

CITY OF OAKLAND
AGENDA REPORT

2008 DEC -4 PM 3:09

TO: Office of the City Administrator
ATTN: Dan Lindheim
FROM: Finance and Management Agency
DATE: December 16, 2008

RE: **Resolution Authorizing Implementation of the Provisions of Section 414(h)(2) of the Internal Revenue Code to Tax Defer Member Paid Contributions to the California Public Employees' Retirement System (PERS)**

SUMMARY

Internal Revenue Code (IRC) Section 414(h)(2) allows public agencies who are members of the California Public Employees' Retirement System (PERS) to designate employee retirement contributions, as required by bargaining unit Memoranda of Understanding, as being "picked-up" by the employer and treated as employer contributions for tax purposes. The effect of a pick-up is to defer tax on employee contribution amounts until the member retires and receives retirement benefits, or separates from employment and takes a refund of contributions. Absent the 414(h)(2) provision applicable to governmental plans, employee contributions to PERS would automatically be after-tax contributions (e.g., taxable income to the employee at the time the contribution was made).

A resolution has been prepared that will allow the City of Oakland to designate required employee contributions made by employees in the Miscellaneous group to PERS as being "picked-up" by the employer and treated as employer contributions for tax purposes.

FISCAL IMPACT

The proposed resolution creates no fiscal impact or cost to the City of Oakland.

BACKGROUND

Memoranda of Understanding between the City and bargaining units representing the Miscellaneous group (SEIU Local 1021, IFPTE Local 21, IBEW Local 1245, and Deputy City Attorney V and Special Counsel Association) require that the City pay a portion of the eight percent (8%) employee contribution for each represented employee (the percentage contributed by the employee may vary by MOU). Employees in these bargaining units have a portion of their income deducted as "Retirement Offset." The proposed resolution is required to be on file with PERS to authorize the City to treat the "Retirement Offset" amount as pre-tax income.

Memoranda of Understanding with Police and Park Rangers require the City to pick up the entire employee contribution of nine percent (9%). Those employees do not have a "Retirement Offset" deduction from their paychecks. Safety employees covered by IAFF Local 55

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(Firefighters) have a "Retirement Offset" for the full nine percent (9%) employee contribution to PERS. There is already a resolution on file with PERS that authorizes the Firefighters' pre-tax deduction under IRC Section 414 (h)(2), so no additional action is required.

IRS Revenue Ruling 2006-43 describes the actions required for governmental agencies to "pick-up" or treat certain contributions as employer contributions to a plan qualified under Section 401(a) of the Code. PERS is such a plan. If certain criteria are met, this ruling will be applied prospectively. Section 414(h)(2) specifically provides a special rule for qualified plans established by a State government or political subdivision thereof, or by any agency or instrumentality of the forgoing. Under this rule, contributions, although designated as employee contributions, are nevertheless treated as employer contributions if the contributions are picked up by the employing unit.

KEY ISSUES AND IMPACTS

Revenue Ruling 2006-43 provides, in general, that an employee contribution will not be treated as "picked-up" under IRC 414(h)(2) unless:

1. The employer specifies that the contributions, although designated as employee contributions, are being paid by the employer, and
2. The employer does not permit participating employees to opt out of the pick-up or to receive the contributed amounts directly instead of having them paid by the employer to the plan.

Further, Revenue Ruling 2006-43 allows employers who do not have written evidence of a pick-up, but their actions show that they intended to establish and carry out a pick-up, to be treated as meeting the requirements of 414(h)(2) for past pre-tax contributions if the employer takes formal action in writing prior to December 31, 2008 with respect to future picked-up contributions. The City of Oakland falls into this category and therefore has prepared a resolution to establish the required written documentation by the December 31st deadline. Adoption of the resolution will insure that employees in the Miscellaneous group will be allowed to continue pre-tax payroll deductions of their PERS employee contribution. This will exclude the employees' contribution from federal gross income and withholding requirements.

Additionally, it has been determined that the City's payroll system meets the requirements established by PERS to participate in the pre-tax payroll deduction for employee contributions. Eligible employees (Miscellaneous group) will benefit from making PERS retirement employee contributions on a pre-tax basis.

SUSTAINABLE OPPORTUNITIES

There are no economic, environmental, or social equity opportunities resulting from this action.

DISABILITY AND SENIOR CITIZEN ACCESS

The proposed action does not impact disability and senior citizen access.

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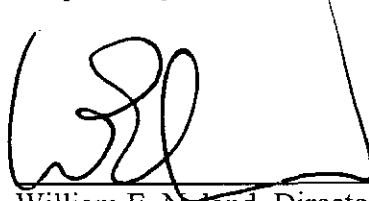
RECOMMENDATION(S) AND RATIONALE

The adoption of this resolution will allow City employees in the Miscellaneous group to continue to have payroll deductions for PERS retirement employee contributions deducted on a pre-tax basis after December 31, 2008. This resolution deals with the tax treatment of employee retirement contributions to PERS, authorizing them to be deducted on a pre-tax basis at no cost to the City.

ACTION REQUESTED OF THE CITY COUNCIL

Staff recommends that City Council approve the Resolution authorizing implementation of IRC Section 414(h)(2) to tax defer member contributions (miscellaneous group) paid to PERS.

Respectfully submitted,

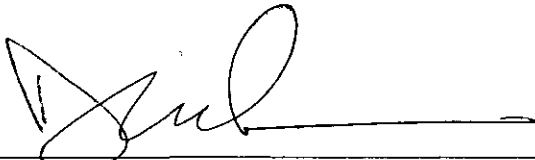


William E. Noland, Director
Finance and Management Agency

Reviewed by:
Marcia Meyers
Director of Personnel
Office of Personnel Resource Management

Prepared by:
Yvonne S. Hudson, HR Manager
Retirement and Benefits

APPROVED AND FORWARDED TO THE
FINANCE AND MANAGEMENT COMMITTEE:



OFFICE OF THE CITY ADMINISTRATOR

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FILED
OFFICE OF THE CITY
OAKLAND**OAKLAND CITY COUNCIL**
City Attorney2008 DEC -4 PM 5:09
RESOLUTION NO. _____ C.M.S.

Introduced by Councilmember _____

RESOLUTION AUTHORIZING IMPLEMENTATION OF THE PROVISIONS OF SECTION 414(h)(2) OF THE INTERNAL REVENUE CODE TO TAX DEFER MEMBER PAID CONTRIBUTIONS TO THE CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM (PERS)

WHEREAS, the City of Oakland has the authority to implement the provisions of section 414(h)(2) of the Internal Revenue Code (IRC); and

WHEREAS, the Board of Administration of the Public Employees' Retirement System adopted its resolution regarding section 414(h)(2) IRC on September 18, 1985; and

WHEREAS, the Internal Revenue Service has stated in December 1985, that the implementation of the provisions of section 414(h)(2) IRC pursuant to the Resolution of the Board of Administration would satisfy the legal requirements of section 414(h)(2) IRC; and

WHEREAS, the City of Oakland has determined that even though the implementation of the provisions of section 414(h)(2) IRC is not required by law, the tax benefit offered by section 414(h)(2) IRC should be provided to its employees who are members of the Public Employees' Retirement System; now, therefore be it

RESOLVED:

- I. That the City of Oakland will implement the provisions of section 414(h)(2) Internal Revenue Code by making employee contributions pursuant to California Government Code section 20691 to the Public Employees' Retirement System on behalf of its employees who are members of the Public Employees' Retirement System. "Employee contributions" shall mean those contributions to the Public Employees' Retirement System which are deducted from the salary of employees and are credited to individual employee's accounts pursuant to California Government Code section 20691.
- II. That the contributions made by the City of Oakland to the Public Employees' Retirement System, although designated as employee contributions, are being paid by the City of Oakland in lieu of contributions by the employees who are members of the Public Employees' Retirement System.
- III. That employees shall not have the option of choosing to receive the contributed amounts directly instead of having them paid by the City of Oakland to the Public Employees' Retirement System.

- IV. That the City of Oakland shall pay to the Public Employees' Retirement System the contributions designated as employee contributions from the same source of funds as used in paying salary.
- V. That the amount of the contributions designated as employee contributions and paid by the City of Oakland to the Public Employees' Retirement System on behalf of an employee shall be the entire contribution required of the employee by the Public Employees' Retirement Law (California Government Code sections 20000, et seq.).
- VI. That the contributions designated as employee contributions made by the City of Oakland to the Public Employees' Retirement System shall be treated for all purposes, other than taxation, in the same way that member contributions are treated by the Public Employees' Retirement System.

IN COUNCIL, OAKLAND, CALIFORNIA, _____, 20 _____

PASSED BY THE FOLLOWING VOTE:

AYES - BROOKS, BRUNNER, CHANG, KERNIGHAN, NADEL, QUAN, REID, and PRESIDENT DE LA FUENTE

NOES -

ABSENT -

ABSTENTION -

ATTEST: _____

LaTonda Simmons
City Clerk and Clerk of the Council
of the City of Oakland, California