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**California Public Employees' Retirement System  
Benefit Services Division**

## **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 (allowances) payable from CalPERS are subject to dollar limits imposed by section 415(b) of the Internal Revenue Code (IRC).

### **What is the Replacement Benefit Plan?**

The Replacement Benefit Plan<sup>1</sup> (RBP) is a **qualified excess benefit arrangement** pursuant to IRC section 415(m). This plan provides for the replacement of the portion of the retirement allowance that exceeds the IRC section 415(b) dollar limit. Members in the RBP will receive a separate check from the State Controller's Office. All of the members' prior CalPERS employers whose service was included in the retirement allowance calculation are invoiced each year the allowance exceeds the limit.

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, a beneficiary, or a survivor whose allowance exceeds his or her personalized IRC section 415(b) dollar limit is eligible to participate in the RBP.

### **What is the 2017 IRC Section 415(b) annual dollar limit?**

The maximum annual retirement benefit payable to a member who retires between age 62 and age 65 is \$215,000 for the 2017 calendar year. The dollar limit is set annually by the Internal Revenue Service (IRS).

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<sup>1</sup> The Replacement Benefit Plan (RBP) is governed by Government Code sections 21750-21765 (inclusive) and California Code of Regulations sections 589 – 589.10 (inclusive.)

### **Under what circumstances can the IRC Section 415(b) annual limit be reduced?**

For members who retire under the age of 62, their personalized annual limit will be age-adjusted to the actuarial equivalent of \$215,000 beginning at age 62.

The \$215,000 annual limit is reduced for any member who retires with less than ten years of service in CalPERS.

### **What circumstances do not reduce the IRC Section 415(b) annual limit?**

An employee, with 15 or more years of full-time service, with a police or fire department of the state or local political subdivision of the state providing police protection, firefighting services, or emergency medical services, will not be subject to an age-adjustment reduction to their annual limit if he or she retires before age 62.

Note: Under IRC Section 415(b)(2)(H), correctional, probation, and parole employees are subject to an age-adjustment reduction if he or she retires under the age of 62.

A survivor's allowance payable due to the pre-retirement death of a member, or a member who qualifies for disability retirement will not be subject to an age-adjustment reduction, regardless of their age at retirement.

### **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 may be tested against the IRC section 415(b) limit in effect at the time of the retiree's death.

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

Members are required to participate in the RBP each year in which their allowance exceeds their personalized dollar limit. Limited allowances are retested every January against the new IRC section 415(b) annual limit.

### **How do taxes apply to the RBP?**

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

The RBP payment is subject to OASDI and/or Medicare taxes if, **at any time while employed**, the individual's earnings were subject to these taxes.

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. Monthly benefits subject to FICA tax will be held until enough has accrued to pay the tax in full, in one lump sum; therefore, it is possible that the first or more RBP payments will be held to pay these taxes.

The taxes are computed as follows:

1. Actuarial factors calculate the present value<sup>2</sup> of the lifetime replacement benefit per employer.
2. FICA taxes are computed as follows:
  - For 2017 the OASDI tax rate is 6.2 percent.
  - For 2017 the Medicare tax rate is 1.45 percent.
3. CalPERS invoices the employer(s) for their taxes.
4. CalPERS deducts any applicable OASDI and/or Medicare taxes from the retiree's RBP checks.
5. CalPERS remits both employee and employer taxes to the IRS.
6. At the end of the tax year, CalPERS issues W-2 tax forms to the retiree for the RBP checks paid, one from each former employer.

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***Important:*** *The information included in this document is general. The California Public Employees' Retirement Law and the Internal Revenue Code are complex and subject to change. If there is a conflict between the law and the information in this document, the law supersedes the information in this document.*

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<sup>2</sup> 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.