City of Santa Clara
The Center of What's Possible

Memorandum

Date: August 31, 2017

To: Mayor and City Councilmembers

From: City Manager Rajeev Batra

Subject: Retirement Benefits and Internal Revenue Code Section 401 (A)(17)

On March 7, 2017, the City Council approved a 5% salary adjustment for the Interim City Manager (myself) under Item 14 A 4 on the regular Council agenda. Also part of the motion was to get a confirmation on the IRS section related to pension paid above the IRS cap in order for the City to pay the difference in retirement. This action was taken while I was still an employee of the City and it is for the services previously rendered not after my retirement. Below are minutes specifically related to the item under Section 14 A 4 titled:

The Council proceeded to consider the Director of Human Resources' report recommending a **5% merit salary increase for Interim City Manager Rajeev Batra** per the Miscellaneous Management Memorandum of Understanding and to update the Compensation Schedule from $25,141 per month to $26,398 per month. A Council discussion followed. **MOTION** was made by Mahan, seconded and unanimously carried, that the Council **approve** the recommendation subject to written confirmation of the application of the Internal Revenue Code Section 401(A)(17) related to the compensation limitation law.

Staff has followed up with this matter, while it is difficult to get a response from the IRS a written opinion has been received from a CPA Tax Consultant, Mr. Harpreet Chaudhary CPA, CFP who understands these IRS sections. He has reviewed the specific section of the IRS code 401(A)(17) and confirmed that the City could pay the retirement benefit based on the difference of the IRS salary cap, for 2016 that amount is $265,000.00, and the actual pension salary. Mr. Chaudhary has confirmed "The difference is a non-qualified pension amount and may not be deductible to an employer for tax purposes, but the city should not have that issue for taxation purposes."

Attached are CALPERS Circular letter to show the IRS cap of $265k for 2016, an e-mail from a professional tax consultant and minutes from the March 7 Council meeting. As such I would like to provide this information to Finance to implement this motion as approved by the City Council on March 7, 2017. The same rules and guidelines applied by CalPERS should be followed by the City of Santa Clara independently, CALPERS does not have any objections.

Unlike other city retirees who were also above CALPERS cap and the City sends its share of retirement contribution to CALPERS, in this case there will need to be a separate agreement between the City and myself for the City to issue the check directly to the employee (myself). I will request the City Attorney's Office to draft such an agreement.

Attachments: CalPERS Circular Memo with IRS Caps
E Mail from Mr. Harpreet Chaudhary, Area Financial Services
Minutes from the March 7, 2017 Meeting

CalPERS

Payroll
Circular Letter

California Public Employees' Retirement System
P.O. Box 942715
Sacramento, CA 94229-2715
(888) CalPERS (or 888-225-7377)
TTY: (877) 249-7442
www.calpers.ca.gov

February 28, 2017

Circular Letter No: 200-010-17
Distribution: IV, V, VI, X, XII, XVI

To: All CalPERS Employers

Subject: **2017 Compensation Limits for Classic and New Members**

The purpose of this Circular Letter is to update your agency on the 2017 compensation limits for classic and new Public Employees' Pension Reform Act (PEPRA) members and provide guidelines on how to report payroll when Internal Revenue Code (IRC) or PEPRA limits have been reached in a calendar year. Section 401(a)(17) of the IRC provides earnings limits on annual compensation that can be taken into account under qualified retirement plans for some classic CalPERS members. Government Code section 7522.10 of the PEPRA provides the authority for the earnings limit for all new members.

The employer should notify all classic or new members who are subject to the compensation limit requirements.

The compensation limit for classic members for the 2017 calendar year is $270,000. Employees with membership dates prior to July 1, 1996, are not impacted by these limits.

The compensation limits for classic members during 2010-16 are:

2016	2015	2014	2013
$265,000	$265,000	$260,000	$255,000

The compensation limit for new members for the 2017 calendar year is:

Social Security participants	Non-Social Security participants
$118,775	$142,530

The compensation limits for new members during 2013-16 are:

Year	Social Security participants	Non-Social Security participants
2016	$117,020	$140,424
2015	$117,020	$140,424
2014	$115,064	$138,077
2013	$113,700	$136,440

Compensation limits for both classic and new members do not limit the salary an employer can pay, but rather limits the amount of compensation taken into account under the defined benefit plan.

Report earnable compensation to CalPERS for classic members; report pensionable compensation to CalPERS for new members. Classic and new members should not make contributions on compensation that exceeds the limit for each calendar year. In addition, exclude items such as overtime, automobile allowances, and lump-sum payouts for all compensation reported.

The employer is responsible for monitoring when an employee meets or exceeds the limit. Once a participant reaches the compensation limit, the employer must continue reporting compensation as earned; however employer and employee contributions should no longer be reported for the rest of the calendar year. my|CalPERS will track classic and new member earnings over multiple CalPERS contracting agencies. Therefore, if a member is hired in the middle of the year from another CalPERS agency, my|CalPERS will notify you, the current employer, when the member reaches or exceeds the compensation limit. Monitoring and contribution reporting begins anew at the beginning of each calendar year. The end date of the payroll earned period determines in which calendar year the period falls.

Federal law does not allow CalPERS to refund over-reported contributions to an active CalPERS member. The employer must report these adjustments and refund the money to the employee(s) once these adjustments have posted.

Impact on Final Compensation

For classic members, final compensation is the average annual compensation earnable for a 12- or 36-consecutive-month period of employment, depending on the employer contract.

Classic members' retirement allowances are subject to final compensation limits under IRC section 401(a)(17). The calculation of each 12-month period will be subject to the annual compensation limit in effect for the calendar year in which the **12-month period begins.** If final compensation exceeds 12 months, each 12-month period is calculated based on the applicable annual compensation limit for that 12-month period.

For new members, final compensation is the average annual pensionable compensation for a 36-consecutive-month period of employment.

New members' retirement allowances are subject to pensionable compensation limits under Government Code section 7522.10. The pensionable compensation limit — used to calculate final compensation — is calculated based on the limit in effect for each calendar year and the number of days per year included in the final compensation period.

Training

An online training class, "my|CalPERS Payroll: Reporting Past the Compensation Limit" is available for employers. This class provides instruction on how to report payroll information when the compensation limit has been reached. To enroll in online training, log in to my|CalPERS and select the **Education** tab.

If you have any questions, please call our CalPERS Customer Contact Center at **888 CalPERS** (or **888**-225-7377).

Renee Ostrander, Chief
Employer Account Management Division

From: Harpreet Chaudhary [mailto:harpreet@areafinancialinc.com]
Sent: Tuesday, August 01, 2017 4:15 PM
To: Rajeev Batra
Subject: Re: IRS Related Question

Rajeev,

This section does have a limit on the salary for computation of Pensions (the limit by the way is 270K for 2017 , it was 265 for 2016)

What this means is that CalPERS is not going to pay more than 270k/PA.

This does not mean that the employer cannot pay the difference to make up a higher amount.

The difference is a non-qualified pension amount and may not be deductible to an employer for tax purposes, but the city should not have that issue for taxation purposes.

In my opinion the city could pay you the difference.

Regards