IRC SECTION 415(b) REPLACEMENT BENEFIT PLAN FACT SHEET

The California Public Employees Retirement System (CalPERS) is subject to federal tax laws applicable to governmental tax-qualified pension plans. Annual retirement benefits (allowance) payable from CalPERS are subject to dollar limits imposed by Section 415(b) of the Internal Revenue Code (IRC).

- 2015 Annual Limit = $210,000 for people who retire between the ages of 62-65
- Annual Limit is reduced for people who retire under the age of 62

At retirement, each retirement allowance payable is screened to determine if it is subject to limitation under IRC Section 415(b). Factors used to determine the limit include:

- Retiree’s age at retirement
- Retirement option and beneficiary’s age at retirement
- Taxed member contributions
- Rollover and post-tax contributions used to purchase service credit

The age 62-65 dollar limit is used instead of the actual age dollar limit:

- For allowances of police officer and firefighter members with 15 or more years of service as full-time employees of a police department or a fire department providing police protection, firefighting services, or emergency medical services. Service with employers other than a police or fire department, such as correctional facilities, does not qualify for this higher limit.
- For a survivor’s allowance payable due to the pre-retirement death of a member
- For disability retirement

If an allowance is determined to be subject to the limit, CalPERS administers the Replacement Benefit Plan (RBP) which allows for the “replacement” of the annual allowance that exceeds the IRC Section 415(b) limit to the extent permitted by law. The RBP is a “pay as you go” fund; all of the retiree’s prior CalPERS employers are invoiced and payment from all of those employers must be received before RBP benefits can be issued to the retiree.

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1 Ages 62-65 are defined as “normal retirement age” by the Social Security Administration
2 Retirement allowances are not tested before retirement due to the individualized nature of testing.
What is the Replacement Benefit Plan\(^3\)?

The RBP is the CalPERS plan that provides for replacement of the retirement allowance that exceeds the IRC Section 415(b) dollar limit. If an allowance is determined to exceed the limit, the total allowance will be paid from two sources, the Public Employees Retirement Fund (PERF) and the Replacement Benefit Fund (RBF). All of the retiree’s prior CalPERS employers whose service is included in the retirement allowance calculation are invoiced each year the allowance exceeds the limit; CalPERS must receive payment from all of the employers before issuing payment to the retiree.

Every CalPERS employer is deemed to participate in the RBP in accordance with Government Code section 21761.

Who is eligible to participate in the RBP?

A CalPERS retiree who became a CalPERS member prior to January 1, 2013, or a beneficiary or survivor whose allowance exceeds his or her personalized IRC Section 415(b) dollar limit.

How does the RBP affect the retiree’s death benefits?

If the death benefit is a monthly allowance payable to a beneficiary, the beneficiary’s allowance is tested for the IRC Section 415(b) limit in effect at the time of the retiree’s death. The testing uses the same factors that applied to the retiree’s personalized dollar limit at retirement. If the individual beneficiary’s allowance exceeds the dollar limit, the beneficiary will receive payment from the PERF and the RBF.

How do taxes apply to the RBP?

The income received through the RBP is a wage under federal tax law and is subject to Federal Insurance Contributions Act (FICA) tax during the first year an allowance is limited. FICA consists of the Old Age, Survivors and Disability Insurance (OASDI) Social Security tax and the Hospital Insurance/Medicare (Medicare) tax.

If OASDI and/or Medicare taxes are due on the replacement benefit, these taxes must be paid first, before any replacement benefit payment is issued to the retiree. Therefore, it is possible that the first one or more replacement benefit payments will be entirely deducted to pay these taxes. The replacement benefit is subject to OASDI and/or

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\(^3\) The Replacement Benefit Plan (RBP) is governed by Government Code sections 21750-21765 (inclusive) and California Code of Regulations sections 589 – 589.10 (inclusive.)
Medicare taxes if, at any time while employed, the individual’s earnings were subject to these taxes.

The taxes are computed as follows:

1. Actuarial factors calculate the present value\(^4\) of the lifetime replacement benefit.

2. Taxes are computed on the present value as follows:
   - Social Security tax rate for employees is 6.2%, up to maximum earnings of $118,500 for 2015.
   - Social Security tax rate for employers is 6.2%, up to maximum earnings of $118,500 for 2015.
   - Medicare tax rate is 1.45% for employees and employers with no maximum earnings amount.

3. CalPERS invoices the employer(s) for their taxes.

4. CalPERS deducts any applicable OASDI and Medicare taxes from the retiree’s replacement benefit checks.

5. CalPERS remits both employee and employer taxes to the IRS.

6. At the end of the tax year, CalPERS issues the retiree W-2 tax forms for the replacement benefits paid, one from each former employer.

**How long must a retiree participate in the RBP?**

The IRS issues an update of the IRC 415(b) limit for each calendar year. The allowances of retirees in the RBP are retested every January against the new IRS limit. Retirees are required to participate in the RBP each year in which their allowances exceed their personalized dollar limits.

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\(^4\)Present value is the discounted amount the retiree will receive in lifetime replacement benefits. This discounted amount is based on CalPERS’ valuation interest rate, the post-retirement mortality table, and the Cost-of-Living Adjustment assumption. For tax purposes, the present value is treated as if it were fully paid in the year the replacement benefit becomes payable.