time, seasonal and temporary employees to be exempt from FICA tax, the plan must provide for full and immediate vesting of contributions. This provision makes section 457 eligible deferred compensation plans a potentially beneficial retirement plan for this purpose, since all participant contributions are fully and immediately vested.

III.8 Could an employer make contributions to a section 457 plan mandatory?

Yes. The employer can require employees to contribute the minimum benefit/contribution requirement.

III.9 What are the benefits of using an eligible section 457 plan to allow employees not to be subject to FICA taxes?

The government cost for the plan may be less than the cost to pay the employer's share of the FICA tax. The employee may actually see a greater benefit from the section 457 contributions since, unlike the FICA tax, these contributions reduce wages for federal income tax purposes.