Financial Forum

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Q. Can our township participate in the Social Security system AND have a pension plan?

It is possible for an employer to have both a pension plan and participate in the Social Security system, depending on the answers to the following questions:

- Is a "218 agreement" in place, and is the employee participating in a pension plan covered under the agreement?
- Does the pension plan meet the tests described in federal tax law to be considered a "public retirement system"?

All state and local government employees fall into one of three categories with respect to Social Security coverage:

1) Those covered by a 218 agreement, which is a voluntary arrangement between the state, local and federal governments to provide coverage for all or a specific class of public employees in the Social Security system *(also called voluntary coverage)*
2) Those not covered by a 218 agreement and not covered by a public retirement system *(mandatory coverage)*
3) Special exemptions, such as certain emergency workers—those hired for a specific emergency with no intention of permanent employment—and election workers who earn less than a specified amount for a calendar year (currently $1,500 year), may be excluded from Social Security.

If your township doesn't have a 218 agreement or if an employee is not covered by the 218 agreement, we then must determine if the township's pension plan meets the requirements to be considered a public retirement system. First, we need to identify the type of plan your township has established, which generally falls into one of two categories:

- **Defined benefit plans**, which are based on the participant's receiving future benefits, usually expressed in a monthly benefit, based on a percentage of future earnings
- **Defined contribution plans**, which generally are funded based on a percentage of an employee's compensation

Next, compare the plan's coverage or benefits to federal requirements specific to each plan type:

Defined Benefit Plans

- Basic benefits accrued under the plan must be comparable to basic benefits the employee would have accrued under Social Security—at least 1.5 percent of average compensation received in the last three years of employment multiplied by the number of years of service. *(See IRS Revenue Procedure 91-40 or your plan administrator for further details.)*

Defined Contribution Plans

- An allocation of at least 7.5 percent of the employee's compensation is made to his or her accounts.
- Contributions from employee and employer are taken into account for above test.
- All contributions for part-time and seasonal employees must be non-forfeitable.

Armed with the information above, we can determine that:

IF an employee works for a township with a 218 agreement and the employee is covered by the agreement, the township may establish a public retirement system covering that employee.

IF the township doesn't have a 218 agreement and has a public retirement system, the employee covered by the public retirement system may not participate in Social Security, as federal law prohibits voluntary participation in Social Security for state and local government employees. They must participate either through a 218 agreement or the mandatory coverage for employment not covered by a public retirement system.

IF the township doesn't have a 218 agreement and wishes to provide employees with both Social Security coverage and a pension plan, the pension plan must fail the federal requirements previously described.

Most employment is subject to Medicare taxes except for certain exclusions for election workers and emergency workers, and possibly the continuing employment exceptions outlined in federal law for those employed prior to March 1986.

Information provided in Financial Forum *should not be considered legal advice, and readers are encouraged to contact their township auditor and/or attorney for advice specific to their situation.*