

REFUNDS AND DISTRIBUTIONS

EMPLOYER MANUAL

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REFUNDS AND DISTRIBUTIONS

EMPLOYER
MANUAL

Certain life events may entitle a VRS member or a member's beneficiary to receive a refund and/or a distribution, depending upon the member's plan. Throughout this chapter, usage of "refund" refers to taking defined benefit funds from the member contribution account (MCA) and "distribution" refers to receiving contributions and net investment earnings from the defined contribution component for Hybrid Retirement Plan members.

ELIGIBILITY

The following individuals may be eligible to take their funds:

- A member who terminates VRS-covered employment, provided that the member does not become re-employed in another VRS-covered position within one full calendar month of termination (must be a bona fide break in service);
- A member who terminates VRS-covered employment and moves to a non-covered (part-time, non-classified, wage) position with a different VRS-participating employer without a full calendar month break in service (All agencies of the Commonwealth of Virginia are considered to be one employer);
- A Plan 1 or Plan 2 member who takes a work-related disability retirement; or
- The beneficiary of a member or retiree who dies with money remaining in his account(s).

Note: A member who becomes covered by an Optional Retirement Plan (ORP) may transfer his funds to his ORP account. An ORP is a defined contribution retirement plan only available to certain eligible employees.

The following individuals are not eligible to take a refund or distribution:

- A member who continues employment in a VRS-covered position;
- A member who terminates VRS-covered employment and moves to a non-covered (part-time, non-classified, wage) position with the same employer, unless the member incurs a full calendar month break in service;
- A member on leave (including educational leave) with or without pay unless employment is terminated;
- A member of VRS who transfers to another VRS-covered position or a position covered under the State Police Officers' Retirement System (SPORS), the Virginia Law Officers' Retirement System (VaLORS), the Judicial Retirement System (JRS) or any of the Optional Retirement Plans (other than a trustee-to-trustee transfer to the ORP account) or alternative retirement plans established by the *Code of Virginia* without at least a full calendar month break in service;

- An educator or faculty member who goes on summer break after completing a contract period with an employer, if the educator or faculty member will be returning to employment with the same or another VRS-participating employer at the beginning of the next contract period;
- A member of VRS who is employed with a university and who elects an ORP, unless the member terminates VRS-covered employment and has at least a full calendar month break in service. A member who does not terminate employment may transfer the balance of the funds to the ORP or leave the funds in VRS. A member who leaves the funds in VRS becomes a member in deferred status. A member who wants to transfer retirement contributions and interest to an ORP must complete a Request for Transfer of Refund to ORP (VRS-3ORP);
- A member who retires for service or non-work-related disability; or
- A non-vested member who has no member-paid defined benefit contributions, unless involuntarily separated from his job through causes not related to job performance or misconduct;
- A member on short-term or long-term disability who wishes to continue to receive disability benefits.

REFUNDS AND DISTRIBUTIONS

When a member terminates employment, he either becomes a deferred member by leaving his defined benefit contributions and interest in the retirement system or he can take a refund of his MCA. Depending on his vesting status and when the contributions were made, a refund of the MCA includes the member's retirement contributions, as well as any employer-paid member wcontributions, payments the member may have made to purchase service credit, plus any interest accrued on the account balance. For a Hybrid member, a distribution from the defined contribution component is determined by the amount of contributions and his net investment earnings. A Hybrid member may take a refund, distribution or both. A Hybrid member may also choose to leave funds in his defined contribution accounts.

BREAK IN SERVICE

A member must have a full calendar month break in service before taking a refund or distribution. The one full calendar month break in service must take place over a period the employee normally would work. For teachers and other contract employees, summer breaks or intersession periods do not count toward this break in service. The Internal Revenue Service (IRS) prohibits distributions from a qualified pension without a bona fide break in service.

Note: All agencies of the Commonwealth of Virginia are considered to be one employer. For example, an employee of the College of William and Mary who accepts a position with the Department of Environmental Quality remains an employee of the Commonwealth and is not eligible for a refund or distribution.

A member who terminates covered employment to work in a part-time wage position with the same employer is not eligible to take a refund or distribution unless there is a bona fide break in service of at least a full calendar month between the two positions. The member must not be reported on the employer’s payroll for at least a full calendar month.

MEMBERSHIP IMPLICATIONS

If a member decides to take a refund or distribution, VRS benefits may be impacted, depending on which funds are withdrawn. If a member takes a refund of the MCA, VRS membership and the service credit represented by the amount of the refund are lost. If a Hybrid member takes a distribution from the defined contribution component but does not take a refund, he remains a deferred member. The chart below reflects refund and distribution options and the impact on membership status.

If the member is...	and takes a...	then...
Plan 1 or Plan 2	refund of the MCA (defined benefit);	he terminates membership in VRS;
Hvbrid Retirement Plan	refund of the MCA(defined benefit);	he terminates membership in VRS;
Hybrid Retirement Plan	distribution of the defined contribution account(s) (Hybrid 401(a) Cash Match Plan or Hybrid 457 Deferred Compensation Plan);	he remains in VRS as a deferred member as long as he does not take a refund of the MCA (defined benefit);

If a member takes a refund and returns to a covered position, he will be hired under the plan provisions in effect at the time.

Example: If a Plan 1 member terminates employment and takes a refund but returns to non-hazardous duty VRS-covered employment on January 1, 2018, he will become a Hybrid member.

BENEFIT IMPLICATIONS

Because membership ends when a member takes a refund, VRS benefits also end. If a Hybrid member takes a distribution but leaves his MCA in VRS, there is no impact to his benefits. The following chart explains what happens to the benefits of a member who takes a refund.

Benefit	Refund Effect on the Benefit
Monthly Defined Benefit	The member is no longer eligible for the benefit;
Basic group life insurance	Coverage ceases, but the member may convert the entire amount of Group Life Insurance or any portion of the natural death benefit to an individual whole life policy, with certain conditions, using an Enrollment Form for Conversion of Group Life Insurance (VRS-35);
State Retiree Health Benefits Program	The member is no longer eligible for coverage;
Disability benefits under the Virginia Sickness Disability Program (VSDP) and Virginia Local Disability Program (VLDP)	Short-term and long-term disability benefits end. However, the member can continue long-term care coverage by completing the Authorization of Coverage Retention Long Term Care Plan (VRS-170) and the Protection Against Unintentional Lapse Long Term Care Plan (VRS-171) within 60 days of the date of termination. The member must pay the cost of long-term care coverage;
Commonwealth of Virginia 457 Deferred Compensation Plan and Virginia Cash Match Plan	If the member has money in either plan, he may leave the money in the plan(s) or choose from a variety of distribution options;

PAYMENT AND DISTRIBUTION OPTIONS

The amount of refunded contributions depends on the employee's hire date and if he is vested.

The following chart explains how the hire date affects members:

	Hired Before July 1, 2010	Hired on or after July 1, 2010
Vested	All accumulated contributions and interest are refundable, regardless of hire date;	
Not vested with employer-paid member contributions only	<ul style="list-style-type: none"> • Contributions and interest credited before July 1, 2010 and interest earned on those funds after July 1, 2010 are refundable; • Contributions made after July 1, 2010 and interest earned on those contributions are not refundable; 	<ul style="list-style-type: none"> • Contributions and interest are not refundable; • Refund is not processed and the member goes into deferred status;
Not vested with employer-paid member contributions and member-paid member contributions	<ul style="list-style-type: none"> • Employer-paid member contributions and interest credited before July 1, 2010 and any interest earned on those funds after July 1, 2010 are not refundable; • All member-paid member contributions and interest are refundable; 	<ul style="list-style-type: none"> • Employer-paid member contributions and interest are not refundable; • All member-paid member contributions and interest are refundable;

REFUNDS AND DISTRIBUTIONS

Employer contributions that are not refunded to the member are moved to the employer's Retirement Allowance Account (RAA). If multiple employers are involved, the amount reverts on a pro-rata basis to each employer. The member may later purchase the service representing the refund and any funds that reverted to the RAA.

Note: This rule only applies if the member's termination is due to a reason other than involuntary separation of employment for causes other than job performance or misconduct, death or work related disability retirement.

A Hybrid member with less than four years of service is also eligible to receive a percentage of employer-paid contributions to the defined contribution component, depending on his years of service. A member is always entitled to his own contributions made to defined contribution accounts.

If a Hybrid member is not 100% vested in the employer contributions for the defined contribution component and takes a refund, then his non-vested money is forfeited back to the employer based on the vesting schedule below. If the member has more than one employer, the forfeited money goes to the last employer's forfeiture account at ICMA-RC.

The table below reflects the vesting schedule for the defined contribution component for Hybrid members:

Years of creditable service	Vesting schedule	Allowable withdrawals
1 year	0% vested in the employer contributions	The member forfeits the employer contributions and the net investment earnings on these contributions if he takes a distribution.
2 years	50% vested in the employer contributions	The member may be eligible to withdraw 50% percent of these contributions plus net investment earnings.
3 years	75% vested in the employer contributions	The member may be eligible to withdraw 75% percent of these contributions plus net investment earnings.
4 or more years	100% vested in the employer contributions	The member may be eligible to withdraw 100% percent of these contributions plus net investment earnings.

PAYMENT FOR ANNUAL LEAVE

An employer's personnel policy may provide for paying a terminating member accumulated annual leave in a lump sum amount or to keep the member on the payroll until his leave is exhausted. The method of payment selected affects deductions, benefits and the time when a refund/distribution request may be submitted.

If a member receives a lump-sum payment for the unused leave time, VRS contributions are not deducted and creditable service is not earned. If a member remains on the payroll until all leave is exhausted, VRS contributions continue to be paid and the member earns service credit for the unused leave time. A member is not eligible for a refund until the employer terminates him in myVRS Navigator and a full calendar month break in service has been satisfied.

REFUNDS/DISTRIBUTIONS PAYABLE DUE TO DEATH

If an active member dies, his beneficiary for retirement benefits is eligible for a refund. A beneficiary who is the member's spouse, minor child or parent may choose a monthly benefit if the member was vested or a refund to the exclusion of any other named beneficiary. If the member's death is from a cause compensable under the Virginia Workers' Compensation Act, the designated beneficiary receives a refund and the surviving spouse receives a monthly benefit. If there is no surviving spouse, any surviving minor children equally share the monthly benefit. If there are no surviving minor children, then the surviving parent(s) receive the monthly benefit. If the member was in the Hybrid Retirement Plan, the beneficiary can request a distribution of the defined contributions and net investment earnings according to their beneficiary designation or the order of precedence, as established by the *Code of Virginia*.

A beneficiary who receives a refund or a distribution is required to show positive proof of identity before receiving the funds. When funds are paid by order of precedence, VRS requires a statement indicating all living heirs to include name, address, telephone number, and proof of Social Security number.

If a retiree who did not elect a Survivor Option dies before receiving retirement benefits that equal or exceed the balance of the MCA, the retiree's beneficiary is entitled to receive a refund of the remaining retirement contributions plus interest that has accrued to the date of retirement.

For additional information on death payments, see the Death Benefits Chapter of the Employer Manual.

REFUNDS/DISTRIBUTIONS PAYABLE DUE TO WORK-RELATED DISABILITY RETIREMENT

A member who is approved for work-related disability retirement receives a mandatory refund of his MCA in addition to a monthly retirement benefit from VRS. A Hybrid member may also request the funds from his defined contribution accounts. For additional information on disability retirement, see the Disability Retirement Chapter of the Employer Manual.

LEAVING THE MONEY IN VRS

A member who leaves retirement contributions in VRS defers retirement benefits and retains the service credit that was earned as an employee. This credit can be added to any service credit the member may earn through future VRS-covered employment. If no refund was taken, the member will remain in the same plan if he rejoins VRS-covered employment.

VRS contacts members at full or unreduced Social Security age to provide an unreduced Basic Benefit estimate and the current account balance available for refund. A member whose retirement contributions remain in VRS must start receiving a monthly benefit or take a refund by April 1 following the calendar year in which he reaches age 70½ unless he returns to covered employment or non-covered employment with a participating employer. VRS contacts members who do not retire prior to the calendar year in which they reach age 70½. If the member does not respond and has not submitted a retirement application, the member is retired under the Basic Benefit.

A member who chooses to leave the balance of his MCA in VRS must complete a Name and Address Declaration for Deferred Members (VRS-3A). The employer is responsible for ensuring the member completes a VRS-3A or registers for myVRS and updates his address.

A Hybrid member who chooses to leave his defined contribution accounts in VRS can continue to make changes to his investment allocations and may also roll assets from other eligible retirement plans into the Hybrid 457 Deferred Compensation Plan. A member must take required minimum distributions at age 70½. A member is not allowed to make additional contributions. Changes to defined contribution accounts can be accessed through the Defined Contribution Plans section of the VRS website at www.varetire.org/hybrid.

APPLYING FOR A REFUND AND DISTRIBUTION OPTIONS

A member must wait one full calendar month from the separation date the employer enters in myVRS Navigator to be eligible for a refund or distribution. To request a refund, the member must use the myVRS online self-service tool. myVRS allows the member to consider different refund payment options and walks him through the process step by step. The refund is available via direct deposit within 3-5 business days.

Note: Refunds in the case of death are not initiated through myVRS.

A Hybrid member may take a distribution from either the Hybrid 457 Deferred Compensation Plan or the Hybrid 401(a) Cash Match Plan by completing the VRS Hybrid 457 Deferred Compensation Plan Distribution/Direct Rollover/Transfer Request and/or the VRS Hybrid 401(a) Cash Match Plan Distribution/Direct Rollover/Transfer Request. These forms are located on the Forms page of the Hybrid Retirement Plan section of the VRS website at www.varetire.org/hybrid. Employers are not required to sign off on the distribution forms.

A member with a balance in the Hybrid Retirement Plan defined contribution component may request a distribution as:

- A total or partial lump sum;
- An annuity payment;
- A periodic payment;
- A partial lump sum with remainder paid as a periodic payment or annuity; or
- A rollover to another qualified plan.

For more detailed information on these options and tax withholding, the member should contact ICMA-RC at 1-877-327-5261, option 1.

Note: The member should use the VRS-3ORP, found on the VRS website, to transfer his MCA to an ORP.

TAXATION OF REFUNDS AND DISTRIBUTIONS

VRS makes every effort to provide the best information available on the tax status of a refund or distribution, but it is ultimately the member's responsibility to ensure compliance with all state and federal tax regulations.

Members should read the IRS 402(f) – Special Tax Notice available in myVRS, before taking a refund or distribution. This Special Tax Notice provides information about the potential tax consequences and explains how distributions may be rolled over to an individual retirement account (IRA) or another qualified plan. Members with tax questions should contact the Department of Taxation, the IRS, or a tax advisor.

The taxable portion of a refund and distribution paid to the member is subject to a mandatory 20% federal tax withholding in the year it is issued.¹ In addition, a 4% state tax withholding is applied to the taxable portion of the refund and distribution if the member is a legal resident of Virginia at the time of payment. If the member is no longer a Virginia resident, he is responsible for paying the appropriate taxes to his state of residence. All funds are taxed except the funds on which the member has already paid taxes. VRS or ICMA-RC automatically withholds the required taxes before distributing the funds to the member. In addition to state and federal taxes, a member under age 59½ who receives a distribution from the Hybrid 401(a) Cash Match Plan may have an additional 10% tax penalty imposed by the IRS. The 10% penalty is not applied to distributions from the Hybrid 457 Deferred Compensation Plan. If applicable, the member is responsible for paying the 10% penalty when filing his tax return.

A member can defer tax withholdings and avoid the 10% penalty if he chooses to roll over the taxable contributions and interest directly into a traditional IRA, a Roth IRA (under certain circumstances), 403(b) plan, eligible 457 plan, 401(k) plan, or other qualified plan, as allowed by the *Internal Revenue Code*. Within 60 days of receipt, the member may roll over all or part of the payment to a traditional IRA or to an eligible employer plan that accepts rollovers. The Commonwealth of Virginia 457 Deferred Compensation Plan and Virginia Cash Match Plan accept rollovers from a VRS MCA. For additional information, see the Rollover Options for Refunds or Distributions section in this chapter.

REFUNDS/DISTRIBUTIONS PAID TO A BENEFICIARY

A refund or distribution paid to the surviving spouse of a member may be rolled over in the same manner as the payment to the member. If the surviving spouse elects to receive a direct payment, VRS withholds 20% federal tax. In addition, a 4% state tax withholding is applied if the surviving

¹ Taxes are not withheld for refund amounts under \$200, regardless of who receives the refund. However, the recipient of the refund may be subject to additional taxes when filing the annual tax return.

spouse is a resident of Virginia at the time of payment. These withholding regulations apply only to the portion of the payment that represents taxable contributions and interest.

Even if the funds are paid directly to the spouse, the spouse may still roll over all or part of the payment within 60 days of receipt to a traditional IRA, a Roth IRA (under certain circumstances) or to an eligible employer plan that accepts rollovers.

A refund or distribution paid to a member's beneficiary who is not the surviving spouse may be rolled over into a traditional IRA or under certain circumstances, to a Roth IRA. It may not be rolled over to an employer plan. If a non-spouse beneficiary elects the payment to be made directly to the beneficiary, he may not later roll it over to another type of plan.

Payments to a surviving spouse or other beneficiary are generally not subject to the additional 10% tax penalty.

For additional information, see the IRS 402(f) – Special Tax Notice on the VRS website.

ROLLOVER OPTIONS FOR REFUNDS OR DISTRIBUTIONS

A terminated member may elect to roll over his refund or distribution to a traditional IRA, a Roth IRA (under certain circumstances) or to an eligible employer plan that accepts rollovers, including the Commonwealth of Virginia 457 Deferred Compensation Plan and the Virginia Cash Match Plan. The payment may not be rolled over to a Simple IRA, or a Coverdell Education Savings Account (formerly known as an education IRA). This postpones payment of taxes on the funds until the money is actually paid out to the member.

A rollover can be made in one of two ways:

- By VRS;
- By the member (if he opts to receive a direct payment from VRS or ICMA-RC).

A member may elect a direct rollover through myVRS. However, if the refund is less than \$200 of taxable income, VRS pays the funds directly to the member.

A member who elects a rollover after first receiving a payment from VRS must make the rollover within 60 days of receiving the funds. The member may replace federal and state tax withholdings with personal funds to roll over 100% of the refund or distribution. Otherwise, the tax withholding

portion is subject to taxation in the year it is withheld. The amount rolled over is not taxable until the member receives the funds.

Funds received from a refund or distribution may be rolled to either a traditional IRA or an eligible employer plan. An eligible employer plan includes a plan qualified under section 401(a) of the Internal Revenue Code, including the Virginia Cash Match Plan (if the employer provides that plan and the employee is eligible), a 401(k) plan, profit-sharing plan, defined benefit plan, stock bonus plan and money purchase plan; a section 403(a) annuity plan; a section 403(b) tax-sheltered annuity; and an eligible section 457(b) plan maintained by a governmental employer (governmental 457 plan such as the Commonwealth of Virginia 457 Deferred Compensation Plan). The VRS is a defined benefit plan qualified under section 401(a) of the Internal Revenue Code. The member may not roll over a refund into a Roth IRA.

An eligible employer plan is not legally required to accept a rollover. A member who wants to roll over funds to another plan should check with that plan's administrator prior to making the rollover. It is the responsibility of the member to verify that the recipient plan will accept a direct rollover.

If the member made after-tax contributions to VRS, the portion of the payment representing after-tax contributions may not be rolled to a governmental 457 plan. If the after-tax contributions are to be rolled to an employer plan that accepts these rollovers, the refund or distribution payment cannot be paid to the member.

If the member rolls after-tax contributions into a traditional IRA, it is the member's responsibility to report the amount of these after-tax contributions to the IRS. Once the member rolls after-tax contributions into a traditional IRA, those amounts cannot later be rolled over to an employer plan.

Note for employers participating in the Virginia Cash Match Plan: The member may roll over both taxable and after-tax funds to the Virginia Cash Match Plan by completing an Incoming Transfer/Direct Rollover form available through the Defined Contribution Plans section of the VRS website at www.varetire.org or by calling 1-877-327-5261 (VRS DCPLAN1). The funds may also be rolled over to the Commonwealth of Virginia 457 Deferred Compensation Plan.

ATTACHMENTS TO REFUNDS AND DISTRIBUTIONS

VRS refunds and distributions are exempt from county and municipal tax and are not subject to execution, attachment, garnishment or any other process whatsoever, except under the following conditions:²

- IRS tax levies (the member will be notified by the IRS and VRS regarding the amount of the attachment.);
- Debt to an employer who has employed the member;
- Child support payments;
- Marital property as stated in an Approved Domestic Relations Order.

PAYMENTS PROCURED BY FRAUD OR FALSE STATEMENTS

Any payment to a member or beneficiary which is later determined to have been procured on the basis of any knowingly false statement or falsification of records may be recovered from the member or beneficiary by:

- Credit against future payments due the member or beneficiary;
- Legal action against the member or beneficiary; or
- Deducting any overpayment of benefits from insurance proceeds.

The member or beneficiary is given an opportunity to dispute any such proceedings in accordance with provisions of the Administrative Process Act.

² See Code of Virginia §51.1-124.4.