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**California Public Employees' Retirement System  
Retirement 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.

### **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) (IRC 415) dollar limit. Members in the RBP will receive a separate paper check from the State Controller's Office. All 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 payee, a beneficiary, or a survivor whose allowance exceeds his or her personalized IRC 415 limit is eligible to participate in the RBP.

### **IRC 415 vs IRC 401(a)(17) (IRC 401)**

IRC 415 places an annual dollar limitation on the total retirement benefit an individual can receive from a tax-qualified pension plan such as CalPERS.

Conversely, IRC 401 provides dollar limitations on annual compensation that can be considered under a qualified retirement plan and is only applicable to persons who first became members or participants of CalPERS on or after July 1, 1996 and before January 1, 2013. This limit is set by the U.S. Department of Treasury and places a maximum on the amount of compensation that may be considered for calculating a member's retirement benefit with CalPERS. A CalPERS

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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).

member's final compensation (FC) may be capped at the limit in effect for each 12 or 36 consecutive-month period that is used to calculate their retirement allowance.

### **What is the 2020 IRC 415 annual dollar limit?**

The maximum annual retirement benefit payable is \$230,000 for the 2020 calendar year. For members who retire under age 62, their personalized annual limit will be **age-adjusted**<sup>2</sup> to the actuarial equivalent of the \$230,000 annual retirement benefit. The age-adjustment reduction does not apply for members that retire at age 62 or older.

### **Under what circumstances can the IRC 415 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 \$230,000 beginning at age 62.

The \$230,000 annual limit is reduced for any member who retires with less than ten years of service under a CalPERS covered employer.

### **What circumstances do not reduce the IRC 415 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 415 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. Retirement allowances are retested every January against the new IRC 415 annual limit using the member's age at retirement.

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<sup>2</sup> 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.

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

If OASDI and/or Medicare taxes are due, **these taxes must be paid first**, before any replacement benefit payment is issued to the retiree. Monthly benefits subject to FICA taxes will be held until enough has accrued to pay these taxes in full, in one lump sum; therefore, it is possible that **the first or more RBP payments will be held to pay these taxes**.

FICA taxes are applied as follows:

1. Actuarial factors calculate the **present value**<sup>3</sup> (PV) of the lifetime replacement benefits per employer.
2. FICA taxes are computed as follows:
  - For 2020 the OASDI maximum taxable earnings amount is \$137,700.
  - For 2020 the OASDI tax rate is 6.2 percent.
  - For 2020 the Medicare tax rate is 1.45 percent.
  - An additional 0.9% Medicare tax is withheld on a retiree's PV in excess of \$200,000.
3. CalPERS invoices the employer(s) for their portion of the taxes.
4. CalPERS deducts any applicable FICA taxes from the retiree's RBP check.
5. CalPERS remits both employer and employee taxes to the IRS.
6. At the end of the tax year, CalPERS issues W-2 tax forms to the retirees for the RBP checks paid.

## Administrative Fee

In accordance with Government Code sections 21750-21765 and California Code of Regulations sections 589-589.10, CalPERS may charge an administrative fee to maintain the RBP. For calendar year 2020, the administrative fee has been reduced to 0.00%. The administrative fee amount may be changed periodically to ensure compliance with applicable state laws and regulations.

***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>3</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.