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Payroll Concepts

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California Association of School Business Officials

PAYROLL CONCEPTS WORKSHOP

2018

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Presentation Slides

Welcome to the 2018

Payroll Concepts

CASBO Workshop
Spring 2018

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Before We Get Started

- Restroom Facilities
- Breaks
- Lunch
- Materials
- Evaluations- On Line

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Today's Covered Concepts

- 2017-18 Payroll Updates
- Employee Classifications
- Salary Computations
- Withholding Federal and State Taxes
- Paying Employees
- Employee Leaves
- Retirement System Issues

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Publications

A Copy of the Following Publications are in the back of your handout:

- Federal State Reference Guide Publication 963
- Collecting Employee Overpayments

2018 Payroll Updates

2018 Payroll Rates

- Social Security and Medicare
- State Unemployment Insurance
- California State Disability Insurance
- Pension Plan Contribution Limits
  - 403 (b) TSA's
  - 457 (b) Deferred Compensation
    - Age 50 Catch up Contribution

2018 Payroll Rates

- State Teachers Retirement System
- Public Employees Retirement System
- Federal Standard Mileage Rates
- Qualified Transportation Limits
- Advance Earned Income Credit Limitations
- Supplemental Withholding Rates

Employee Classifications SECTION TWO

Certificated

Classified

Board Members

Retirees

Is the Position Certificated or Classified?

- Certificated Service are positions which require credentials issued by the Commission on Teacher Credentialing (CTC).
- Classified service includes all positions not requiring certification qualifications with the following exceptions:

These Positions are not Classified or Certificated

- **Substitute and short term employees, employed for less than 75% (195 days) of a school year**
- **Apprentices**
- **Professional experts employed on a temporary basis for a specific project**

Education Code Sections for Employee Classifications

- **Certificated**
  - See Section 2 / Pages 2 through 7
- **Classified**
  - See Section 2 / Pages 8 through 16

Board Members

- Board Members should be paid through the payroll system
- **No** – For TSA Eligibility
- **Yes** – For 457 Plan Eligibility
- **Yes** – For Tax Withholding
  - Internal Revenue Code Sections
    - 340 2(c)and 3121 (b)(F)(iv)

Board Members

- **Yes** – For Social Security Coverage
  - Prior to July 1, 1994, Board Members were required to pay into social security under Government Code 22015 as PERS Members
  - Board Members do not qualify for PERS -- they are covered under OBRA 90 – (Not in a retirement system so they qualify for Social Security)

Board Members

- **Yes** – For Medicare Coverage
- **No** – Unemployment Insurance
- **No** – State Disability Insurance
  - (if applicable to district)

Hiring A Cal-STRS Retiree

Earnings Limitation

2017-2018: $43,755

- **A CalSTRS member who retires after January 1, 2013 must wait 6 months (180 days) before they can return to work with a CalSTRS employer.**
  - **Narrow Exemption for Distressed Schools**

Under a narrow exemption effective through June 30, 2017, if a retiree returns to work as a trustee, fiscal expert, fiscal adviser, receiver or special trustee in a position appointed by the State Superintendent of Public Instruction, County Superintendent of Schools, State Board of Education or Board of Governors of the California Community Colleges to assist schools in financial or academic distress, they may be exempt from the postretirement earnings limit.

Hiring A CalSTRS Retiree

- Employers must report retiree earnings as a retired member to CalSTRS no later than 45 days after the end of the pay period.
- Retirement benefit will be reduced dollar for dollar by any compensation earned from CalSTRS-covered employment during the first 180 calendar days following the retiree's most recent retirement effective date, up to their benefit payable during that period. This requirement also applies to Cash Balance Benefit participants who receive their retirement benefit as an annuity.
- **CalSTRS Retiree Position Limitation**
  - CalSTRS retirees are prohibited employment in a classified position while retired with the exception of employment as a Teachers Aide *(Education Code 45134-C)*

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State of California EDUCATION CODE Section 45134

- 45134. (a) Notwithstanding any other provisions of law, no minimum or maximum age limits shall be established for the employment or continuance in employment of persons as part of the classified service.
- (b) Any person possessing all of the minimum qualifications for any employment shall be eligible for appointment to that employment, and no rule or policy, either written or unwritten, heretofore or hereafter adopted, shall prohibit the employment or continued employment, solely because of the age of any person in any school employment who is otherwise qualified.
- (c) No person shall be employed in school employment while he or she is receiving a retirement allowance under any retirement system by reason of prior school employment, except that a person may be hired:
  - (1) Pursuant to Article 8 (commencing with Section 21220) of Chapter 12 of Part 3 of Division 5 of Title 2 of the Government Code.
  - (2) As an aide in one of the following circumstances:
    - (A) An aide is needed in a class with a high pupil-teacher ratio.
    - (B) An aide is needed to provide one-on-one instruction in remedial classes or for underprivileged students.
    - A person working as an aide pursuant to this subdivision shall not receive service credits for purposes of the State Teachers' Retirement System.

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State of California EDUCATION CODE Section 45134 (CONT.)

- (d) The provisions of subdivision (c) shall be inapplicable to persons who were employed in the classified service of any school district as of September 18, 1959, and who are still in the employ of the same district on the effective date of this subdivision, and the rights of those persons shall be fixed and determined as of September 18, 1959, and no such person shall be deprived of any right to any retirement allowance or eligibility for any such allowance to which he or she would have been entitled as of that date. Any such person who, by reason of any provision of law to the contrary, has been deprived of any right to retirement allowance or eligibility for such an allowance, shall, upon the filing of application therefor, be reinstated to such rights as he or she would have had had this subdivision been in effect on September 18, 1959.
- (e) This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter. (Amended by Stats. 2005, Ch. 351, Sec. 40. Effective January 1, 2006.)

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Hiring a CalPERS Retiree

Government Code Section 21224

- CalPERS retirees can be hired by the district if the retiree has the skills needed to perform work of limited duration or the employment is needed to prevent stoppage of public business.
- May be employed up to 960 hours per fiscal year for employment with all CalPERS employers combined. CalPERS considers it the equal responsibility of both the employer and retiree to ensure the retiree does not work more than 960 hours per fiscal year.
- The pay rate the retiree receives is within the pay rate range paid to other employees performing comparable duties as listed on the employer's publically available pay schedule.
- In addition to Pay Rate, the retiree cannot receive any benefit, incentive, compensation in lieu of benefits, or other form of compensation in addition to the hourly rate.

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Hiring a CalPERS Retiree

- No retirement contributions are collected or paid for employed retirees.
- All retirees hired as retired annuitants must be enrolled and their payroll reported to CalPERS.
- **Note:** A retiree can be appointed once as an interim employee to a vacant position during the recruitment for a permanent replacement. The recruitment must be "opened" and in place before the retiree is appointed. All other retired annuitant requirements apply to interim appointments.

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Hiring a CalPERS Retiree

- If the retiree is under "normal retirement age" at retirement, employment with a CalPERS employer is not allowed, even if an exception to the 180 day wait period applies, unless:
  - There must be no agreement to return to work between the member and the CalPERS employer prior to retirement and
  - There is a bona fide break in service of 60 calendar days between the retirement date and the date the retiree's employment will begin

- **All CalPERS members who retiree January 1, 2013 or later must serve a 180 days wait period between the retirement date and the first day of post retirement employment. There are certain exceptions to this wait period requirement.**

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Hiring a CalPERS Retiree

Termination of Retirement for Unlawful Employment

- Current Law Requires Reinstatement from Retirement, i.e., Termination of Retirement for ANY Violation, Minor or Major.
  - Retiree and Employer share Equal Responsibility in Preventing Violations.

Hiring a CalPERS Retiree

- CalPERS Retirees can be Employed in Other Public Retirement Systems Without Termination of Retirement, Including CalSTRS Certificated (Teaching) Positions
  - No Appointment in My|CalPERS
  - No Reporting Hours to CalPERS
  - No 180 Day Wait Period

CalPERS Retiree/Unemployment

- **CalPERS Circular Letter 200-265-05**
  - Effective January 1, 2005, a district cannot hire a retired annuitant that received unemployment compensation for prior retired annuitant employment with any public employer during the 12 month period prior to reappointment.

Salary Computations
SECTION 3

Salary Computations

- **BASE PAY RATE**
  - determined by the employee's position and step/range on a board approved salary schedule.
- **ADDITIONAL PAY**
  - Overtime, stipends, bonuses and special compensation may be paid as additional pay.

Salary Computations

- **Salary Schedules**
  - Most salary schedules should be developed outside of the payroll department in order to have true segregation of duties and strict accountability.
  - The placement of an employee on the salary schedule should also be outside of payroll.

Salary Computations
Types of Pay

- **Normal Pay**
  - Employees may be paid on a monthly, hourly or daily basis.
- **Retroactive Pay**
  - Certificated positions will require a days to days recalculation since they are paid on a daily basis.
  - Classified positions will receive an adjustment calculated on the difference of the monthly or hourly salary rate. All overtime is to be paid.

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Salary Computations
Types of Pay

- **Deferred Pay**
  - 10 or 11 Month Employees paid over 11 or 12 months after they have worked
  - Constructive Receipt Rules - the salary becomes taxable for federal and state purposes at the time the employee had an opportunity to receive it, or during the 10 or 11 months worked

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Salary Computations
Overpayments

- Overpayments to employees may be repaid by personal check, cash or payroll deductions.
- **Payroll deductions for salary overpayments may only be used if authorized by the employee,** except for recovery of payment for unearned vacation days.
  - If the employee does not authorize the deduction of the overpayment, the district can follow the appropriate legal collection procedures to obtain recovery of the funds.
- The calculation of the overpayment recovery is often complicated as the amount to be collected from the employee will depend on the tax regulations, regarding current or prior year overpayments, voluntary deduction, etc.

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Certificated Salary Computations

- Certificated employees are paid based on an annual contract and a set number of duty days.
- The duty days are tied to a salary schedule or a contract.
- Certificated employees are not provided holiday and vacation pay under the Education Code

Work Days
Certificated 12 Month Employee

CERTIFICATED

365 DAYS PER YR

-104 (SAT & SUN)

- 13 HOLIDAYS*

248 WORK DAYS

**** # of days varies per district***

Certificated Salary Computations

Ed Code 45041:

- If a Certificated employee fails to serve the full year, Education Code Section 45041 requires the employee to receive a proration of annual salary, based on days served, over the total days of required service

Certificated Salary Computations

- **Late Hires**
  - Employees hired after the beginning of the school year must have a full-time daily rate of pay calculated. This will be used to determine the first and subsequent monthly amounts to be paid over the remainder of the contract year.
  - The employee must be paid at the correct monthly rate of pay to ensure that the accurate full time equivalent (FTE) service credit is reported to CalSTRS.

Certificated Salary Computations- LATE HIRE

Step 1: **Full Time Contract Amount**

Contract Period: September 1 to June 30

Annual Base from Salary Schedule: $35,000.00
FTE (1.0 x $35,000): $35,000.00

Base Contract Days: 185
Pay Periods: 10

Monthly Pay Rate: $35,000.00 ÷ 10 months = $3,500.00

Daily Pay Rate: $35,000 ÷ 185 days = $189.19

Certificated Salary Computations- LATE HIRE

- **Step 2:** **Late Hire Monthly Calculation**

Full Time Daily Rate: $189.19
Full Time Monthly Rate: $3,500.00
Hire Date: October 7th
Work Days left in School Year: 152

LH Contract Amount: $189.19 x 152 days = $28,756.88

Future Salary Paid November to June (8 Pay Periods):
$3,500.00 x 8 = $28,000.00

Certificated Salary Computations- LATE HIRE

- **Step 3:** **1st Paycheck Adjustment – October**

***Calculate*:**

Actual Annual Contract: $28,756.88
Future Paychecks: - $28,000.00
1st Paycheck in October: $ 756.88

Certificated Salary Computations

- Change in Assignment/Contract Change
  - A change in assignment that involves a change in days, pay rate, etc., should be reported and paid separately for retirement service credit reporting to CalSTRS.
  - The number of days at each assignment must be counted. This requires an early termination calculation on the old rate and a late hire calculation on the new rate.

Work Days Classified 12 Month Employee

365 DAYS PER YR
-104 (SAT & SUN)
261 WORK DAYS

- **Classified employees are paid based on a monthly salary.**
- **Under Education Code Section 45203, all probationary and permanent employees that are a part of the classified service are entitled to holiday pay.**

Classified Salary Computations

- Classified employees are entitled to vacation pay under Education Code Section 45197 after completion of the initial probation period.
  - **When a classified employee terminates, they are entitled to a lump-sum compensation pay off for all earned and unused vacation.**
  - **If an employee was advanced vacation, the employer shall deduct the unearned days of vacation from the final pay**.

Classified Salary Computations

- **Classified Substitute, Short Term and Limited Term employees are not entitled to vacation under the education code.**
  - Districts do have an option to provide vacation pay if they so choose.

Classified Salary Computations
Daily Rate Factors

21.67	5 work days per week x 52 weeks = 260 work days per year. 260 divided by 12 months = 21.67 standard work days per month.
21.75	365 days, less 104 weekend days (52 x 2) = 261 work days per year. 261 divided by 12 months = 21.75 standard days per month.
22.00	Real work days in each month vary between: 20, 21, 22 and 23. The average is closes to 22.
Actual Days	Divide the monthly rate by the actual days in a month (least used).

Classified Salary Computations
Hourly Rate Factors

173.33	8 hours per day x 5 days per week = 40 hours per week 40 hours per week x 52 weeks = 2080 hours per year 2080 hours divided by 12 months = 173.33 standard hours per month
174.00	365 days, less 104 weekend days (52 x 2) = 261 work days per year. 261 days per year x 8 hours = 2088 hours per year 2088 hours divided by 12 months = 174 standard hours per month
176.00	If 22 days per month is standard, then 22 days per month x 8 hours per day = 176 standard hours per month

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Classified Calculation
Late Hire/Termination

- **Several factors will determine if an employee will receive a larger salary by paying for days worked as opposed to docking for days not worked.**
  - **Number of work days in the adjusted month.**
  - **The hire or term date of the employee.**
  - **The daily rate factor method being used.**

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Classified Pay Adjustments

- **<u>The main idea is to be consistent with the method your district uses for the calculation.</u>**

For example a district policy may be as follows:

- ***When a Classified Employee begins employment on the 2nd through the 15th of a month, deduct the employee for days not worked.***
- ***When a Classified Employee begins employment on the 16th through the 31st of a month, pay the employee for days worked.***
- ***For the best employee benefit, calculate both ways and give the employee the best results***

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Classified Calculation
Late Hire/Termination

Classified New Hire Effective: 6/11
21 Working Days / 12 Month Employee / Monthly salary = $1,936.00

Method 1
$1,936.00 ÷ 173.33 = $11.17 hourly rate
$11.17 hourly rate x 8 hours = $89.36 daily rate
$89.36 x 6 days not worked = $536.16
$1,936.00 - $536.16 = ***$1,399.84 June Paycheck***
Method 2
$89.36 x 15 days worked = ***$1,340.40 June Paycheck***
$1,399.84 – $1,340.40 = $59.44
****$59.44 less than Method 1 calculation****

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Overtime Pay
Who is Covered?

- Non-exempt employees as determined by the FLSA and the Education Code are covered by overtime rules.
- In general, certificated teachers, administrators, and management employees are exempt from overtime rules.
- See the "New White Collar Exemptions" table in this section

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Regulations for Overtime

- Non-Exempt Classified Employees are entitled to overtime pay based on:
  - Collective Bargaining Agreement Language;
  - Education Code Regulations
  - Federal Fair Labor Standards Act

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Classified Education Code 45128/88027

- Overtime is defined to include any time required to be worked in excess of eight hours in any one day and in excess of 40 hours in any calendar week.
- For the purpose of computing the number of hours worked, time during which an employee is excused from work because of holidays, sick leave, vacation, compensating time off, or other paid leave of absence shall be considered as time worked by the employee.

Classified Education Code 45128/88027

- **For a workday established of seven hours or more and a workweek of less than 40 hours but 35 hours or more**
  - **all time worked in excess of the established workday and workweek shall be deemed to be overtime.**

Classified Education Code 45131/88030

- Employees whose workday consists of four hours or more for not more than five consecutive working days shall be compensated for any work required to be performed **on the sixth or seventh day** following the commencement of the workweek at the rate equal to 1 1/2 times the regular rate of pay of the employee.

Classified Education Code 45131/88030

- An employee having an average workday of less than four hours during a workweek shall be compensated at a rate equal to 1 1/2 times the regular rate of pay for any work required to be performed on the **seventh day** following the commencement of his workweek.

Calculating Overtime

- **First determine the hours the employee is receiving pay for.**
- **Paid hours include hours worked and any excused paid time such as holidays, sick leave, vacation, and compensatory time taken.**

Calculating the Overtime Rate

- **Overtime is calculated based on the "Regular Rate of Pay" as defined by the Fair Labor Standards Act**
- **To arrive at the Regular Rate of Pay the formula is:**

  All Includible Compensation divided into all hours Compensated

Calculating Overtime

- On June 2, 2016, the Ninth Circuit Court of Appeals ruled that cash payments given to non exempt employees when they decline to take health and welfare benefits must be included in the regular rate of pay for the purpose of calculating the OT rate of pay.
- The regular rate of pay must include not just wages, but all other forms of compensation. Longevity payments would also be included in the regular rate of pay.
- Your district should work with your legal counsel for advice when developing your policy.

Regular Rate of Pay for Overtime Calculations

- **Regular Rate Includes**
  - Longevity payments
  - Shift Differentials
  - Bilingual Stipend
  - Non-discretionary Bonus- (An agreed upon bonus associated with measure of performance or production of work
  - Vacation, Sick Leave, Holiday or Other Excused paid absences.
  - Retroactive and Cost of Living Pay
  - Cash in Lieu
- **Regular Rate Excludes**
  - Reimbursed Expenses
  - Gifts on Certain Occasions
  - Uniform Allowances
  - Discretionary Bonus- Employer has discretion to pay and it has not been promised by a contract or other agreement

Identifying Overtime Hours Example 1

- See Section 3 Page 30
- Timecard April #1

Identifying Overtime Hours Example 2

- See Section 3 Page 31
- Timecard April #2

Identifying Overtime Hours Example 3

- See Section 3 Page 32
- Timecard April #3

Paying Overtime on Multiple Assignments

- When a non-exempt employee is paid two or more different rates for doing two or more different jobs, overtime is required to be calculated taking all jobs into consideration.

Exception – all these factors must occur:

- —The part time or secondary position is in a different capacity from the primary job and;
- —The work is performed solely at the employee's option and;
- —The work is only performed on an occasional and sporadic basis.

Handling Multiple Job Rates

- **Two Methods allowed for computing the regular rate of pay for overtime purposes**
  - **Weighted Average Method**
  - **Rate in Effect Method**
- **You can always pay overtime using the highest rate of the multiple jobs**

Handling Multiple Job Rates
Weighted Average Method

- The employee's total straight-time wages for the workweek at all applicable rates of pay are divided by the total hours worked at all jobs he performed.
  - **Employee works 33 hours at $10 per hour and 10 hours at $15 per hour.**
  - **$330.00 plus $150.00 = 480.00 divided by 43 hours worked = $11.16**
  - **$11.16 x .5 = $5.58 (additional half time premium)**
  - **$5.58 x 3 OT hours = $16.74 overtime earnings**
  - **$480.00 + $16.74 = $496.74 total weekly compensation**

Handling Multiple Job Rates
Weighted Average Method

- Employee works 33 hours at $10 per hour and 10 hours at $15 per hour and receives $500.00 per month for **cash in lieu of benefits**
- Step one: $330.00 + $150.00 = $480.00
- Step two: $500.00 x 12 months = $6,000.00/52 weeks = $115.38
- Step three: $480.00 + $115.38 = $595.38/43 hour =$13.85 regular rate of pay for week
- Step four: $13.85 x .50 = $6.92 (additional half time premium)
- Step six: 3 (overtime hours) x $6.92 = $20.76 overtime pay due to employee
- Step seven: $480.00 + $20.76 = $506.76 Total Weekly Compensation

Handling Multiple Job Rates

An employer and employee can mutually agree to compensate for the overtime based on the rate of the job the overtime was earned if;

- **The employee's straight-time average hourly earnings for the workweek must at least equal minimum wage.**
- **There must be an individual or collective agreement between the employer and employee to pay this method. (This should be in writing)**

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Handling Multiple Rates
Rate in Effect Method

- **The overtime hours for which the overtime rate is paid must qualify as overtime hours under FLSA**
- **The number of overtime hours paid must equal or exceed the number of overtime hours worked**

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Handling Multiple Rates
Rate in Effect Method

- Employer must maintain records showing the date of the agreement and the period it covers and which employees (or group of employees) is covered.
- All of the above must apply in order to use this method.

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Pay Deductions
SECTION 4

Pay Deductions

- Voluntary Deductions
  - Insurance premiums
  - Credit union
  - 403(b) and 457(b)
  - Section 125 Plan
  - Savings bonds
  - Charitable contributions
  - Association dues
  - Union dues
  - Income protection plans

Pay Deductions

- Statutory Deductions
  - Federal and state income taxes
  - State Disability
  - Social Security/Medicare
  - CalSTRS or CalPERS
  - Alternative retirement systems
  - Union Dues for employees covered under collective bargaining

Pay Deductions

- Involuntary Deductions
  - IRS Levies
  - Franchise Tax Board Levies
  - Child Support and Spousal Support Orders
  - Medical Support Orders
  - Student Loans
  - DMV
  - Creditor Garnishments
  - Administrative Wage Garnishments
  - You can not discharge an employee because of garnishment.

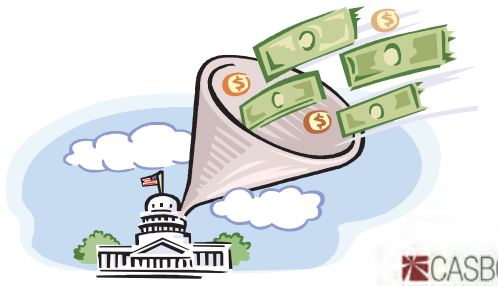
Pay Deductions

- Payroll Deductions for Money Owed To The Employer
  - Required to do so by state or federal law
  - Deduction is expressly authorized in writing
  - When a deduction to cover health, welfare or pension contributions is expressly authorized by a wage or collective bargaining agreement.

Pay Deductions

- Payroll Deductions For Money Owed To The Employer
  - Restrictions on collecting overpayments from employees
    - Labor Code 224
    - CSEA v. State of California

Withholding Federal and State Taxes SECTION 5



Form W-4

- The employer should have on file a signed Form W-4 for all newly hired employees on or before the first day of employment.
- The form is effective with the employee's first pay period.
- If a new employee fails to submit a Form W-4, the employer is required to withhold at Single and 0 exemptions.

Form W-4

- A Form W-4 remains in effect until the employee submits a new form.
- An exception would be employees who claim exempt from federal income tax withholding which requires the filing of a new Form W-4 no later than February 15 each year.
- Revised Forms W-4 are to be in effect no later than the beginning of the first payroll period that ends on or after the 30th day the revision is received.

Invalid Forms W-4

- Employers have a responsibility not to accept and withhold on any invalid Forms W-4.
- A Form W-4 is invalid when:
  - The language or format of the form has been altered including additions and deletions
  - The form is not signed or completed properly
  - The employee indicates to the employer that the information on the form is incorrect
  - A flat dollar amount or percentage is requested for withholding.

Invalid Forms W-4

- If the employee fails to submit a new form, withholding must be
  - based on the employee's last valid Form W-4.
  - When a previous Form W-4 does not exist, the employer is required to withhold on the employee as single with no allowances.

Employer Reporting Requirements on Form W-4

- Effective April 14, 2005, employers are not required to send the IRS Forms W-4 that show withholding of more than 10 allowances or that show an exempt filing unless requested by the IRS in writing.

IRS Notice to the Employer (the "Lock-in Letter")

- Employers may receive a notice from the IRS (commonly referred to as a "lock-in letter") specifying the maximum number of withholding exemptions permitted for a specific employee

Employer Reporting Requirements on Form W-4

- Lock-in letters are to take effect no earlier than the first pay period beginning at least 60 days after the date of the letter.
- During this period, the employee can challenge the lock-in letter directly to the IRS.
- If the employee gives a new Form W-4 to the employer, the employer should disregard it until notified by the IRS to withhold based on that form.

Employer Reporting Requirements on Form W-4

- In addition to the lock-in letter, the IRS will provide the employer with an "employee notice" (the IRS will also mail a similar notice to the employee's last known address).
  - Send to employee within 10 business days of receipt.
- If the employee is no longer employed by the employer, the employer must send a written response stating that fact to the IRS office designated in the notice.

Rules for Withholding on Non-Resident Aliens

- IRS has issued rules for determining the amount employers must withhold from nonresident alien employees' wages for services performed in the U.S. and for how nonresident alien employees complete Form W-4.
- See Section 5 / Pages 4 through 5

Social Security & Medicare Coverage

Employees may be covered under Social Security and/or Medicare by the following federal actions:

- Voluntary Section 218 Agreements
- COBRA 1986- Medicare Coverage
- OBRA 1990- Social Security Coverage of Employees Not Covered By a Pension.

Social Security/Medicare Coverage

- Prior to OBRA 1990, State & Local Government Employees were only covered by Social Security if they were under a state voluntary Section 218 Agreement.
- For School Employers, PERS is the State Social Security Administrator

OBRA 90

Required that services performed by a state and local government employee will be covered under Social Security or a public retirement plan providing meaningful benefits.

- Define Contribution Plans generally qualify as a retirement plan if an allocation of contribution is equal to 7 ½ % of the employee's compensation
- The 7 ½ % can be any combination between employee and employer as to who pays what %.

Result of OBRA 90

- If An Employee is not a member of STRS/PERS or Alternative Retirement System the Employee Must Be In Social Security.
- If the Employee's Position is covered under a Section 218 Agreement they must also be in Social Security even if in a Retirement System.

COBRA 1985 Medicare Coverage

- Mandated Mandatory Medicare coverage if hired after March 31, 1986
- Employee also covered under Medicare if
  - Qualified under OBRA 90 or
  - Special Section 218 Election

Social Security and Medicare Coverage for Retirees

- All retirees hired after March 31, 1986 are subject to Medicare tax withholding regardless of their age.
  - The withholding tax applies even if they are eligible to receive Medicare benefits while working.
- OBRA '90 specifically excludes a qualified retired annuitant from mandatory social security coverage if they are rehired with an employer that participates in the same retirement plan from which they retired.

K-12 Students

- Exempt from SS/Medi coverage if their services are performed in an educational institution where they are enrolled and regularly attending classes.
- The service must be performed concurrently with attending classes.

Community College Students

Internal Revenue Procedure 98-16 states that the student must be attending classes at least on a half-time basis of what is required of a full time student.

Social Security Form SSA-1945

- Effective January 1, 2005
- Send Copy to the Applicable Retirement System
  - STRS & PERS & Alternative Retirement Systems - employees hired beginning January 1, 2005 who are covered under these system and do not pay into Social Security.
  - SEE FORM in this section

Social Security Form SSA-1945

- **Who Is Exempt from Completing the Form SSA-1945?**
  - Employees hired before January 1, 2005.
  - Employees who contribute into Social Security through their employment with the school district.
  - Students who do not pay into Social Security.

Social Security/Medicare Tax Issues

- IRS Answers Questions on Public Employer Social Security/Medicare Tax Issues
  - See Section 5 / Pages 26 through 28

State Form DE-4

- **Form DE-4 Employee Withholding Allowance Certificate**
  - **Employee must complete the DE-4 for state tax withholding if he/she wants the number of allowances for California personal income tax withholding to be different from the number of allowances claimed for federal income tax withholding purposes.**

State Form DE-4 ATTENTION: CHANGE

The reporting of the certificates to the Internal Revenue Service (IRS) shall satisfy state reporting requirements. A federal determination that a withholding exemption certificate is invalid or incorrect shall also be effective for state withholding purposes. Thus, if you are instructed by the IRS to withhold as though an employee were a single person claiming no exemptions, then you must do likewise for state withholding purposes. If the IRS specifies marital status and the permissible number of exemptions an employee may claim, such a federal determination shall also be effective for state withholding purposes.

Page 14 of DE44 Employers Guide

State Unemployment Insurance

- State unemployment contributions are paid by the employer and not withheld from the employee.
- Schools do not pay into the Federal Unemployment System and do not file IRS Form 940.
- The Unemployment Rate is determined in accordance with the rate formula specified by Section 823(b) of the California Unemployment Insurance Code. The rate for all participants of the School Employees Fund is established annually.

State Unemployment Insurance

- The schools regular unemployment insurance rate applies to all employee's wages except the following:
- Board members
- Elected Officials
- Students who are enrolled and are regularly attending classes at the school district, college or university where they are employed
- Students under 22 years of age enrolled in a non-profit or public educational institution in a program, which combines academic instruction with work experience

State Disability Insurance

- School districts are not required by the state to cover their employees or offer state disability insurance
- SDI coverage may be available to district employees whose bargaining unit has negotiated the benefit or provides it as a district benefit for employees.
- Before districts can offer SDI coverage, an application has to be completed and filed with the Employment Development Department for an identification number.

State Disability Insurance

- **Who Pays SDI?**
  - **Employees pay for disability insurance and its administration.**
  - **Some employers may be paying the SDI tax for their employees.**
  - **For 2018 the SDI tax rate is 1.0 percent of wages up to $114,967.00.**

Calculating Taxes

- For Federal and State Income Taxes, Wages become taxable when they are paid, not when they are earned.
- Wages are considered paid when the employee receives the paycheck or when it is constructively received.
- When the money is made available to the employee (payday) it is then considered constructively received.

Taxable Income

When employees contribute to certain benefits and voluntary deductions with "pretax" dollars, the contribution reduces taxable wages.

PRE-TAX DEDUCTION	FEDERAL WAGE REDUCTIONS	STATE WAGE REDUCTIONS	SOCIAL SECURITY /MEDICARE WAGE REDUCTIONS
CalSTRS	YES	YES	NO
CalPERS	YES	YES	NO
Qualified Alternative Retirement Plan	YES	YES	NO
403 (b) & 457 (b)	YES	YES	NO
Café. Section 125	YES	YES	YES
Ca. Qualified Ride Share	NO	YES	NO

Calculating Taxes

- Calculating the withholding of taxes is done by determining the taxable wages and using the applicable tax charts provided by the IRS (federal) and the Employment Development Department (state taxes).
- The method most commonly used by school districts in computerized payroll systems is the Percentage Method based on the annual tax rate chart.

Calculating Taxes

- In order to calculate withholding taxes employers need to know
  - Taxable Income
  - Pay Frequency
  - W-4/ DE 4 Status
- Payroll staff should understand how to manually calculate tax withholding.

Calculating Federal W/H

FEDERAL CALCULATION EXAMPLE

- Monthly Salary: $6,301.42
- Pay Frequency: 12 months/ Monthly pay
- W-4 Status Married, 1
- CalSTRS $504.11
- TSA $308.00
- Caf/125 $156.70

Calculating Federal W/H

- $6,301.42 (monthly salary) – $504.11 (CalSTRS) – $308.00 (TSA) – $156.70 (Sec. 125) = $5,332.61 (monthly taxable earnings)
- $5,332.61 (monthly taxable earnings) x 12 (pay frequency) = $63,991.32 (annual taxable earnings)
- **Now Go to Tax Chart**

Calculating Federal W/H

- $63,991.32 (annual taxable earnings) - $4,150.00 (one W-4 exemption) = $59,841.32 (adjusted wages)
- $59,841.32 (adjusted wages) – $30,600.00(excess over from tax chart) = $29,241.32 (excess amount)
- **$1,905.00** (amount of tax) + ($29,241.32 x 12% = $**3,508.96**) = $5,413.96 (total annual withholding)
- $5,413.96 (total annual withholding) ÷ 12 months = **$451.16 (pay period taxes)**.

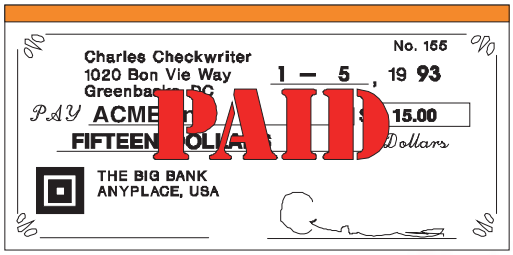
Supplemental Tax Withholding

- For 2018 the federal supplemental tax rate is 22%
- California supplemental tax rate is 6.6% and 10.23% on bonuses.
- Used for supplemental wages only.

Supplemental Tax Withholding

- Examples of supplemental wages include:
  - Retroactive wage increases
  - Bonuses, prizes, and awards
  - Severance or dismissal pay
  - Overtime pay
  - Reimbursement for nondeductible moving expenses
  - Payment for unused, accumulated sick leave or vacation payoff

Paying Employees
SECTION 6



Paying Employees

- State laws control how and when employees are paid
  - Direct Deposit is allowed but cannot be mandated under California law
  - Ca. Labor Code regulates requirements for paycheck information to employees
  - Education Code regulations time of payments for school districts.

Direct Deposit

- Employees authorize electronic payments to be credited to their bank accounts on payday.
- Employers originate the electronic payment entries for the payment system through a financial institution known as the Originating Depository Financial Institution (ODFI).
- Automated Clearing House (ACH) is the central clearing facility that distributes the entries to the receiving financial institutions. It also performs the required settlement functions.
- Receiving depository financial institutions (RDFI) receive the individual transactions and post the funds to the accounts of depositors (employees).

Direct Deposit

- Employee authorization does not have to be in writing but is recommended to provide recovering funds in the event of overpayments.
- The authorization form should provide the following information:
  - The employee's bank routing number
  - The type of account (checking/share draft/ or savings)
  - The account number

Direct Deposit Authorizations

- The most accurate way to receive information is to have the employee attach a cancelled check to an authorization form.
  - Savings account slips are not recommended as they may not provide accurate information for direct deposit purposes.
- The authorization form should also include information about termination procedures and effective dates for implementing the direct deposit.
  - Also include language that indicates the employee understands procedures for recovering errors or overpayments into their account.

Direct Deposit Prenotification

- No longer required but recommended.
- Can be done on same file as regular deposits
- If the pre-notification is not returned to the employer within 6 banking days, the first live payroll entry can be processed for deposit.

Direct Deposit Corrections

- If a mistake is made, employers can generate a "single entry reversal" through ACH within five banking days from the settlement date of the original direct deposit.

Handling Missing Deposits

- Assure the employee that their money is safe and the issue will be resolved.
- Ask the employee if they are basing not seeing their deposit on information obtained from the ATM machine.
  - Direct deposits may not have yet been posted for ATM purposes by the employee's financial institution.
  - Ask the employee to contact their banking representative to see if their deposit has been credited to their account.

Handling Missing Deposits

- If the employee's financial institution did not receive the deposit verify the account number with the employee.
- Check the RDFI's routing number and inquire into any possible mergers that may have occurred.
- If a solution still has not been found, contact the ODFI financial institution and speak to your contact representative.

Pay Statements

- **California Labor Code Section 226**
  - Effective January 1, 2008 you can use no more than the last four digits of the employees SSN on the document
  - You can use an employee ID number instead of SSN
- **AB 1522**
  - Requires that Sick Leave information is given with pay statements states that if you give a check stub or pay statement to an employee

Time of Payments

Certificated Payments
EC 45048 & 45049

SALARY TYPES	PAYMENT SCHEDULE
Monthly Contract & Substitute Certificated Employees (EC 45048)	Shall be paid on the last working day of the current month; no later than the fifth (5th) calendar day of the succeeding month.
Monthly Part-time Adult School Employees (EC 45048)	Shall be paid on or before the tenth (10th) of the following month.
Extra Assignments based on: Hourly, Daily, Monthly, Biweekly, Semimonthly, or Once Every Four (4) Weeks (EC 45049)	For performing teaching (including summer school) or other services outside normal teaching duties; shall be paid within ten (10) calendar days after the end of each calendar month or pay period during which services are performed.
Extra Assignments based on: Lump-Sum Payments (EC 45049)	Shall be paid within ten (10) days after termination of the services. (Assignment completion date)

Certificated Payments
EC 45048 & 45049

SALARY TYPES	PAYMENT SCHEDULE
Retroactive Pay Increases (EC 45049)	Salary changes shall be made no later than three (3) regular pay periods or three (3) months, whichever is longer, after the date the agreement is ratified. Retroactive payments must be paid within twenty (20) business days of the date employees actually receive the salary increases.
Column Movement (EC 45049)	Salary changes shall be made no later than three (3) regular pay periods or three (3) months, whichever is longer after the employee files proper documentation.

Certificated Payments
EC 42646

PAYMENT SCHEDULE	ISSUES TO ADDRESS
Issue date shall be on or before the 10th calendar day following the end of the payroll period. If employee is paid once a month, payment is due on the last working day of the month	Payroll Periods may be established by County Offices. Can be used in place of Education Code 45048

Classified Salary Payments
EC 45166, 42644, 42646

SALARY TYPES	PAYMENT SCHEDULE
All Classified Employees (EC 45166) K-12 (EC 88165) Comm. College	Shall be paid on the last working day of the current month which the employee was in paid status
Full-time Classified Employees (EC 42644) K-12 (EC 85244) Comm. College	Labor performed between the 1st and 15th shall be paid between the 16th and 26th day of the month during which the labor was performed; labor performed between the 16th and last day of the month shall be paid between the 1st and 10th day of the following month
Alternative Payroll Procedure (EC 42646) K-12 (EC 85260) Comm. College	Issue date shall be on or before the 10th calendar day following the end of the payroll period. If employee is paid once a month, payment is due on the last working day of the month
Error In Salary (EC 45167) K-12 (EC 88166) Comm. College	Supplemental payment shall be made within 5 workdays of time error was discovered

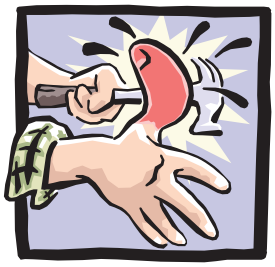
Paying Terminating Employees

- California Labor Code Section 220 **exempts** school districts and community colleges from California Labor Code 201 which provides for immediate payment of terminated employees by California employers.
- Terminated school employees may be paid their final pay on the next scheduled payroll cycle.

Classified Errors in Salary

- **Education Code 45167**. Whenever it is determined that an error has been made in the calculation or reporting in any classified employee payroll or in the payment of any classified employee's salary, the appointing authority shall, within five workdays following such determination, provide the employee with a statement of the correction and a supplemental payment drawn against any available funds.

Illness / Injury Leaves



The following slides illustrate how to use an employee's sick and differential leave for an employee who is not on Worker's Compensation Leave.

Leaves of Absence

- Pregnancy Disability Leave Act
  - California Government Code Section 12945
- **California Family Rights Act**
  - **California Govt Code Section 12945.2**
- Parental Leave
  - California AB2393 effective 1/1/17
- Using Sick Leave for Family Care
  - California Labor Code Section 233

Leaves of Absence

- FMLA Family Medical Leave Act
- FMLA for members of the Armed Forces.
- California AB392
  - Effective 10-9-2007 10 days of unpaid leave for family members
- California AB1522 Sick leave for All
  - Effective 1/1/15, Right to accrue and take sick leave effective 7/1/15 FAQ's available @ dir.ca.gov/dlse

Certificated Illness Leave
5 School Months at 50% Sick Pay

Education Code 44983/87788

- 5 School Months Begin
- Use Accumulated Sick Leave
- 50% pay for balance of 5 school month period.

- Court cases have stood that Ed. Code 44983/87786 allows employees to receive a new five month period each fiscal year, even for the same illness or injury

Certificated Illness Leave Sub Pay Deduct

Education Code 44977

- Use Accumulated Sick Leave
- 5 School Months Begin
- Sub Pay Deduction for a 5 month period per illness and/or injury.
  - (five school months includes holidays but not summer and off-track periods)
- An employee shall not be provided more than one five month period per illness and/or injury.
- Balance may be used in next school year for same illness and/or injury.

Certificated Illness Leave Sub Pay Deduct – Community College

Education Code 87780

- 5 School Months Begin
- Use Accumulated Sick Leave
- Sub pay deduction for balance of 5 school month period.

Classified Illness Leave 5 Months Sub Pay Deduct

- **Education Code 45196/88196**
- BEGIN 5 CALENDAR MONTH
  - Use Accumulated Sick Leave
  - Use Accrued Compensatory Time
  - Use Vacation Leave
- Employee is entitled to salary less amount paid to a substitute if a substitute is hired.

Classified Illness Leave
100 Days at 50% Pay

Education Code 45196/88196

- Employee Is Entitled To 100 Working Days Of 50% Sick Pay Each Fiscal Year
  - **100 Days Start**
  - **Use Accumulated Sick Leave**
  - **50% pay for balance of 100 day period**

Re-Employment Lists

- K-12 Certificated – Education Code 44878.1
  - Provides for re-employment list of 39 months for a status teachers and 24 months for probationary teachers.
- Community College Academic Employees do not have an Education Code that address what the next step is

Re-Employment Lists

- Classified Education Codes 45195-88185
- Provides that once a classified employee exhausts all paid leave, they may apply for additional paid or unpaid leave not to exceed 6 months.
- Once all leaves have been exhausted the employee is placed on a 39 month rehire list.

WORKERS COMPENSATION LEAVES

- Certificated --EC 44984/87783
- Classified -- EC 45192/88192
  - Provides 60 Working Days Of Full Pay
  - The 60 working days are paid before going into an employee's sick and differential leave
  - 60 Days Is Per Injury/Illness
  - Benefit is Non-Taxable

Certificated – 5 School Months -50% Sick Pay Education Code 44983/87788

- 60 Days Worker Comp Pay
- 5 SCHOOL MONTHS BEGIN
- Use Accumulated Sick Leave
- Balance of 5 School Months is at 50% Pay

Certificated Community College – Sub Pay Deduct - Education Code 87780

- 60 Days Workers Comp Pay
- 5 School Months Begin
- Use Accumulated Sick Leave
- Sub Pay Deduction for Balance of 5 School Month Period

Certificated K-12 Sub Pay Deduct Education Code 44977

- 60 Days Workers Comp Pay
- Use Accumulated Sick Leave
- 5 School Months Begin
- Sub Pay Deduction for a five-month period per illness/injury
- An employee shall not be provided more than one 5 month period per illness/injury.
- Balance may be used in the next year for same illness/injury.

Classified Leave- 50% Sick Pay Rule Education Code 45196/88196

- 60 Days of Worker's Comp Pay
- 100 Days Start
- Use Accumulated Sick Leave
- 50% pay for balance of 100 day period
  - Holidays & Other Paid Leave excluded in 100 Days

Classified Leave – 5 Calendar Month Education 45196/88196

- Begin 5 Calendar Month
- 60 Day Worker's Comp Leave
- Use Accumulated Sick Leave
- Use Accrued Compensatory Time
- Use Vacation Leave
- The employee is entitled to salary less amount paid to a substitute *if a substitute is hired*

Workers Compensation Leaves

- Workers' Compensation Abatements
  - Using a third party, such as a claim adjuster

CASBO

INFLATED SICK LEAVE

- **Calculate Inflated Sick Leave when**:
  - **An Employee Has Exhausted 60 Days Workers Compensation Leave and Begins to Use Sick Leave**
  - **and the District Is Recovering the Payment for Workers Compensation Claims on Behalf of Employee**

CASBO

EXAMPLE OF SICK LEAVE ADJUSTMENT

- Employee Daily Rate $ 126.00
- W/C Daily Rate - 55.00
- Adjusted Value of Sick Leave $ 71.00

Sick Leave Adjustment

$71.00

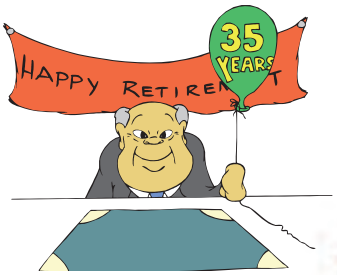
$126.00 =56%

CASBO

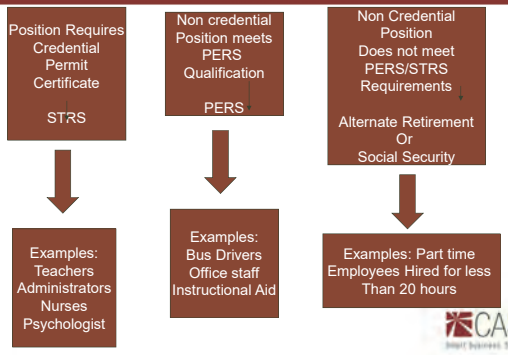
Sick Leave Adjustment

- The Sick Leave Can Be Adjusted By Inflating the Leave Balance
- Employee Has A Balance of 16 Days Of Sick Leave
- 16 Days Divided By 56% = 29 Days Of Adjusted Sick Leave to track
- **See Calculation Worksheet Form – Page 31**

State Retirement Issues
SECTION 8



Which System?



PERS/STRS Retirement Systems

Defined Benefit Plan (DB) – promised benefit based on the following factors

Formula using

1. Age at time of retirement
2. Years of Service
3. Final Compensation level based on retirement tier

Note: DB plan is different than Defined Contribution (DC) plans like 457 (b) and 403(b) Plans

Retirement Contributions

- Member Contributions

  CalSTRS

  2% @ 60 10.25%

  2% @ 62 9.205% (PEPRA)

  DBS 8%

  CalPERS

  Classic Members 7%

  New Members 6.5% (PEPRA)

Retirement Contributions

- **District Contributions**
  - **14.43% for STRS**
  - **14.43% for STRS Reduced Workload**
  - **8.25% for DBS**

  - **15.531% for PERS**
  - PERS rate changes every fiscal year based on Actuarial assessment – PERS rate is a employer pool rate

CalSTRS COMPENSATION CAP

Section 401(a)(17) of the IRC provides earnings limits on annual compensation for some 2% at 60.

For 2017-2018 the CalSTRS Compensation Cap for CalSTRS 2% at 60 Members who became a CalSTRS DB member or CB participant on or after July 1, 1996-Employee portion only is $270,000.00

CalSTRS COMPENSATION CAP

Compensation Cap for CalSTRS 2% at 62-Employee portion only

- Chapter 296 added section 7522.10 to the Government Code, which establishes a limit on compensation used to calculate benefits for CalSTRS 2% at 62, including compensation credited to the DBS Program. For CalSTRS 2% at 62, the cap on compensation is equal to 120 percent of the 2013 Social Security wage base and will be adjusted annually based on changes to the Consumer Price Index for All Urban Consumers.
- From July 1, 2017 to June 30, 2018, the compensation cap for CalSTRS 2% at 62 is $143,082.

CalSTRS Membership Qualifications

As of January 1, 2013 under the Public Employees' Pension Reform Act of 2013 (**PEPRA**) employees who performed creditable service for CalSTRS prior to 1/1/2013 are considered 2% at 60 and employees who performed creditable service for CalSTRS after 1/1/2013 are considered 2% at 62.

- **Full-Time 100% Contract** Qualifies Immediately at Start of Contract
- **Part-Time 50%-99%** Qualifies 2nd Pay Period from Hire
- **Substitute-Long Term/Daily/Hourly**
  - Qualifies After 100 Days/600 Hrs.
  - Qualifies 1st of Following Pay Period
  - Qualifies With A Single District

CalSTRS Membership Qualifications

- Ed Code 22504
- Employed to Provide Creditable Service on a part time basis
  - Qualifies After 60 Hours/10 Days
  - Qualifies First of Following Pay Period
  - Qualifies With A Single District

If Funds are on deposit with STRS from previous employment – Compulsory membership regardless of the type of employment less than half time*

CalSTRS Membership Qualifications

- Retirement Qualification Rules – page 9

CalSTRS Membership Qualifications

- Permissive Election
  - Effective the Pay Period Following the Employee's Signature. (effective 1/1/17)
  - Due to CalSTRS Within 30 Days from Employee's Signature. (effective 1/1/17)
  - **Use ES 350 Form for Election**

Qualifying Elections

- CalSTRS Member Qualifying for Classified Position
  - 60 Days to Elect to stay in STRS
- CalPERS member Qualifying for a Certificated Position
  - 60 Days to Elect to stay in CalPERS
  - **USE FORM ES-372 FOR ELECTION**

Form ES 372 "Right to Elections"

- Education Code 22509 Districts are required to ensure that employees have been given the form within 10 working days of hire.
- It is recommended that districts retain the written acknowledgement from employees that they have been advised and given Form 372.
  - This has been a common audit finding by CalSTRS.
  - Due to Retirement Systems Within 30 Days from Employee's Signature (effective 1/1/17)

Certificated Retirement Scenarios

- For examples see various Certificated Retirement Scenarios Section 8 / Pages 11 through 16

STRS Creditable Compensation
Education Code Section 22119.5

- Contributions on service in excess of one year will be creditable to the Define Benefit Supplemental (DBS) program and not used in the calculation of compensation earnable for final compensation purposes.
- Non Creditable Compensation if:
  - Position is not eligible for state apportionment **and**
  - Position does not require credential, certificate or permit from the Commission on Teacher Credentialing (CTC) **or**
  - Is not activities related to, and an outgrowth of the instructional and guidance program of CA Public Schools when performed for the same employer for which the member is performing creditable service.
  - Position does not meet community college standards

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STRS Creditable Compensation
CA Code of Regulations 27401

- Possession or Attainment of a Certificate, License, Special Credential or Advanced Degree
- Career or Service Longevity
- Hiring, Transfer or Retirement (incentive)
- Employment in a Position that is Hazardous or Difficult to Staff
- Employment in an Assignment in which the Number of Students Enrolled Exceeds the Contractual Amount.
- Achievement of a Performance Benchmark
- Compensation that is paid Contingent upon Availability of Funds.

CASBO

STRS Creditable Compensation
CA Code of Regulations 27401

- Remuneration That is Paid in Addition to Salary
  - Paid in Cash in Accordance with Publicly Available Written Agreement
  - Not Associated with the Performance of Additional Service
  - Paid to entire Class of Employees
    - In the same dollar amount, same percentage of salary or same percentage of amount being distributed

CASBO

STRS Creditable Compensation
CA Code of Regulations 27401

- Remuneration in addition to Salary Does Not Include the Following:
  - Cash paid by an employer to an employee who receives cash in lieu of a fringe benefit, or cash in lieu of an expense paid or reimbursed by the employer
  - Cash paid by an employer on behalf of an employee for a fringe benefit, expense or reimbursement
  - Cash paid by an employer to an employee that is the remainder from money allocated for fringe benefits or expenses that are paid by the employer

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STRS Creditable Compensation
Education Code Section 22119.3

- Creditable Compensation for members who are subject to the California Public Employees' Pension Reform Act of 2013
  - Remuneration that is paid **Each Pay Period** in which **Creditable Service is Performed for That Position**
  - Shall be paid in Cash by an employer to All Persons in the same class in accordance with a publicly available written contractual agreement…..
  - Does **Not** Include any One-Time or Ad Hoc Payments made to a member

CASBO

STRS Service Credit

- STRS service credit is calculated by STRS by dividing earnings by Pay Rates of pay lines reported as code "01" and "03"

Pay Rate: $3000.00 Earnings: $3000.00
Service dates: 3/1/2017 – 3/31/2017
Service Credit = $3000/$3000 = 1 Month

CASBO

CalSTRS and Temp Agency/ 3rd Party Work

- Earnings that are subject to Creditable Compensation are Required to be Reported if Retired from CalSTRS
- Earnings Limit is Applicable for this work

CalPERS Membership

Qualify If:

As of January 1, 2013 under the Public Employees' Pension Reform Act of 2013 (**PEPRA**) employees who were members of CalPERS or a reciprocal system prior to 1/1/2013 are considered Classic Members and employees who become members of CalPERS for the first time after 1/1/2013 are considered New Members.

- Permanent Full-Time (40 hours per week)
- Part-Time averaging at least 20 hours per week, for at last one year
- Full-time for a temporary appointment in excess of 6 months
- Currently a member of CalPERS- including membership established with another CalPERS agency

CalPERS Membership

- **CLASSIC VS. PEPRA NEW MEMBER SCHOOL SCENARIOS** – see attachment at the end of chapter.

CalPERS Membership

- Temporary, seasonal, on call, emergency, substitute, or irregular basis
  - Qualifies When Worked 1000 Hours or 125 days in a Fiscal Year
  - Overtime Hours Are Included for Qualifying Purposes
  - Work for All Divisions within the County are included for Qualifying Purposes
  - If they qualify in June enroll in membership

CalPERS and Temp Agency Work-Cir 200-065-14

- Temporary employees hired through a staffing or 3rd party agency and you have the right to control and direct their daily duties.
- Must Monitor for Membership Qualifications
- Report Earnings Based on a Publicly Available Salary Schedule for Members and Retired Annuitants
- Time Worked is Eligible for Purchase as Service Prior to Membership
- These employees are most likely considered employees of your agency and must be treated as if they were directly hired by your agency

CalPERS Membership-Reciprocity

Member Reciprocal Self-Certification Form (PERS-CASD-801)

This form is for employers to use to identify if new employees are classic members due to reciprocity. Employers need to properly identify the status of members at the time of hire.

See attached Circular Letter 200-063-12

CalPERS Membership-Reciprocity

- Reciprocity is an agreement among California Public Retirement Systems to allow members to move from one public employer to another within a specific time limit without losing some valuable retirement and related benefit rights.
- There is no transfer of funds or service credit between retirement systems when an employee establishes reciprocity. They become a member of both systems and are subject to the membership and benefit obligations and rights of each system (for example, minimum retirement age may vary between systems).
- Employees must retire on the same date from each public retirement system participating in a reciprocal agreement for all benefits of reciprocity to apply. Employees will receive a retirement check from both systems when they retire.
- Both systems will use the highest compensation earnable under any system in computing final compensation if retirement from all systems is concurrent.

CASBO

CalPERS Membership-Reciprocity

- As a result of PEPRA, effective January 1, 2013, CalPERS will consider movement between California Public Retirement Systems that are subject to reciprocity when they determine which benefit formula applies to our employees and they may be a Classic Member 2% @ 55 instead of a New Member 2% @ 62. This does not apply to CalSTRS.
- When an employee is hired into a CalPERS covered position they need to be asked if they are a member of another California Public Retirement System.
- There is no reciprocity established between CalPERS and CalSTRS, but there is an agreement with CalSTRS to provide similar benefits.
- For more information see CalPERS Publication 15, When You Change Retirement Systems

CASBO

CalPERS Membership Exclusions

- Independent Contractors
- Elected or appointed officers (effective July 1, 1994)
- Students employed by a school district they attend in a position established for students only

CASBO

CalPERS Compensation

- Pay Rate - a member's normal monthly rate of pay or base pay.
  - Report as earned according to the job classification,
  - Must be reflected in a publicly available pay schedule or bargaining unit agreement.

CalPERS Compensation

- Requirement For a Publicly Available Pay Schedule (CCR 570.5)
  - Has been duly approved and adopted by the employer's governing body in accordance with requirements of applicable public meeting laws.
  - Identifies the position title for every employee position
  - Shows the pay rate for each position
  - Indicates the time base for each pay rate
  - Indicates an effective date and date of any revisions
  - Schedule is publicly available and does not reference another document
  - Retained for 5 years

CalPERS Compensation Cap

Section 401(a)(17) of the IRC provides earnings limits on annual compensation for some 2% at 55 CalPERS Members.

The compensation cap for CalPERS Classic Members who became a CalPERS DB participant on or after July 1, 1996-Employee portion only is $275,000.00.

CalPERS Compensation Cap

Compensation Cap for CalPERS New Members- Employee portion only

For New Members who participate in Social Security, compensation is capped at the Social Security Wage Base. For 2018 the compensation cap is $121,388.

For New Members who do not participate in Social Security, compensation is capped at 120% of the Social Security Wage Base. For 2018 the compensation cap is $145,666.

CalPERS Special Compensation

- Special Compensation – Additional pay that an employee receives for special skills or knowledge.
  - Limited to what is indicated by a labor policy or agreement to similarly situated members of a group or class of employment.
  - Reported in addition to and separately from pay rate.
  - Reported in Pay Periods when earned.

Reportable Special Compensation Cal. Code of Regulations 571 (a)

- Incentive pay – includes bonus pay and longevity
- Educational pay – includes educational incentive pay but not cost of tuition, books, or registrations
- Premium/Temporary Upgrade pay (only applies to Classic Members)- includes working out of class pay

Reportable Special Compensation
Cal. Code of Regulations 571 (a)

- Holiday Pay- when employees are required to work during scheduled holidays and paid over and above the normal salary.

Reportable Special Compensation
Cal. Code of Regulations 571 (a)

- Uniform Allowances (only applies to Classic Members) - Compensation paid or reimbursed for the monetary value of purchasing, renting and maintaining required clothing
  - Clothing must be a substitute for personal attire clothing (per IRS definition)
  - Excludes items considered safety equipment such as protective vests, pistols, bullets, and steel-toed boots

Non-Reportable Compensation

- Automobile Allowance
- Overtime
- Cafeteria Plans

Reporting CalPERS Overtime Government Code 20635.1

- Circular Letter #200-211-05 "Proper Reporting of Overtime Pay Rates for School Members"
- Employees paid "overtime" rates for hours between "full-time" and 40 hours/week
  - Report "straight-time" rate
  - Report "straight-time" earnings

CASBO

CalPERS Service Credit

- A member in **full-time** employment will be credited one year of service credit
  - 10 Months of Work
  - 215 Days of Work
  - 1,720 Hours of Work in fiscal year
- SERVICE CREDIT= EARNINGS ÷ PAYRATE FOR EACH SERVICE PERIOD

CASBO

ANY QUESTIONS ?

CASBO

The End

CASBO

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Table of Contents

Section 1: 2017-18 Updates

Section 1
PAYROLL UPDATES

2018 PAYROLL UPDATES

Social Security/Medicare

	2018
Social Security Wage Base	$128,400
Maximum Social Security Tax	$7,960.80
Employee and Employer Social Security Tax Rate	6.2%
Medicare Wage Base	None
Maximum Medicare Tax	None
Employee and Employer Medicare Tax Rate	1.45%
Employee additional Medicare Tax on earnings above $200,000	.9%
Amount of Earnings needed to qualify for a Quarter Coverage	$1,320

State Unemployment Insurance

	2017-2018
Wage Base	None
Employer Contribution Rate	.05%

California State Disability Insurance(SDI)

	2018
Wage Base	$114,967
Contribution Rate up to Wage Base	1.0%
Maximum SDI Contribution	$1,149.67

Supplemental Withholding Rates

	2018
Federal Supplemental Rate	22%
Million Dollars or more in Supplemental Wages	37%
California Supplemental Rate	6.6%
California Supplemental Rate for Bonuses	10.23%

Pension Plan Contribution Limits

	2018
Maximum Contribution Limitation for define contribution plans under §415(c)(1)(A	$55,000
Limitations on Exclusions for Elective Deferrals under:	
§403(b) Tax-Sheltered Annuities	$18,500
§457(b) Deferred Compensation Plan	$18,500
Age 50 catch up contributions	$6,000

2018 PAYROLL UPDATES

State Teachers Retirement System

	2017-2018
STRS Contribution Rate (employer)	14.43%
STRS Contribution Rate - employee 2% @60 employee 2% @ 62	10.25% 9.205%
STRS Reduced Workload (employer)	14.43%
STRS Reduced Workload (employee)	10.25%
STRS Retiree Earnings Limit	$43,755
PEPRA 2% at 62 Compensation Cap-employee portion only under IRC 401(a)(17)	$143,082

Public Employees Retirement System

	2017 - 2018
PERS Contribution Rate (Employer)	15.531%
PERS Contribution Rate (Employee-CLASSIC) PERS Contribution Rate (Employee-PEPRA NEW)	7.00% 6.50%
PEPRA Compensation Cap-employee portion only under 401(a)(17) limit with Social Security	121,388
PEPRA Compensation Cap-employee portion only under 401(a)(17) limit without Social Security	145,666

Federal Standard Mileage Rates

	2018
Business Miles	$0.545/mile
Charitable Activities	$0.14/mile
Relocation Related suspended for tax years 2018-2025	NONE
Medical Related	$0.17/mile

2018 PAYROLL UPDATES

Minimum Wage Rates

The Federal Fair Labor Standards Act (FLSA) and the California Wage Orders contain minimum wage requirements. School districts and community colleges must adhere to the minimum wage that provides the best benefit to the employee.

Federal Minimum Wage

The current federal minimum wage is $7.25 per hour.

On May 25, 2007, the FLSA was amended to increase the federal minimum wage in three steps:

1. $5.85 per hour effective July 24, 2007
2. $6.55 per hour effective July 24, 2008
3. $7.25 per hour effective July 24, 2009

The increases will still put the federal minimum wage below the California minimum wage, which provides the best benefit for California employees.

The California Minimum Wage

The current California minimum wage is $11.00 per hour for employers with 26 or more employees. Less than 26 employees the minimum wage is $10.50 per hour

Examples of some cities where the minimum wage is higher than the State minimum wage, be sure and check the cities your district office is located:
*Berkeley's minimum wage effective 10/1/17 is $13.75; 10/1/18 increases to $15.00 per hour
*San Francisco's minimum wage effective 7/1/17 is $14.00; 7/1/18 increases to $15.00 per hour,

2018 PAYROLL UPDATES

*Oakland’s minimum wage effective 1/1/2017 is $12.86 per hour.
*Richmond’s minimum wage effective 1/1/2017 $13.00 per hour.
*San Jose’s minimum wage effective 1/1/2018 $13.50 per hour.
*Los Angeles minimum wage effective 7/1/17 $12.00; increases 7/1/2018 to $13.25 per hour.
*San Diego’s minimum wage effective 1/1/2017 $11.50 per hour.

Section 2: Employee Classifications

Section 2

EMPLOYEE CLASSIFICATIONS

Employee Classification

OVERVIEW

The California Education Code along with collective bargaining agreements provide the regulations in regards to hiring, compensation, and benefits that apply to Certificated and Classified Employees. The first task will be to decide whether the individual will qualify as a certificated or classified employee. To make this determination, the first area to consider is whether the position is considered Certificated or Classified Service as defined under the California Education Code.

In general:

- Certificated positions require certification qualifications (credentials). Ed Code 22119.5.
- Classified service includes all positions not requiring certification qualifications with a few exceptions as found in Education Code Section 45103/88003.

CERTIFICATED EMPLOYEES

EDUCATION CODE SECTION 44830 (K-12)

Employment of Certificated Persons

(a) The governing board of a school district shall employ for positions requiring certification qualifications, only persons who possess the qualifications therefore prescribed by law. It is contrary to the public policy of this state for any person or

persons charged, by the governing boards, with the responsibility of recommending persons for employment by the boards to refuse or to fail to do so for reasons of race, color, religious creed, sex, or national origin of the applicants for that employment.

(b) A school district governing board shall not initially hire on a permanent, temporary, or substitute basis a certificated person seeking employment in the capacity designated in his or her credential, unless that person has demonstrated basic skills proficiency as provided in Section 44252.5 or is exempted from the requirement by subdivision (c), (d), (e), (f), (g), (h), (i), (j), (k), (l), or (m).

(1) The governing board of a school district, with the authorization of the Commission on Teacher Credentialing, may administer the state basic skills proficiency test required under Sections 44252 and 44252.5.

(2) The superintendent, in conjunction with the commission and local governing boards, shall take steps necessary to ensure the effective implementation of this subdivision. It is the intent of the Legislature that in effectively implementing this subdivision, school district governing boards shall direct superintendents of schools to prepare for emergencies by developing a pool of qualified emergency substitute teachers. This preparation shall include public notice of the test requirements and of the dates and locations of administrations of the tests. District governing boards shall make special efforts to encourage individuals who are known to be qualified in other respects as substitutes to take the state basic skills proficiency test at its earliest administration.

(3) Demonstration of proficiency in reading, writing, and mathematics by any person pursuant to Section 44252 satisfies the requirements of this subdivision.

(c) (1) A certificated person is not required to take the state basic skills proficiency test if he or she has been employed in a position requiring certification in any school

district within 39 months prior to employment with the district or if he or she is a retired certificated employee who meets all of the following requirements:

(A) He or she has taught 15 years or more in a California public school.

(B) He or she has been employed at least five of those 15 years in the same school district that desires to reemploy that person and has been employed as a full-time classroom teacher within the last five years or concurrently enrolls in a teacher refresher course that meets all of the following requirements:

(i) The course is developed and administered by the employing school district.

(ii) The course is aligned with the state content and performance standards for pupils, adopted pursuant to subdivision (a) of Section 60605.

(iii) The course is approved by the local governing board.

(C) He or she has been employed as a classroom teacher or administrator within the last 10 years.

(2) A person holding a valid California credential who has not been employed in a position requiring certification in any school district within 39 months prior to employment and who has not taken the state basic skills proficiency test, but who has passed a basic skills proficiency examination that has been developed and administered by the school district offering that person employment, may be employed by the governing board of that school district on a temporary basis on the condition that he or she will take the state basic skills proficiency test within one year of the date of his or her employment.

(3) A certificated person who is employed for purposes of the class size reduction program set forth in Chapter 6.10 (commencing with Section 52120) of Part 28 is not required to take the state basic skills proficiency test if he or she has been employed in

a position requiring certification in any school district within 39 months prior to employment with the district. A person holding a valid California credential who has not been employed in a position requiring certification in any school district within 39 months prior to employment for purposes of the class size reduction program and who has not taken the state basic skills proficiency test may be employed by the governing board of that school district on a temporary basis on the condition that he or she will take the state basic skills proficiency test within one calendar year of the date of his or her employment.

(d) This section does not require a person employed solely for purposes of teaching adults in an apprenticeship program, approved by the Apprenticeship Standards Division of the Department of Industrial Relations, to pass the state proficiency assessment instrument as a condition of employment.

(e) This section does not require the holder of a child care permit or a permit authorizing service in a development center for the handicapped to take the state basic skills proficiency test, so long as the holder of the permit is not required to have a baccalaureate degree.

(f) This section does not require the holder of a credential issued by the commission who seeks an additional credential or authorization to teach, to take the state basic skills proficiency test.

(g) This section does not require the holder of a credential to provide service in the health profession to take the state basic skills proficiency test, if that person does not teach in the public schools.

(h) If the state basic skills proficiency test is not administered at the time of hiring, the holder of a vocational designated subject credential who has not already taken and

passed the state basic skills proficiency test may be hired on the condition that he or she will take the test at its next local administration.

(i) If the holder of a vocational designated subject credential does not pass a proficiency assessment in basic skills pursuant to this section, he or she shall be given one year in which to retake and pass the proficiency assessment in basic skills. If at the expiration of the one-year period he or she has not passed the proficiency assessment in basic skills, he or she shall be subject to dismissal under procedures established in Article 3 (commencing with Section 44930).

(j) This section does not require the holder of a vocational designated subject credential to pass the state basic skills proficiency test as a condition of employment. The governing board of each school district, or each governing board of a consortium of school districts, or each governing board involved in a joint powers agreement, which employs the holder of a vocational designated subject credential shall establish its own basic skills proficiency for these credentials and shall arrange for those individuals to be assessed. The basic skills proficiency criteria established by the governing board shall be at least equivalent to the test required by the district, or in the case of a consortium or a joint powers agreement, by any of the participating districts, for graduation from high school. The governing board or boards may charge a fee to individuals being tested to cover the costs of the test, including the costs of developing, administering, and grading the test.

(k) This section does not require the holder of an adult education designated subject credential for other than academic subjects, who is employed in an instructional setting for 20 hours or less per week, to pass the state proficiency assessment as a condition of employment.

(l) This section does not require certificated personnel employed under a foreign exchange program to take the state basic skills proficiency test. The maximum period of exemption under this subdivision shall be one year.

(m) Notwithstanding any other law, a school district may hire a certificated teacher who has not taken the state basic skills proficiency test if that person has not yet been afforded the opportunity to take the test. The person shall take the test at the earliest opportunity and may remain employed by the district pending the receipt of his or her test results.

Education Code 87400 (Community Colleges)

Employment for Academic Positions

Governing boards of community college districts shall employ for academic positions, only persons who possess the qualifications therefore prescribed by regulation of the board of governors. It shall be contrary to the public policy of this state for any person or persons charged, by those governing boards, with the responsibility of recommending persons for employment by those boards to refuse or to fail to do so for reasons of race, color, religious creed, sex, or national origin of those applicants for that employment.

CLASSIFIED EMPLOYEES

Education Code Section 45103 (K-12)

Classified Service in Districts NOT Incorporating the Merit System

(a) The governing board of any school district shall employ persons for positions not requiring certification qualifications.

The governing board shall, except where Article 6 (commencing with

Section 45240) or Section 45318 applies, classify all of these employees and positions. The employees and positions shall be known as the classified service.

(b) (1) Substitute and short-term employees, employed and paid for less than 75 percent of a school year, shall not be a part of the classified service.

(2) Apprentices and professional experts employed on a temporary basis for a specific project, regardless of length of employment, shall not be a part of the classified service.

(3) Full-time students employed part time, and part-time students employed part time in any college work study program, or in a work experience education program conducted by a community college district pursuant to Article 7 (commencing with Section 51760) of Chapter 5 of Part 28 and that is financed by state or federal funds, shall not be a part of the classified service.

(4) Part-time playground positions shall not be a part of the classified service, where the employee is not otherwise employed in a classified position. Part-time playground positions shall be considered a part of the classified service when the employee in the position also works in the same school district in a classified position.

(c) Unless otherwise permitted, a person whose position does not require certification qualifications shall not be employed by a governing board, except as authorized by this section.

(d) As used in this section:

(1) "Substitute employee" means any person employed to replace any classified employee who is temporarily absent from duty. In addition, if the district is then engaged in a procedure to hire a permanent employee to fill a vacancy in any classified position, the governing board may fill the vacancy through the employment, for not more than 60 calendar days, of one or more substitute employees, except to the extent that a collective bargaining agreement then in effect provides for a different period of time.

(2) "Short-term employee" means any person who is employed to perform a service for the district, upon the completion of which, the service required or similar services will not be extended or needed on a continuing basis. Before employing a short-term employee, the governing board, at a regularly scheduled board meeting, shall specify the service required to be performed by the employee pursuant to the definition of "classification" in subdivision (a) of Section 45101, and shall certify the ending date of the service. The ending date may be shortened or extended by the governing board, but shall not extend beyond 75 percent of a school year.

(3) "Seventy-five percent of a school year" means 195 working days, including holidays, sick leave, vacation and other leaves of absence, irrespective of number of hours worked per day.

(e) Employment of either full-time or part-time students in any college workstudy program, or in a work experience **education** program shall not result in the displacement of classified personnel or impair existing contracts for services.

(f) This section shall apply only to districts not incorporating the merit system as outlined in Article 6 (commencing with Section 45240).

Education Code 45104 (K-12)

Positions Not Requiring Certification Qualifications

45104. Every position not defined by this **code** as a position requiring certification qualifications and not specifically exempted from the classified service according to the provisions of Section 45103 or 45256 shall be classified as required by those sections and shall be a part of the classified service. Such positions may not be designated as certificated nor shall the assignment of a title to any such a position remove the position from the classified service, nor shall possession of a certification document be made a requirement for employment in any such position. Nothing in this section shall be construed to prohibit the employment of any individual in a position described by this section as part of the classified service who is in possession of certification qualifications, nor shall the possession of certification qualifications be grounds for the elimination of an individual for consideration for employment in such a position. This section shall apply to districts which have adopted the merit system in the same manner and with the same effect as though it were a part of Article 6 (commencing with Section 45240) of this chapter.

Education Code 45256 (K-12)

Classified Service; Establishment; Exclusions

(a) The commission shall classify all employees and positions within the jurisdiction of the governing board or of the commission, except those that are exempt from the classified service, as specified in subdivision (b). The employees and positions shall be known as the classified service. "To classify" shall include, but not be limited to, allocating positions to appropriate classes, arranging classes into occupational hierarchies, determining reasonable relationships within occupational hierarchies, and preparing written class specifications.

(b) All of the following are exempt from the classified service:

(1) Positions which require certification qualifications.

(2) Full-time students employed part time.

(3) Part-time students employed part time in any college workstudy program, or in a work experience **education** program conducted by a community college district pursuant to Article 7 (commencing with Section 51760) of Chapter 5 of Part 28 and that is financed by state or federal funds.

(4) Apprentice positions.

(5) Positions established for the employment of professional experts on a temporary basis for a specific project by the governing board or by the commission when so designated by the commission.

(6) Part-time playground positions, where the employee is not otherwise employed in a classified position. Part-time playground positions shall be considered part of the classified service when the employee in the position also works in the same school district in a classified position.

(c) (1) Employment of either full-time or part-time students in any college workstudy program, or in a work experience **education** program shall not result in the displacement of classified personnel or impair existing contracts for services.

(2) Nothing in this section shall prevent an employee, who has attained regular status in a full-time position, from taking a voluntary reduction in time and retaining his or her regular status under the provisions of this law.

(d) No person whose contribution consists solely in the rendition of individual personal services and whose employment does not come within the scope of the exceptions listed above shall be employed outside the classified service.

(e) A part-time position is one for which the assigned time, when computed on an hourly, daily, weekly, or monthly basis, is less than 87 1/2 percent of the normally assigned time of the majority of employees in the classified service.

Education Code Section 88003 (Community Colleges)

Classified Service in Districts NOT Incorporating the Merit System

The governing board of any community college district shall employ persons for positions that are not academic positions. The governing board, except where Article 3 (commencing with Section 88060) or Section 88137 applies, shall classify all those employees and positions. The employees and positions shall be known as the classified service. Substitute and short-term employees, employed and paid for less than 75 percent of a college year, shall not be a part of the classified service. Part-time playground positions, apprentices and professional experts employed on a temporary basis for a specific project, regardless of length of employment, shall not be a part of the classified service. Full-time students employed part time, and part-time students employed part time in any college work-study program, or in a work

experience education program conducted by a community college district and which is financed by state or federal funds, shall not be a part of the classified service. Unless otherwise permitted, a person whose position does not require certification qualifications shall not be employed by a governing board, except as authorized by this section.

"Substitute employee," as used in this section, means any person employed to replace any classified employee who is temporarily absent from duty. In addition, if the district is then engaged in a procedure to hire a permanent employee to fill a vacancy in any classified position, the governing board may fill the vacancy through the employment, for not more than 60 calendar days, of one or more substitute employees, except to the extent that a collective bargaining agreement then in effect provides for a different period of time.

"Short-term employee," as used in this section, means any person who is employed to perform a service for the district, upon the completion of which, the service required or similar services will not be extended or needed on a continuing basis. Before employing a short-term employee, the governing board, at a regularly scheduled board meeting, shall specify the service required to be performed by the employee pursuant to the definition of "classification" in subdivision (a) of Section 88001, and shall certify the ending date of the service. The ending date may be shortened or extended by the governing board, but shall not extend beyond 75 percent of a school year.

"Seventy-five percent of a college year" means 195 working days, including holidays, sick leave, vacation and other leaves of absences, irrespective of number of hours worked per day.

Employment of either full-time or part-time students in any college work-study program, or in a work experience **education** program shall not result in the displacement of classified personnel or impair existing contracts for services.

This section shall apply only to districts not incorporating the merit system as outlined in Article 3 (commencing with Section 88060).

Education Code Section 88004 (Community Colleges)
Positions not Specifically Exempted

Every position not defined by the regulations of the board of governors as an academic position and not specifically exempted from the classified service according to the provisions of Section 88003 or 88076 shall be classified as required by those sections and shall be a part of the classified service. These positions may not be designated as academic by the governing board of a district nor shall the assignment of a title to any such a position remove the position from the classified service.

Nothing in this section shall be construed to prohibit anyone from being employed in a classification because he or she possesses the minimum qualifications required of faculty members or academic administrators, nor shall the possession of those qualifications be grounds for the elimination of an individual from consideration for employment in a classified position.

This section shall apply to districts which have adopted the merit system in the same manner and with the same effect as though it were a part of Article 3 (commencing with Section 88060) of this chapter.

Education Code Section 88076 (Community College Merit Districts)
Establishment of Classified Service; definitions; positions excluded

(a) The commission shall classify all employees and positions within the jurisdiction of the governing board or of the commission, except those which are exempt from the classified service, as specified in subdivision (b). The employees and positions shall be known as the classified service. "To classify" shall include, but not be limited to, allocating positions to appropriate classes, arranging classes into occupational hierarchies, determining reasonable relationships within occupational hierarchies, and preparing written class specifications.

(b) The following positions and employees are exempt from the classified service:

(1) Academic positions.

(2) Part-time playground positions.

(3) Full-time students employed part time.

(4) Part-time students employed part time in any college work-study program or in a work experience education program conducted by a community college which is financed by state or federal funds.

(5) Apprentice positions.

(6) Positions established for the employment of professional experts on a temporary basis for a specific project by the governing board or by the commission when so designated by the commission.

Employment of either full-time or part-time students in any college work-study program, or in a work experience education program shall not result in the displacement of classified personnel or impair existing contracts for services.

However, nothing in this section shall prevent an employee, who has attained regular status in a full-time position, from taking a voluntary reduction in time and retaining his or her regular status under the provisions of this law.

No person whose contribution consists solely in the rendition of individual personal services and whose employment does not come within the scope of the exceptions listed above shall be employed outside the classified service.

A part-time position is one for which the assigned time, when computed on an hourly, daily, weekly, or monthly basis, is less than 871/2 percent of the normally assigned time of the majority of employees in the classified service.

BOARD MEMBERS

Under the California Government Code for retirement purposes, Board Members are not employees but are considered "elected officials". However, for tax reporting and withholding purposes Board Members are considered employees. Internal Revenue Code Sections 3401(c) and 3121 (b) (7) (F) (iv) states "the term employee includes an officer, employee, or elected official of the U.S., a State, or political subdivision thereof…."

403 (b) TSA Eligibility

Board members are not eligible under the 403 (b) regulations to participate in a 403 (b) plan.

457 (b) Deferred Compensation Plan

Board members may participate in a 457 (b) plan if the plan document so allows.

Federal and State Income Tax Withholding

Board members are treated as employees for tax withholding and should be paid through payroll and issued a Form W-2 for any compensation paid for their services.

State Unemployment Insurance

Board members are not covered for State Unemployment Insurance.

Social Security/Medicare Coverage

Board members are required to be covered under Social Security and Medicare. The only exception would be for a Board Member elected before July 1, 1994 and who was a member of PERS at a district that did not have a Section 218 agreement that covered them.

CalSTRS/CalPERS

Board members are not covered to be members of CalSTRS. They are also not covered to be members of CalPERS unless they were elected at the district before July 1, 1994.

Effective July 1, 1994, Government Code Section 20361 (c) excluded Board Members from coverage into CalPERS who were not already members of the system as of that date.

HIRING RETIREES

Districts need to be aware of certain regulations when hiring back a CalSTRS or CalPERS retiree. Both systems have work restrictions on when, what positions, and how much time or compensation the individual can receive.

Retirees that are hired back to do the same duties they did as employees before retirement, or duties of any other employee position covers, should be paid through

the payroll system as a short-term or substitute employee. In these cases, retirees may not be considered "Independent Contractors" by the IRS or California EDD. Incorrect misclassification can subject the district to federal and state penalties for improper tax withholding and reporting.

1) Hiring a CalSTRS Retiree

Should not exceed the Earnings Limitation set by CalSTRS

July 1, 2017 to June 30, 2018 the earnings limit is $43,755.

Assembly Bill 340, Public Employees' Pension Reform Act of 2013 (PEPRA):

CalSTRS members who retire on or after January 1, 2013 are subject to the $0 earnings limit for the first 180 days after retirement regardless of age.

There is a very narrow exemption from this requirement if a retiree has reached normal retirement age; and their appointment is necessary to fill a critically needed position; the governing body of the employer, such as a school board, approves the appointment by resolution at a public meeting; the retiree did not receive any financial inducement to retire; and the termination of service was not the cause of the need to acquire the retiree's services. All of these criteria have to be met, and the employer must submit the required documentation to CalSTRS substantiating the eligibility for this exemption. CalSTRS must receive the exemption request and required documentation before the retiree can begin working. If approved, this exemption only applies to the separation-from-service requirement—the postretirement earnings limit still applies.

Notification requirements and Reporting of Post-Retirement Earnings by Employer:

Section 22461 requires employers to notify retired CalSTRS members of the earnings limits and report earnings to CalSTRS each month.

STRS retirees are prohibited employment in a classified position while retired with the exception of employment as a Teachers' Aide ***(Education Code 45134). This section is outside the Teachers' Retirement Law and would be enforced by the Department of Education.***

2) Hiring a CalPERS Retiree- Government Code Section 21224

A CalPERS retiree can be hired by a district for a temporary assignment if the employment is during an emergency to prevent stoppage of public business or the retiree has skills needed by the district for a limited duration.

- May be employed up to 960 hours per fiscal year
- Compensation shall not be less than minimum or greater than employees performing comparable duties.

Assembly Bill 340, Public Employees' Pension Reform Act of 2013 (PEPRA):

- A CalPERS member who retirees and does not seek employment until after **January 1, 2013 must wait 180 days before returning to CalPERS covered employment**.

Note: A one-time per retiree extension of the 960 hour rule may be approved by CalPERS in an emergency situation. The request must be processed before the 960 hours has expired for the retiree.

Unemployment Insurance

A district cannot hire a retired annuitant that received unemployment insurance payments within the previous 12 months. Districts should have any CalPERS retirees fill out Form DPA 715. (See copy of form in this section)

CalPERS Employment After Retirement with a CalPERS Covered Employer

CalPERS Circular Letter #200-181-04 discusses the final regulations stating that a CalPERS member who has not reached normal retirement age must have a 60 calendar day separation in service prior to returning to employment as a retired

annuitant, and there must be no agreement to return to work between the member and the CalPERS employer prior to retirement. (See the Circular letter in this section)

3) Social Security and Medicare for Retirees

Retirees who retire from one of the state pension systems may be exempt in some situations from paying contributions into Social Security.

All retirees hired after March 31, 1986 are subject to Medicare tax withholding regardless of their age. The withholding tax applies even if they are eligible to receive Medicare benefits while working.

OBRA '90 specifically excludes a qualified retired annuitant from mandatory social security coverage if they are rehired with an employer that participates in the same retirement plan from which they retired. To be considered a qualified retired annuitant, the employee must be receiving retirement benefits or has reached normal retirement age under the retirement plan.

Example:

June 1, ~~2012~~2018, a teacher retires from a school district that participates in the State Teachers Retirement System and begins receiving retirement benefits from the plan. On January 14, 2019, the retiree is hired to substitute teach in a school district that also participates in the State Teachers Retirement System. The retiree is considered a qualified rehired annuitant and is not required to be covered by the OBRA 90' provisions of social security. The retiree would however qualify for Medicare coverage.

CALSTRS
HOW WILL YOU SPEND YOUR FUTURE?

California State Teachers'
Retirement System
Executive Office
PO Box 15275
Sacramento, CA 95851-0275
CalSTRS.com

March 9, 2017

TO: All County Superintendents of Schools
District Superintendents of Schools
Charter School Administrators
Community College Districts and
Other Employing Agencies

FROM: Jack Ehnes
Chief Executive Officer

SUBJECT: Employer Directive 2017–03
Supersedes Employer Directive 2016–03
Postretirement Earnings Limit for the 2016–17 Fiscal Year, 2017–18 Fiscal Year, and 2017 Calendar Year

PURPOSE

This employer directive is intended to inform and remind employers of:

- The application of the earnings limit for retired CalSTRS members.
- The annual postretirement earnings limit for the 2016–17 fiscal year.
- The annual postretirement earnings limit for the 2017–18 fiscal year.
- Requirements for requesting an exemption from the annual postretirement earnings limit to assist schools that are in financial or academic distress. This exemption will sunset on June 30, 2017.
- The postretirement separation-from-service requirement for members and participants during the first 180-calendar days from their retirement date with CalSTRS.
- Requirements for requesting an exemption from the separation-from-service requirement.
- Restrictions on hiring retired CalSTRS members and participants in classified positions.
- Retirement incentive restrictions.
- Requirements for employer communication regarding the earnings limits and, if applicable, the retirement incentive restrictions when hiring CalSTRS members. Also, the employer requirements regarding maintaining accurate records and reporting postretirement earnings to CalSTRS.
- The CalSTRS postretirement excess earnings notification process.
- The disability retirement earnings limit for the 2017 calendar year.
- The disability allowance earnings limit for the 2016–17 and 2017–18 fiscal years.

SCOPE

This directive contains information for county superintendents of schools, school districts, charter schools, community college districts, and any agency that employs retired members of the Defined Benefit (DB) Program (referred to in this directive as "retired CalSTRS members") or retired participants of the Cash Balance (CB) Benefit Program (referred to in this directive as "retired CalSTRS participants") to perform creditable service or that employs CalSTRS members receiving either a Disability Allowance or Disability Retirement benefit in any capacity.

DISCUSSION

Application of Postretirement Earnings Limit

Sections 24214 and 24214.5 of the Education Code impose limitations on retired CalSTRS members who return to work and perform retired member activities. Section 22164.5 defines "retired member activities" as one or more of the activities identified in subdivision (b), (c) or (d) of Section 22119.5 or subdivision (b), (c) or (d) of Section 26113 when performed as either an employee of an employer, an employee of a third party (except under certain circumstances) or an independent contractor within the California public school system. The salary being paid for retired member activities may not be less than the minimum, nor can it exceed the maximum, paid by the employer to other employees performing comparable duties.

If a retired CalSTRS member earns compensation for performing retired member activities during the 180-calendar day separation-from-service period or in excess of the annual postretirement earnings limit, Education Code sections 24214(g) and 24214.5(h) require CalSTRS to reduce the member's retirement benefit dollar-for-dollar, up to a maximum of the member's retirement benefit, until the member has repaid the amount of compensation that was earned during the separation-from-service period or in excess of the earnings limit.

Postretirement Earnings Limit for the 2016–17 and 2017–18 Fiscal Years

The postretirement earnings limit for retired CalSTRS members for the 2016–17 *fiscal* year is $41,732.

The postretirement earnings limit for retired CalSTRS members for the 2017–18 *fiscal* year is $43,755.

The limit is adjusted annually by CalSTRS and is equal to one-half of the median final compensation amount for all members who retired for service during the fiscal year ending in the previous calendar year.

Exclusion When Working for a Third Party

Retired members employed by a third party are excluded from the postretirement earnings limit and related provisions provided they meet all of the following criteria:

- The retired member is employed by a third party that does not participate in a California public pension system;

- The activities performed by the retired member are not normally performed by the employees of an employer; and
- The activities are performed by the retired member for a limited term of 24 months or less.

Employer reporting of retired members who are employed by a third party under the narrow conditions above is not required. CalSTRS has not identified any example of service that would meet these criteria.

Exemption to the Annual Postretirement Earnings Limit

There is a narrow exemption from the annual postretirement earnings limit available through June 30, 2017, for certain appointments to assist schools in financial or academic distress. There are four specific appointments that are exempt:

- Appointment by the State Superintendent of Public Instruction as a trustee for a school district that has received an emergency apportionment.
- Appointment by a county superintendent of schools as a fiscal adviser or fiscal expert for a school district that must revise its budget or that may or will be unable to meet its financial obligations for the remainder of the fiscal year or the subsequent fiscal year(s).
- Appointment by the State Board of Education as a trustee or a receiver for a local educational agency that has been identified for corrective action under the federal No Child Left Behind Act of 2001.
- Appointment by the Board of Governors of the California Community Colleges as a special trustee for a community college district that fails to achieve fiscal stability or that fails to comply with the Board of Governors' recommendations.

To qualify for this exemption, the appointing authority must certify the following:

- The position was first advertised for appointment to current active or inactive members and no qualified person was available to fill the appointment.
- The appointing authority made a good faith effort to hire a retired member who would reinstate.
- The salary being paid does not exceed the salary that was offered as first advertised to current or inactive members.
- The retired member is normal retirement age when the compensation is earned (for 2% at 60 members, age 60; for 2% at 62 members, age 62).
- The retired member has not received financial inducement to retire, including, but not limited to, any form of compensation or other payment that is paid directly to or indirectly to the member, from any public employer in the previous six months.

When applying for the postretirement earnings limit exemption, employers must complete the *Request for Postretirement Earnings Limit Exemption* (SR 0164) form, which is available in "Reference Items" on the Secure Employer Website. In order for CalSTRS to consider an application for an exemption, we must receive this form and all required documentation before the retired member begins performing retired member activities. If CalSTRS does not receive the *Request for Postretirement Earnings Limit Exemption* form and required documentation prior to

the beginning of a member's postretirement service for that position, CalSTRS will not accept the form for consideration, and the member will not be approved for the exemption.

If the exemption for the annual postretirement earnings limit, as outlined in Education Code section 24214, is approved, the member will only be exempt from the annual postretirement earnings limit. The separation-from-service requirement will still apply unless a member previously received a separation-from-service requirement exemption. In order to be exempt from the separation-from-service requirement, a separate exemption request must have been submitted by the employer and approved by CalSTRS.

Separation-From-Service Requirement

Pursuant to Education Code section 24214.5, there is a 180-calendar day separation-from-service requirement for all retired CalSTRS members, regardless of age, during which the postretirement compensation limit for the performance of retired member activities is zero dollars ($0).

If the retired CalSTRS member returns to work during this period, CalSTRS will reduce the member's retirement benefit by an amount equal to his or her earnings up to the benefit payable during that period. This restriction is in addition to the annual postretirement earnings limit. Any amount the retired CalSTRS member receives during the first 180 calendar days of retirement will also count against the annual postretirement earnings limit for the appropriate fiscal year.

Pursuant to Education Code section 26812, the 180-calendar day separation-from-service requirement applies to Cash Balance Benefit Program annuitants who retired on or after January 1, 2014, no matter their age. If a retired CalSTRS participant receives his or her retirement benefit as a lump sum, the benefit is not payable until 180 days after the date employment was terminate. If a participant electing a lump-sum benefit performs creditable service during the 180-calendar day separation-from-service period, his or her retirement application will be automatically canceled.

Exemption to the Separation-From-Service Requirement

There is a narrow exemption from the 180-calendar day separation-from-service requirement for a retired CalSTRS member or participant under certain circumstances. To qualify for this exemption, the retired CalSTRS member or participant must be at or above normal retirement age at the time the compensation is earned, and the employer must appoint the retired member or participant to a critically needed position that has been approved by the governing body of the employer in a public meeting as reflected in a resolution. The resolution of the appointment must be adopted before the retired CalSTRS member or participant begins performing retired member or participant activities under the exemption. The resolution approving the appointment may not be placed on a consent calendar.

The resolution must include the following specific information and findings:

- The intent to seek an exemption from the 180-calendar day separation-from-service requirement.
- The nature of the employment.

- A finding that the appointment is needed to fill a critically needed position before the 180-calendar day separation-from-service requirement is fulfilled.
- A finding that the member or participant did not receive a retirement incentive or any financial inducement to retire from any public employer.
- A finding that, by retiring, the member or participant did not create the vacancy the member or participant is now filling.

When applying for the separation-from-service requirement exemption, the superintendent, the county superintendent of schools or the chief executive officer of a community college must complete the *Request for Separation-from-Service Requirement Exemption* (SR 1897) form, which is available in "Reference Items" on the Secure Employer Website. CalSTRS must receive this form and the aforementioned resolution indicating the above information to substantiate the eligibility of the retired CalSTRS member or participant for the exemption before the member or participant begins performing service under the exemption. CalSTRS must notify the employer and the retired CalSTRS member or participant within 30 days of receiving the resolution and all required documentation whether the service performed will be subject to or exempt from the 180-calendar day separation-from-service requirement.

If the separation-from-service requirement exemption is approved, the retired CalSTRS member or participant will only be exempt from the separation-from-service requirement. Any earnings during the 180-calendar day period will still be subject to the annual postretirement earnings limit. In order to be exempt from the annual postretirement earnings limit, a separate exemption request would need to be submitted by the employer and approved by CalSTRS.

Education Code sections 24214.5 and 26812 clarify what constitutes a "financial inducement to retire" that would prohibit a retired CalSTRS member or participant from being eligible for an exemption from the separation-from-service requirement.

Classified Position Restrictions

Education Code section 45134 precludes retired CalSTRS members from employment in classified positions in the California public school system. However, this section is outside of the Teachers' Retirement Law and therefore outside the purview of CalSTRS.

Retired CalPERS Postretirement Employment Restrictions

If the employee is a CalSTRS and CalPERS member, please ask the employee to contact CalPERS at 888-225-7377 to determine the impact that returning to work would have on his or her CalPERS benefit.

Retirement Incentive Restrictions

Members who retired with a CalSTRS retirement incentive under Education Code section 22714 will lose the increased service credit attributable to the retirement incentive if they return to employment in any job, including substitute teaching, within five years of receiving the incentive with the school district, community college district or county office of education that granted the retirement incentive. Education Code section 22461 requires the employer to notify retired

members of the employment restrictions in Education Code section 22714 upon retaining their services.

Employer Requirements for Notification of Postretirement Earnings and Employment Restrictions, and Required Reporting of Postretirement Earnings

Upon retaining the services of a retired CalSTRS member, Education Code section 22461 requires employers to notify that member of earnings limitations and employment restrictions for those who receive retirement incentives, regardless of whether the retired member performs the services as an employee of the employer, an employee of a third party or an independent contractor. Employers must also report the retired member's earnings to CalSTRS each month. All postretirement earnings must be reported with Member Code 2 and Assignment Code 61.

CalSTRS Postretirement Excess Earnings Notification Process

CalSTRS sends an *Initial Postretirement Earnings Letter* to the member when postretirement earnings are initially reported by the employer. The *Initial Postretirement Earnings Letter* informs the member of the current earnings limit and describes what occurs if the limit is exceeded. When the employer reports postretirement earnings equal to one-half of the annual postretirement earnings limit, CalSTRS sends a second letter, the *Postretirement Earnings Mid-Limit Letter,* notifying the member of the dollar amount reported to date and reminding the member of the consequences of exceeding the earnings limit.

When a member either violates the 180-calendar day separation-from-service requirement or exceeds the annual earnings limit, CalSTRS sends the member another letter notifying him or her that the excess earnings will be withheld from his or her monthly retirement benefit. CalSTRS gives at least a 30-day notice before commencing collection. If the earnings were reported to CalSTRS in error by a member's employer, the employer is responsible for correcting the previous reporting and notifying CalSTRS that corrected contribution lines were submitted.

Application and Amount of the 2017 Disability Retirement Earnings Limit

The disability retirement earnings limit for the 2017 *calendar* year is $29,550. The limit applies to all earnings regardless of whether the member is self-employed or employed in any capacity in either the public or private sector. The limit is adjusted annually by the Teachers' Retirement Board, if necessary, by the amount of change in the California Consumer Price Index.

Application and Amount of the 2016–17 and 2017–18 Disability Allowance Earnings Limit

The disability allowance earnings limit for the 2016–17 and 2017–18 *fiscal* years is calculated individually for each member based on the member's indexed final compensation amount. Members receiving a disability allowance benefit are also subject to individual monthly and continuous six-month earnings limits based on the member's indexed final compensation. The various limits apply to all earnings regardless of whether the member is self-employed or employed in any capacity in either the public or private sector.

SUMMARY OF REQUIRED ACTIONS

In accordance with Education Code section 22461, upon retaining the services of a retired member either as an employee of an employer, an employee of a third party or as an independent contractor within the California public school system, the employer is required to:

- Notify the retired member of all earnings limits and also the retirement incentive employment restrictions, if applicable.
- Maintain accurate records of the retired member's earnings.
- Report those earnings to the retired member and to CalSTRS monthly, using Member Code 2 and Assignment Code 61, regardless of the method of payment or the fund from which the payments were made.

To learn more about postretirement limitations, please visit CalSTRS.com/general-information/working-after-retirement. If you have questions regarding the postretirement earnings limit, contact Postretirement by email at postretirement@calstrs.com or leave a voicemail at 916-414-5967.

Postretirement Earnings Limit Exemption Matrix

- **Exemption forms AND additional required documentation must be received by CalSTRS before the retired member begins service.**
- **Qualification for an exemption is subject to CalSTRS approval. After completing its review, CalSTRS sends a letter to the member or participant and his or her employer approving or denying the exemption request.**

	Narrow Exemption for Working in Distressed Schools	**Exemption from the Separation-From-Service Requirement**
Details	Four specific appointments are exempt: • Appointment by the State Superintendent of Public Instruction as a trustee for a school district that has received an emergency apportionment. • Appointment by a county superintendent of schools as a fiscal adviser or fiscal expert for a school district that must revise its budget or that may or will be unable to meet its financial obligations for the remainder of the fiscal year or the subsequent fiscal year(s). • Appointment by the State Board of Education as a trustee or a receiver for a local educational agency that has been identified for corrective action under the federal No Child Left Behind Act of 2001. • Appointment by the Board of Governors of the California Community Colleges as a special trustee for a community college district that fails to achieve fiscal stability or that fails to comply with the Board of Governors' recommendations.	In order to qualify for this exemption, the employer must appoint a member to a position that has been approved by the governing body of the employer in a public meeting as reflected in a resolution. The resolution must be adopted before the member begins performing creditable service under the exemption. A member can qualify for this exemption only if he or she has reached normal retirement age (for 2% at 60 members, age 60; for 2% at 62 members, age 62).
Education Code	§24214	§24214.5
Required CalSTRS Form	*Request for Postretirement Earnings Limit Exemption* form *(SR 0164)*	*Request for Separation-from-Service Requirement Exemption* form *(SR 1897)*
Additional Required Documentation	The appointing authority must certify that: • The position was advertised to active or inactive members and no qualified person was available to be appointed. • The appointing authority made a good faith effort to hire a retired member who would reinstate. • The salary being paid does not exceed what was advertised or is currently paid for that position. • Must be normal retired age (for 2% at 60 members, age 60; for 2% at 62 members, age 62) when compensation is earned. • The member did not receive a retirement incentive or any financial inducement to retire from any public employer.	The resolution must specify the following: • The intent to seek an exemption from the 180-calendar day separation-from-service requirement. • The nature of the employment. • The appointment is needed to fill a critically needed position before the 180-calendar day separation-from-service requirement is fulfilled. • The member did not receive a retirement incentive or any financial inducement to retire from any public employer. • The member did not create the vacancy the member is now filling.
Expiration of Exemption and Additional Restrictions	This exemption applies only to the annual postretirement earnings limit. If applicable, the retired member will still be subject to the separation-from-service requirement. To exempt a member from both limitations, the employer must apply for both exemptions separately. This exemption will become inoperative as of July 1, 2017.	This exemption only applies to the separation-from-service requirement. The retired member will still be subject to the annual postretirement earnings limit. To exempt a member from both limitations, the employer must apply for both exemptions separately.

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Date: December 21, 2005
Reference No.:
Circular Letter No.: 200-265-05
Distribution: **IV, V, VI, X, XIX**
Special:

Circular Letter

TO: ALL STATE AGENCIES, AGRICULTURAL DISTRICTS, PUBLIC AGENCIES, STATE COLLEGES & UNIVERSITIES, EMPLOYEE REPRESENTATIVES

SUBJECT: RETIRED ANNUITANTS

Change Limit from 960 Hours in Calendar Year to 960 Hours in Fiscal Year

Effective January 1, 2006, the Legislature has changed the law (Statutes of 2005, Chapter 328, Assembly Bill 1166) that allows a state agency or public agency covered by the California Public Employees' Retirement System (CalPERS) to employ a retired person without reinstatement from retirement or loss or interruption of benefits. Currently, a retired person may be temporarily employed for 960 hours in any *calendar year* without reinstatement. The change allows a retired person to be temporarily employed for 960 hours in any *fiscal year* without reinstatement. The Public Employees' Retirement Law defines fiscal year to mean any year commencing on July 1st and ending with June 30th next following.

The change will take effect on January 1, 2006, midway through the fiscal year. The following provides the maximum hours a state agency or public agency may temporarily employ a retired person without reinstatement from retirement or loss or interruption of benefits:

- January 1, 2006 through June 30, 2006 — 960 hours maximum
- July 1, 2006 through June 30, 2007 — 960 hours maximum
- Future fiscal years — 960 hours maximum

Other Recent Changes in the Law

Unemployment Insurance

Effective January 1, 2005, Government Code section 21224 (Statutes of 2004, Chapter 398, Senate Bill 1439) was amended to preclude a retired annuitant from returning to employment if, during the 12-month period prior to the appointment, the retired annuitant received unemployment insurance based on employment as a retired annuitant.

A retired person who accepts a temporary appointment within 12 months of receiving unemployment insurance as described, must terminate employment on the last day of the current pay period. Further, that person will not be eligible for reappointment as a retired annuitant for 12 months following the last day of employment. A violation of this provision does not require mandatory reinstatement from retirement nor reimbursement of the system.

Requirement for Bona Fide Separation in Service

Effective January 1, 2004, Government Code section 21220.5 was added to the Public Employees' Retirement Law to require that a person who has not attained normal retirement age is required to have a bona fide separation in service before working after retirement without reinstatement or loss or interruption of benefits. The CalPERS Board of Administration subsequently adopted regulations which defined "normal retirement age" and "bona fide separation in service." Those regulations are at California Code of Regulations, title 2, sections 586 – 586.2. Please see Circular Letter 200-181-04 for details about the bona fide separation in service requirements.

For additional information concerning retiree employment, please review the information under **Employment after Retirement** available on the CalPERS Web site at www.calpers.ca.gov. If you have additional questions, please telephone the Employer Contact Center at **888 CalPERS** (or **888**-225-7377).

Lori McGartland, Chief
Employer Services Division

Chapter 3

Salary Computations

A. SALARY SCHEDULES

Most salary schedules should be developed outside of the payroll department in order to have a true segregation of duties and strict accountability. The placement of an employee on the salary schedule should also occur outside of the payroll department. The determination of salary placement will normally depend on an employee's years of experience and education.

B. BASE PAY RATE

Base pay rates for employees are determined by the employee's position and step/range on a board approved salary schedule.

C. ADDITIONAL PAY

Overtime, stipends, bonuses and special compensation may be paid as additional pay.

D. TYPES OF PAY

1. Normal Pay

Employees can receive checks for only the actual months worked. These may be 10, 11, or 12 month employees. Employees may be paid on a monthly, hourly or daily basis. *(Lump sum payments are not considered normal pay.)*

2. Retroactive Pay

When an employee's pay status changes due to a new position, additional educational units or contract settlement, and the effective date is earlier than the current month, retroactive payments are required. Certificated positions will require a days to days recalculation since certificated employees are paid on a daily basis. Classified employees will receive an adjustment calculated on the difference of the monthly or hourly salary rate. Since the rate of pay

has changed, all overtime paid to a classified employee would also need to be recalculated.

3. Deferred Pay

The California Education Code allows districts to participate in allowing their employees who are not paid over a 12 month period to defer their salary until e summer months. When employees have an option to take their salary in 10 months or defer the salary payments until summer, the IRS regulation of "Constructive Receipt" comes into play. Under the constructive receipt rules the salary becomes taxable for federal and state purposes at the time the employee had an opportunity to receive it, or during the 10 months. Districts should seek IRS or County Counsel guidance in regards to the taxation of deferred pay.

E. CERTIFICATED WORK DAYS & SALARY COMPUTATIONS

1. Work Days

Certificated employees are paid based on an annual contract and a set number of duty days. The duty days are tied to a salary schedule or a contract. Certificated non-management employees are not provided with holiday and vacation leave of absence under Education Code. In most cases, districts do offer vacation pay for 11 and 12 month certificated administrative employees. When this occurs, the workdays will include the paid days of vacation when calculating a daily rate of pay.

Certificated Work Days (Based on 12 month employee)

365	Days per Year
-104	Saturdays & Sundays
-13	Holidays (varies per district)
248	Work Days

2. Salary Computations

If a certificated employee fails to serve the full year, Education Code Section 45041 requires the employee to receive a proration of annual salary, based on days served, over the total days of required service. *See Education Code Section 45041*

Warning: Not working a full contract will impact service retirement credits.

F. CERTIFICATED CALCULATION

1. Late Hires

Employees hired after the beginning of the school year must have a full-time daily rate of pay calculated. This will be used to determine the first and subsequent monthly amounts to be paid over the remainder of the contract year.
The employee must be paid at the correct monthly rate of pay to ensure that the accurate full time equivalent (FTE) service credit is reported to CalSTRS.
If the county office is responsible for CalSTRS reporting they must be notified of any late hires.

Step 1: Full Time Contract Amount

Contract Period	Sept 1 to June 30
Annual Base from Salary Schedule	$35,000.00
FTE (1.0 x $35,000.00)	$35,000.00
Base Contract Days	185
Pay Period	10
Monthly Pay Rate	$35,000.00 ÷ 10 months = $3,500.00
Daily Pay Rate	$35,000.00 ÷ 185 days = $189.19

Step 2: Late Hire Monthly Calculation

Actual Annual Contract Amount	$35,000.00
Hire Date	October 7th
Work Days left in School Year	152
Contract Amount Remaining	$189.19 x 152 days = $28,756.88
Amount due over the remaining Nine (9) paychecks Oct to June	$28,756.88

Step 3: 1st Paycheck Adjustment – October

Calculate:

November through June $3,500 x 8 pay periods =	$28,000.00

Then:

Actual Annual Contract	$ 28,756.88
Future Paychecks	- 28,000.00
To pay in 1st Paycheck – October	$ 756.88

2. Change in Assignment/Contract Change

When employees receive a change in assignment that involves a change in days, pay rate, etc., it is important to calculate the individual changes correctly for payment purposes, and to report it to the California State Teachers' Retirement System (CalSTRS) correctly to accurately record service credits. The different assignments should be reported and paid separately for retirement service credit reporting to CalSTRS. For certificated employees, the number of days at each assignment must be counted. This requires an early termination calculation on the old rate and a late hire calculation on the new rate.

Early Termination (Old Rate)
"Old" full-time contract amount ÷ Number of full-time contract days X % FTE X Number of days worked = Earnable *(minus any amount paid)*

Late Hire (New Rate)
"**New**" full-time contract amount ÷ Number of full-time contact days X % FTE X days to be worked = Earnable

CalSTRS no longer requires a "*Change in Base Assignment*" form whenever a change in assignment occurs. See attached Employer Directive 2013-04 CalSTRS No Longer Performs Change of Base Calculations

3. Termination

When a certificated employee terminates employment, the contract must be recalculated to determine final compensation payable.

Calculation Formula
Full-time contract amount ÷ Number of Full-time contract days X % FTE X Number of days worked *minus* Wages paid = Final compensation.

4. Prior-Period Pay Adjustment

When an employee's pay status changes due to a new position, additional educational units or contract settlement, and the effective date is earlier than the current month, retroactive payments are required. You must calculate the monthly rate at the old rate and the monthly rate at the new rate. Use the difference between the monthly rates times the number of retroactive months to find the total amount due.

Example

September 1 – Annual salary is $35,000.00
December 1 – Annual salary changes to $35,500.00 effective September 1

$35,000.00 ÷ 10 = $3,500.00 per month
$35,500.00 ÷ 10 = $3,550.00 per month
New monthly pay rate = $3,550.00
Retroactive pay is $50.00 per month
For 3 months x $50.00 = $150.00

G. CLASSIFIED WORK DAYS AND SALARY COMPUTATION

Classified employees are paid based on a monthly salary. Under Education Code Section 45203, all probationary and permanent employees that are a part of the classified service are entitled to holiday pay.

Classified employees are entitled to vacation pay under Education Code Section 45197. Earned vacation becomes a vested right after completion of the initial probation period. When a classified employee terminates, they are entitled to a lump-sum compensation pay off for all earned and unused vacation. If an employee was advanced vacation, the employer shall deduct the unearned days of vacation from the final pay.

Classified Substitute, Short Term and Limited Term employees are not entitled to vacation under the education code. Districts do have an option to provide vacation pay if they so choose.

Classified Work Days (Based on 12 month employee)

365	Days per Year
-104	Saturdays & Sundays
261	Work Days

H. CLASSIFIED RATE FACTORS

Daily Rate Factors

Many classified employees are paid a monthly salary. In order to pay off vacation upon termination, or to make a deduction if an employee is absent, a factor is used to determine a daily rate. The factor may be the number of workdays (including paid holidays) annually divided into the annual salary.

Most daily rate factors use a number of days per month, divided into the monthly salary rate.

Below are some common factors and the computations for them:

21.67	5 work days per week x 52 weeks = 260 work days per year. 260 divided by 12 months = 21.67 standard work days per month.
21.75	365 days, less 104 weekend days (52 x 2) = 261 work days per year. 261 divided by 12 months = 21.75 standard days per month.
22.00	Real work days in each month vary between: 20, 21, 22 and 23. The average is closest to 22.
Actual Days	Divide the monthly rate by the actual days in a month (least used).

Hourly Rate Factors

To derive an hourly rate from a monthly salary rate, a factor must be used. This is most often used to pay hourly overtime wages. Common factors include:

173.33	8 hours per day x 5 days per week = 40 hours per week 40 hours per week x 52 weeks = 2080 hours per year 2080 hours divided by 12 months = 173.33 standard hours per month
174.00	365 days, less 104 weekend days (52 x 2) = 261 work days per year. 261 days per year x 8 hours = 2088 hours per year. 2088 hours divided by 12 months = 174 standard hours per month.
176.00	If 22 days per month is standard, then 22 days per month x 8 hours per day = 176 standard hours per month.

I. CLASSIFIED LATE HIRE/TERMINATION ADJUSTMENTS

Several factors will determine if an employee will receive a larger salary by

paying the days worked as opposed to docking days not worked. These factors include:

- Number of work days in the adjusted month
- The hire date of the employee
- The daily rate factor method being used

Warning: Not working a full month will impact retirement service credits.

The main idea is to be consistent with the method your district uses for the calculation.

For example a district policy may be as follows

> *When a Classified Employee begins employment on the 2nd through the 15th of a month, deduct payment for days not worked.*
>
> *When a Classified Employee begins employment on the 16th through the 31st of a month, pay the employee for all days worked.*

A district policy may be to pay the daily rate factor for the days worked or pay the monthly salary less the value of the days not worked. If the district wants to give the advantage to the employee, it is sometimes necessary to calculate the adjustment using both methods for comparison. It is still being consistent using two different methods when the goal is to always pay the employee the highest salary calculated.

Late Hire - Example A
Classified New Hire effective June 11th
21 working days in June
12 month employee
Monthly salary = $1,936.00

Method 1
$ 1,936.00 x 12 months = $23,232.00 ÷ 2080 = $11.17 hourly rate
$11.17 hourly rate x 8 hours = $89.36 daily rate
$89.36 x 6 days not worked = $536.16
$1,936.00 - $536.16 = ***$1,399.84 pay for June***

Method 2
$89.36 x 15 days worked = $1,340.40
$1,399.84 – 1,340.40 = $59.44
(This is $59.44 less than Method 1 calculation)
In this case, paying the employee for days worked would have given the employee less salary:

Late Hire - Example B (Comparison)

- Using the same salary and daily rate factor
- Using a month with 23 working days instead of 21
- Using a different hire date

Classified New Hire effective August 17th
23 working days in August
12 month employee
Monthly salary = $1,936.00

Method 1
$1,936.00 x 12 months = $23,232.00 ÷ 2080 = $11.17 hourly rate
$11.17 hourly rate x 8 hours = $89.36 daily rate
$89.36 x 11 days worked = ***$982.96 pay for August***

Method 2
$89.36 x 12 days not worked = $1,072.32
$1,072.32 - $982.96 = $89.36
(This is $89.36 less than Method 1 calculation)
In this case, deducting for days not worked would give the employee less salary:

Termination

When classified employees terminate, it is necessary to determine the actual days worked in the month, pay for any vacation pay of compensatory time owed, and deduct for any advance sick leave use but not earned.

Final payrolls for terminated employees should be processed as soon as possible.

J. CLASSIFIED CHANGE OF ASSIGNMENT

If an employee is ending one assignment during the month and starting a new one, there should be at least two lines with difference pay rate on the retirement report to CalPERS.

K. SUMMER SCHOOL

Summer school pay may be calculated as hourly or daily. Certificated summer school employment is subject to the CalSTRS retirement benefit and payroll deductions.

Ten-month classified employees working summer school would be subject to the California Public Employees' Retirement System (CalPERS) retirement benefit and payroll deductions, if the employee is already a CalPERS member.

Education Code References

Certificated

Section 45040	Deferred Pay
Section 45041/87815	Computation of Salary
Section 45042/87816	Alternative Method for Less Than Full Year
Section 45043/87817	Computation for Employment Beginning in Second Semester
Section 45044/87818	Salary Increase Beginning in Second Semester
Section 45045	Year Round School- Salary
Section 45046	Adjustments to Salaries

Classified

Section 37220	School Holidays
Section 45165	Deferred Pay
Section 45197/88197	Vacation Leave
Section 45203/88203	Classified Holidays

CERTIFICATED

§45040 – Deferred Pay

The governing board of any school district not paying the annual salaries of persons employed by the district in 12 equal monthly payments may withhold from each payment made to each employee an amount equal to 16 2/3 percent thereof.

The total of the amounts deducted from the salary of any employee during any school year shall be paid to him in two equal installments, one installment to be paid not later than the fifth day of August next succeeding, and one installment to be paid not later than the fifth day of September next succeeding.

In the event any employee leaves the service of the district by death or otherwise before receiving such moneys as may be due him, the amount due him shall be paid within 30 days to him or to any other person entitled thereto by law.

§45041 – Computation of Salary

A person in a position requiring certification qualifications who serves less than a full school year shall receive as salary only an amount that bears the same ratio to the established annual salary for the position as the number of working days he serves bears to the total number of working days plus institutes in the annual school term, and any other day when the employee is required by the governing board to be present at the schools of the district. Notwithstanding any provisions of this section to the contrary, a person in a position requiring certification qualifications who serves a complete semester shall receive not less than one-half of the established annual salary for the position. This section shall not be so construed as to prevent the payment of compensation to a person while on leave of absence when the payment of the compensation is authorized by law.

In the event any such person dies during the school year, his estate shall be entitled to receive, as salary owed to the decedent, an amount that bears the same ratio to the established annual salary for the position as the number of working days he served bears to the total number of working days plus institutes in the annual school term, and any other day when the employee was required by the governing board to be present at the schools of the district, less any salary paid to the decedent prior to his death.

§45042 – Alternative Method of Computation/Less Than Full Year

Notwithstanding the provisions of Section 45041, the governing board of a school district may adopt an alternative method of computing the salary received by a person requiring certification qualifications who serves less than a full school year.

Such method shall include the deduction from the employee's regular salary of only that amount actually paid to a substitute or, if a substitute is not employed, the amount which would have been paid to a substitute had a substitute been employed.

For the purposes of this section, the amount which would have been paid to a substitute is that amount established by the district in a published salary schedule for substitute employees.

Such alternative method shall only be applied upon authorization by the school board based upon individual employee application and shall be limited to no more than five days per school year for each employee.

§45043 – Computation for Employment Beginning in Second Semester
Notwithstanding the provisions of Section 45041 or any other provision of law to the contrary, if a person is employed by a school district in a position requiring certification qualifications at the beginning of the second semester of a school year for services during that semester, the compensation of such employee shall be not less than one-half of the annual compensation for that position.

§45044 - Salary Increase Beginning in Second Semester
Whenever a salary schedule increasing the salaries of its certificated employees is adopted by a school district to be effective at the commencement of the second semester of a school year:

(a) The compensation of such employees shall not exceed one-half of the annual compensation for their positions under the former salary schedule for services during the first semester.

(b) The compensation of such employees shall not be less than one-half of the annual compensation for their positions under the newly adopted salary schedule for services during the second semester.

This section shall not be construed to limit the time at which any salary increase ordered by the governing board shall become effective.

§45045 – Year Round School Salary
When a school district operates on a year-round schedule pursuant to Chapter 5 (commencing with Section 37600) of Part 22 of this division, the salary of an employee who is employed for the extended school year and who previously had been assigned to a 9- or 10-month teaching position in the same district shall be adjusted in accordance with the ratio of the extension in the number of days expected to be taught by said employee to the number of days expected to be taught by employees in the district in the school year prior to the commencement of year-round operation.

A full-time probationary or permanent classroom teacher currently employed by a school district which converts to a continuous school program shall not, without his written consent, be required to teach under such program more than 180 days during a school year, or more than the number of days the schools of the district were maintained during the year preceding implementation of the continuous school program, whichever is the greater. This section shall not be construed as limiting the power of school district governing boards to govern the schools of the district, including the assignment of teachers employed by the district.

§45046 – Adjustments to Salaries
Except as otherwise provided in Section 45045, the governing board of a school district in which a continuous school program is in operation pursuant to Chapter 5, (commencing with Section 37600) of Part 22 of this division, but in fewer than all of the schools in the district or with fewer than all of the certificated employees participating

therein, and in which revised salary schedules become effective on a date other than July 1, may adjust the salaries of certificated employees participating in the continuous school program so that the total amount payable to each such employee in a school year does not differ from the salary which would be payable to him over such a period if he were not participating in the program.

CLASSIFIED

§ 37220 – Holidays

(a) Except as otherwise provided, the public schools shall close on the following holidays:
   (1) January 1.
   (2) The third Monday in January or Monday or Friday in the week in which January 15 occurs, known as "Dr. Martin Luther King, Jr. Day." On the Friday preceding which day the schools are closed, schools shall include exercises commemorating and directing attention to the history of the civil rights movement in the United States and particularly the role therein of Dr. Martin Luther King, Jr.
   (3) The Monday or Friday of the week in which February 12 occurs, known as "Lincoln Day." On the day that school is in session prior to the day on which schools are closed for that purpose, all public schools and educational institutions throughout the state shall hold exercises in memory of Abraham Lincoln.
   (4) The third Monday in February, known as "Washington Day." On the Friday preceding, all public schools and educational institutions throughout the state shall hold exercises in memory of George Washington.
   (5) The last Monday in May, known as "Memorial Day."
   (6) July 4.
   (7) The first Monday in September, known as "Labor Day."
   (8) November 11, known as "Veterans Day."
   (9) That Thursday in November proclaimed by the President as "Thanksgiving Day."
   (10) December 25.
   (11) All days appointed by the Governor for a public fast, thanksgiving, or holiday, and all special or limited holidays on which the Governor provides that the schools shall close.
   (12) All days appointed by the President as a public fast, thanksgiving, or holiday, unless it is a special or limited holiday.
   (13) Any other day designated as a holiday by the governing board of the school district.

(b) When any of the holidays on which the schools would be closed falls on Sunday, the public schools shall close on the Monday following.

(c) When any of the holidays on which the schools would be closed falls on Saturday, the public schools shall close on the preceding Friday, and that Friday shall be declared a state holiday.

(d) If any holiday on which the public schools are required to close pursuant to subdivision (a) occurs under federal law on a date different from the date specified in subdivision (a), the governing board of any school district may close the public schools of the district on the date recognized by federal law and maintain classes on the date specified in subdivision (a).

(e) Except for Veterans Day, as designated in paragraph (8) of subdivision (a), the governing board of a school district, by adoption of a resolution, may revise the date upon which the schools of the district close in observance of any of the holidays identified in subdivision (a).

(f) The governing board of a school district may not request a waiver of paragraph (8) of subdivision (a) from the State Board of Education.

37220.5

(a) In addition to the holidays prescribed in Section 37220, public schools may be closed on March 31, known as "Cesar Chavez Day," or the appropriate Monday or Friday following or preceding that date, if the governing board, pursuant to a memorandum of understanding reached pursuant to Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code, agrees to close schools for that purpose.

(b) On March 31 or on the day determined by the governing board, public schools and educational institutions throughout the state may include exercises, funded through existing resources, commemorating and directing attention to the history of the farm labor movement in the United States and particularly the role therein of Cesar Chavez. The State Board of Education shall adopt a model curriculum guide to be available for use by public schools for exercises related to Cesar Chavez Day.

37220.6

(a) There is hereby created the Cesar Chavez Day of Service and Learning program to promote service to the communities of California in honor of the life and work of Cesar Chavez. The program shall be administered by the Governor's Office on Service and Volunteerism, in collaboration with the California Conservation Corps.

(b) The Governor's Office on Service and Volunteerism may make grants based on proposals selected through a competitive process from local and state operated Americorps, National Senior Service Corps, Learn and Serve, or Conservation Corps programs that submit proposals to engage pupils through their schools and school districts in community service that qualifies as instructional time on Cesar Chavez Day, pursuant to Section 37220.5, and that honors the life and work of Cesar Chavez. The programs shall be created and organized in consultation with community groups. The Americorps, National Senior Service Corps, Learn and Serve, or Conservation Corps programs may implement or administer the programs in collaboration with community groups and nonprofit organizations. The proposals shall demonstrate all of the following:

(1) The ways and extent to which the program will be a collaborative effort between schools and the Americorps, National Senior Service Corps, Learn and Serve, or Conservation Corps program.
(2) The ways that the service will be connected to instruction on the life and work of Cesar Chavez provided on Cesar Chavez Day.
(3) The way in which the service provided will make a meaningful contribution to the community.

(c) Grants made pursuant to subdivision (b) shall be in the amount of one dollar ($1) for each participating pupil, or two hundred fifty dollars ($250) for each school, whichever is greater. The Governor's Office on Service and Volunteerism may, at its discretion, adjust the grant amount to account for school district size, the size of the project, and the demand on existing funding. Under no circumstances may the amount granted exceed the amount of funding appropriated to carry out this section.
(d) In order for the community service performed under this program to be counted as instructional time, the service shall be performed under the supervision of a teacher, as defined in subdivision (a) of Section 46300.
(e) The Superintendent of Public Instruction shall develop or revise, as needed, a model curriculum on the life and work of Cesar Chavez and submit the model curriculum to the State Board of Education for adoption pursuant to subdivision (b) of Section 37220.5. Upon adoption, the Superintendent of Public Instruction shall distribute the model curriculum to each school.
(f) It is the intent of the Legislature that nothing in this section, or in the act that adds this section, shall be construed to impose a mandate on school districts.
(g) For the purposes of this section, "school district" includes school districts, charter schools, and county offices of education.

37220.7
(a) In addition to the holidays prescribed in Section 37220, public schools may be closed on the fourth Friday in September, known as "Native American Day," if the governing board, pursuant to a memorandum of understanding reached pursuant to Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code, agrees to close schools for that purpose.
(b) On the fourth Friday in September, or if schools are closed on that date as specified in subdivision (a), on an alternate day determined by the governing board, public schools and educational institutions throughout this state may include exercises, funded through existing resources, commemorating and directing attention to the many contributions that Native Americans have made to this country. The State Board of Education may adopt a model curriculum guide to be available for use by public schools for exercises related to Native American Day.

37220.8.
(a) On and after July 1, 2002, the Governor's Office on Service and Volunteerism may make grants pursuant to subdivision (b) of Section 37220.6 based on proposals

selected through a competitive process from community-based organizations with strong capacity to design and implement programs that provide high quality service and learning opportunities to pupils in kindergarten and in grades 1 to 12, inclusive.

The proposals shall provide all of the following:

(1) Evidence of tax-exempt status pursuant to Section 501(c)(3) of the Internal Revenue Code for all nongovernmental proposals.
(2) Evidence of strong financial management systems as determined by the Governor's Office on Service and Volunteerism.
(3) Experience designing and implementing youth service and learning programs.

(b) Eligible organizations need not have experience administering government funds; however, those organizations that have received government funds shall have a history of effectively administering those funds.
(c) Funding for these community-based organizations is limited to one million dollars ($1,000,000) per year, with single grants not to exceed one hundred thousand dollars ($100,000).
(d) Community-based organizations that do not apply directly to the Governor's Office on Service and Volunteerism for funding pursuant to subdivision (b) of Section 37220.6 remain eligible to receive funds through partnerships with other eligible programs including the programs listed in that subdivision.
(e) This section shall become inoperative on July 1, 2004, and, as of January 1, 2005, is repealed, unless a later enacted statute, which becomes effective on or before January 1, 2005, deletes or extends the dates on which it becomes inoperative and is repealed.

§ 45165 – Deferred Pay

The governing board of any school district not paying the annual or monthly salaries of persons employed by the district in 12 equal monthly payments may withhold, upon election by the individual employee, from each payment made to such employee an amount as follows:

(a) For an employee employed 11 months of a year an amount equal to 8 1/3 percent thereof and the total amount deducted to be paid not later than the 10th day of September next succeeding.
(b) For an employee employed 10 months of a year an amount equal to 16 2/3 percent thereof and the total amount deducted to be paid in two equal monthly installments not later than the 10th day of August and the 10th day of September next succeeding.
(c) For an employee employed nine months a year an amount equal to 25 percent thereof and the total amount deducted to be paid in three equal monthly installments not later than the 10th day of July, the 10th day of August and the 10th day of September next succeeding.

If the provisions of Section 42644 are made applicable to any district the provisions of this section shall apply except that the amount deducted from each regular pay period

and ultimate dates for payment of the amount deducted shall be computed and set in accordance with the system adopted under Section 42644.
Once an employee has elected to be brought under the provisions of this section such election shall not be revocable until the commencement of the next ensuing fiscal year.

However, in the event any employee leaves the service of the district by death or otherwise before receiving such moneys as may be due him, the amount due him shall be paid within 30 days of the last working day to him or any other person entitled thereto by law.

This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

§ 45197 - Vacation Leave

(a) Every public school employer shall grant to regular classified employees an annual vacation at the regular rate of pay earned at the time the vacation is commenced. Such vacation shall be as determined by the public school employer, but not less than five-sixths of a day for each month in which the employee is in a paid status for more than one-half the working days in the month, provided the employee is regularly employed five days per week, seven to eight hours a day. An employee in a paid status for less than one-half the working days in a month shall have his vacation credit accrued on the basis provided for in subdivision (b) or (c).

(b) In lieu of accrual of vacation credit on a monthly basis and proration as prescribed in subdivision (a), a district may provide for accrual of vacation credit on any of the following bases:
   (1) For all employees or classes of employees who work a full workweek of 40 hours the district shall provide 0.03846 hour of vacation credit for each hour of paid service, not including overtime.
   (2) For all employees or classes of employees who work a full workweek of 37.5 hours the district shall provide 0.04087 hour of vacation credit for each hour of paid service, not including overtime.
   (3) For all employees or classes of employees who work a full workweek of 35 hours the district shall provide 0.04379 hour of vacation credit for each hour of paid service, not including overtime.

(c) For all employees regularly employed for fewer than 35 hours a week, regardless of the number of hours or days worked per week, the vacation credit shall be computed at the rate of 0.03846 for each hour the employee is in paid status, not including overtime.

(d) Vacation may, with the approval of the employer, be taken at any time during the school year. If the employee is not permitted to take his full annual vacation, the amount not taken shall accumulate for use in the next year or be paid for in cash at the option of the governing board.

(e) Earned vacation shall not become a vested right until completion of the initial six months of employment

(f) The employee may be granted vacation during the school year even though not earned at the time the vacation is taken.

(g) If an employee is terminated and had been granted vacation which was not yet earned at the time of termination of his services, the employer shall deduct from the employee's severance check the full amount of salary which was paid for such unearned days of vacation taken.

(h) Upon separation from service, the employee shall be entitled to lump-sum compensation for all earned and unused vacation, except that employees who have not completed six months of employment in regular status shall not be entitled to such compensation.

(i) This section shall not apply to substitute, short-term, or limited-term employees, as they are defined in Sections 45103 and 45286, unless such employees are specifically included by the public school employer.

(j) The public school employer may expand the benefits provided for in this section.

(k) This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

§ 45203 – Classified Holidays

All probationary or permanent employees that are a part of the classified service shall be entitled to the following paid holidays provided they are in a paid status during any portion of the working day immediately preceding or succeeding the holiday:

- January 1,
- February 12 known as "Lincoln Day,"
- the third Monday in February known as "Washington Day,"
- the last Monday in May known as "Memorial Day,"
- July 4,
- the first Monday in September known as "Labor Day,"
- November 11 known as "Veterans Day,"
- that Thursday in November proclaimed by the President as "Thanksgiving Day,"
- December 25,
- Every day appointed by the President, or the Governor of this state, as provided for in subdivisions (b) and (c) of Section 37220 for a public fast, thanksgiving or holiday, or any day declared a holiday under Section 1318 or 37222 for classified or certificated employees.

School recesses during the Christmas, Easter, and mid-February periods shall not be considered holidays for classified employees who are normally required to work during that period. However, this shall not be construed as affecting vacation rights specified in this section.

Regular employees of the district who are not normally assigned to duty during the school holidays of December 25 and January 1 shall be paid for those two holidays

provided that they were in a paid status during any portion of the working day of their normal assignment immediately preceding or succeeding the holiday period.
When a holiday listed in this section falls on a Sunday, the following Monday shall be deemed to be the holiday in lieu of the day observed. When a holiday listed in this section falls on a Saturday, the preceding Friday shall be deemed to be the holiday in lieu of the day observed. When a classified employee is required to work on any of these holidays, he or she shall be paid compensation, or given compensating time off, for such work, in addition to the regular pay received for the holiday, at the rate of time and one-half the employee's regular rate of pay.

The provisions of Article 3 (commencing with Section 37220) of Chapter 2 of Part 22 shall not be construed to in any way limit the provisions of this section, nor shall anything in this section be construed to prohibit the governing board from adopting separate work schedules for the certificated and the classified services, or from providing holiday pay for employees who have not been in paid status on the days specified herein. Notwithstanding the adoption of separate work schedules for the certificated and the classified services, on any school day during which pupils would otherwise have been in attendance but are not and for which certificated personnel receive regular pay, classified personnel shall also receive regular pay whether or not they are required to report for duty that day.

In addition to the other paid holidays specified in this section, the classified service may be entitled to a paid holiday on March 31 known as "Cesar Chavez Day," and a paid holiday on the fourth Friday in September known as "Native American Day," provided they are in a paid status during any portion of the working day immediately preceding or succeeding the holiday, if the governing board, pursuant to a memorandum of understanding reached pursuant to Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code, agrees to the paid holiday.
This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240).

OVERTIME

Exempt Employees

The FLSA defines categories of "white collar" employees who are exempt from overtime requirements. The classification of an employee as exempt is based on the employee's actual job duties and not the employee's job title. To be exempt, the employee must meet both the duties and salary tests of their category.

Certificated staff meets the exemption under the professional and/or administrative tests. Some classified employees may also be exempt from overtime by meeting the Executive, Administrative or Computer exemption tests.

"White Collar" Exemptions
Fair Labor Standards Act

Table 1. – Comparison of Salary Levels

EARNINGS	**FINAL REGULATIONS**
Less than $455.00/Week	Guaranteed Overtime
$455 / Week to $100,000 / Year	Standard Duties Test
$100,000 / More than Year	Highly Compensated Test
****Effective December 1, 2016****	
Less than $913.00/Week	Guaranteed Overtime
$913/Week to $47,476.00/Year	Standard Duties Test
$134,004	Highly Compensated Test

Table 2. – Duties Test for Executive Employees

SALARY LEVEL	**FINAL STANDARD TEST $455 per WEEK**
Duties	Whose primary duty is management of the enterprise in which the employee is employed or of a customarily recognized department or subdivision thereof; Who customarily and regularly directs the work of two or more other employees; **and** Who has the authority to hire or fire other employees or whose suggestions and recommendations as to the hiring, firing, advancement, promotion or any other change in status of other employees are given particular weight.

OVERTIME

Table 3. – Duties Test for Administrative Employees	
SALARY LEVEL	**FINAL STANDARD TEST $913 per WEEK**
Duties	Whose primary duty is the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; **and** Whose primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

Table 4. – Duties Test for Professional Employees	
SALARY LEVEL	**FINAL STANDARD TEST $913 per WEEK**
Duties	Whose primary duty is the performance of work requiring knowledge of an advanced type (defined as work which is predominantly intellectual in character, and which includes work requiring the consistent exercise of discretion and judgment) in the field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction; **or** Whose primary duty is the performance of work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.

(See the Fact Sheet #17A from US Department of Labor – Wage and Hour Division)

2. Non-Exempt Employees

Employees who do not qualify as exempt are known as "non-exempt" employees. Non-exempt employees must be paid overtime based on the federal, state, or collective bargaining agreement that provides the best overtime benefit.

3. Federal and State Regulations for Calculating Overtime

To calculate overtime, each workweek must be looked at individually. The Fair Labor Standards Act (FLSA) is the federal law that sets the minimum requirements that govern the rules for paying overtime. Under the FLSA regulations, any employee deemed "non-exempt" must be paid a premium of 50% of the employee's **regular rate of pay** for the hours worked over 40 in a workweek. This is known as time and a half pay. The FLSA does not set any requirements for paying double-time.

The FLSA allows individual states to set higher benefits for overtime pay. The California Labor Code and Wage Orders requires overtime to be paid at a rate of time and a half for hours worked over 8 in a day or 40 in a week. The California Labor Code and Wage Orders also provide for double time to be paid beyond 12 hours in a day or after 8 hours worked on the 7th consecutive day. California school and community college districts are **exempt** from the overtime rules as are set in the California Labor Code and Wage Orders.

4. Overtime Rules for School and Community College Districts

California school and community college districts have three sets of regulations they must apply to assure employees are corrected paid overtime wages:

- Collective Bargaining Agreements
- California Education Code
- Fair Labor Standards Act

Collective bargaining agreements may provide for the best overtime benefit by exceeding the requirements of the Education Code and/or FLSA. In this case, overtime calculations are to be based on the Collective Bargaining Agreements for employees who are covered under the agreement.

If an employee is not covered under the collective bargaining agreement, the California Education Code and FLSA overtime requirements take effect. The California Education Code provides overtime requirements for "non-exempt" employees who have been defined as "Classified Service". (Refer to the Employee Classification Section of this manual for the definition of classified service.)

A "non-exempt" employee who is not covered by collective bargaining or the Education Code should be paid overtime in accordance with the FLSA regulations. The FLSA regulations should also be consulted for other pay situations that are not addressed in a collective bargaining agreement or the Education Code.

5. Identifying Overtime Hours

Several factors must be reviewed to determine if hours worked should be paid as overtime hours. The first factor is what regulation applies to the employee. Is the employee covered under a collective bargaining agreement that addresses overtime? If

so, follow the terms of the collective bargaining agreement. If the collective bargaining agreement does not cover the employee or address overtime pay, review the California Education codes.

When reviewing the Education codes, a determination first has to be made as to whether the employee meets the definition of "classified service" under Education Code Section 45103. If the employee position does not meet the definition, then the employees hours worked should be reviewed to determine overtime based on the Fair Labor Standards Act. *See examples 1-3 on the following pages for how to apply the Education Code in determining overtime hours.*

6. Calculating Overtime Pay Rates

Overtime is calculated based on the employee's "Regular Rate of Pay." The Regular Rate of Pay includes all compensation for employment except payments specifically exempted by the FLSA. This means that if a non-exempt employee receives additional types of pay such as longevity, shift differentials, bilingual pay, cash in lieu of benefits, etc… that pay must be included to determine the overtime rate for the employee. Below is a chart of the types of pay that must be included and can be excluded to determine the Regular Rate of Pay.

Regular Rate Includes	Regular Rate Excludes
Longevity payments	Reimbursed Expenses
Shift Differentials	Gifts on Certain Occasions
Bilingual Stipend	Uniform Allowances
Non-discretionary Bonus- (An agreed upon bonus associated with measure of performance or production of work)	Discretionary Bonus- Employer has discretion to pay and it has not been promised by a contract or other agreement
Vacation, Sick Leave, Holiday or Other Excused paid absences.	
Retroactive and Cost of Living Pay	
Cash in Lieu	

To arrive at the Regular Rate of Pay the formula is
All Includible Compensation Divided into All Hours Compensated

The Fair Labors Standards Act sets the formula for "Regular Rate of Pay" only requiring all includible compensation to be divided by time worked. The California Education Code provides a better benefit for employees defined as "classified service" by requiring the formula to include all hours compensated instead of only hours worked.

Education Code Section 45128/88027
"For the purpose of computing the number of hours worked, time during which an employee is excused from work because of holidays, sick leave, vacation, compensating time off, or other paid leave of absence shall be considered as time worked by the employee."

Calculating Overtime for Hourly Non-Exempt

STEP 1 $\frac{\text{All wages paid includible in overtime rate}}{\text{All hours worked}}$ = Regular Rate of Pay

STEP 2 Regular rate of pay x .5 x hours of overtime = Premium pay for overtime

STEP 3 Total pay for workweek + Premium pay for overtime = Total weekly compensation

NOTE: In step 3 you multiply the regular rate of pay by .5 rather than by 1.5 (for time and one half). This is because the overtime hours have already been calculated at straight time in paying the regular rate.

EXAMPLE 1: A night custodian worked 44 hours during one week at $15.00 per hour.	
STEP 1	44 hours X $15 = $ 660.00
STEP 2	$15.00 x .5 x 4 hours = $30.00 Premium pay
STEP 3	$660.00 + $30.00 = $690.00 Total Weekly Compensation

EXAMPLE 2: A night custodian worked 44 hours during one week at $15.00 per hour, received $350.00 per month for cash in lieu.	
STEP 1	44 hours X $15 = $ 660.00
STEP 2	$350.00 (cash in lieu) X 12 months = $4,200.00/52 week = $80.77
STEP 3	$660.00 + $80.77 = $740.77/44 hours = $16.84 regular rate of pay
STEP 4	$16.84 x .50 = $8.42 per hour
STEP 5	$8.42 + $16.84 = $25.26 OT pay per hour
STEP 6	$25.26 X 4 OT hours = $101.04 OT pay for week
STEP 7	$660.00 + $101.04 = $761.04 Total Weekly Compensation

Calculating Overtime for a Salaried Employee

Since overtime is calculated on hours, it is necessary to convert salaries into hourly rates. In order to do this, the following formulas are used:

Employee's Salary X Numbers of Pay Periods in a Year

52 weeks x Hours Normally Worked Each Week

40 hours per week = 2,080 hours
37.5 hours per week = 1,950 hours
35 hours per week = 1,820 hours

Or

Annual Salary

52 weeks X Hours Normally Worked Each Week

Or
Monthly Salary

Divide monthly amount by 173.33

EXAMPLE:

A non-exempt 12 month employee is paid a monthly salary of $2,000 for working a 40 hour week. Employee has worked 8 hours overtime.

STEP ONE $2,000 x 12 months = $24,000
52 weeks x 8 hours= 2080 = $11.54 Regular rate of pay

STEP TWO $11.54 x 1.5 x 8 hours = $138.48

STEP THREE $138.48 + $2,000.00 = $2,138.48 Total Monthly Pay

In this case, 1.5 was used instead of .5 as the employee has only been paid for working 40 hours not 48.

Paying Overtime on Multiple Assignments

When a non-exempt employee is paid two or more different rates for doing two or more different jobs, overtime is required to be calculated taking all jobs into consideration.

Exception – all these factors must occur:

- —The part time or secondary position is in a different capacity from the primary job and;
- —The work is performed solely at the employee's option and;
- —The work is only performed on an occasional and sporadic basis.

Calculating Multiple Job Rates

Methods allowed for computing the regular rate of pay for overtime purposes

- Weighted Average Method
- Rate in Effect Method
- Employer can pay total overtime at the highest hourly rate of the two jobs

Weighted Average Method

The employee's total straight-time wages for the workweek at all applicable rates of pay are divided by the total hours worked at all jobs he/she performed.

EXAMPLE 1:
Employee works 33 hours at $10 per hour and 10 hours at $15 per hour

Step one: $330.00 + $150.00 = $480.00 total straight compensation
Step two: $480.00/43 hours = $11.16 regular rate of pay
Step three: $11.16 x .5 = $5.58 (additional half time premium)
Step four: $5.58 x 3 (overtime hours) = $16.74 overtime earnings
Step five: $480.00 + $16.74 = $496.74 Total Weekly Compensation

EXAMPLE 2:
Employee works 33 hours at $10 per hour and 10 hours at $15 per hour and receives $500.00 per month for cash in lieu of benefits

Step one: $330.00 + $150.00 = $480.00
Step two: $500.00 x 12 months = $6,000.00/52 weeks = $115.38
Step three: $480.00 + $115.38 = $595.38/43 hour =$13.85 regular rate of pay for week
Step four: $13.85 x .50 = $6.92 (additional half time premium)
Step five: $6.92 x 3 (overtime hours) = $20.76 overtime pay due to employee
Step six: $480.00 + $20.76 = $506.76Total Weekly Compensation

Rate in Effect Method

An employer and employee can mutually agree to compensate for the overtime based on the rate of the job the overtime was earned if;

1) The employee's straight-time average hourly earnings for the workweek at least equals minimum wage.

2) There must be an individual or collective agreement between the employer and employee to pay this method.

3) The overtime hours for which the overtime rate is paid must qualify as overtime hours under FLSA

4) The number of overtime hours paid must equal or exceed the number of overtime hours worked

5) Employer must maintain records showing the date of the agreement and the period it covers and which employee (or group of employees) is covered.

Education Code References

§ 45128/88027 - Overtime
The governing board of each district shall provide the extent to which, and establish the method by which ordered overtime is compensated. The board shall provide for such compensation or compensatory time off at a rate at least equal to time and one-half the regular rate of pay of the employee designated and authorized to perform the overtime.

Overtime is defined to include any time required to be worked in excess of eight hours in any one day and in excess of 40 hours in any calendar week. If a governing board establishes a workday of less than eight hours but seven hours or more and a workweek of less than 40 hours but 35 hours or more for all of its classified positions or for certain classes of classified positions, all time worked in excess of the established workday and workweek shall be deemed to be overtime. The foregoing provisions do not apply to classified positions for which a workday of fewer than seven hours and a workweek of fewer than 35 hours has been established, nor to positions for which a workday of eight hours and a workweek of 40 hours has been established, but in which positions employees are temporarily assigned to work fewer than eight hours per day or 40 hours per week when such reduction in hours is necessary to avoid layoffs for lack of work or lack of funds and the consent of the majority of affected employees to such reduction in hours has been first obtained.

For the purpose of computing the number of hours worked, time during which an employee is excused from work because of holidays, sick leave, vacation, compensating time off, or other paid leave of absence shall be considered as time worked by the employee.

§45130/88029 – Exclusions from Overtime Provisions
Notwithstanding the provisions of Sections 45127 and 45128, a personnel commission, when applicable, or a governing board of a school district may specify certain positions or classes of positions as supervisory, administrative, or executive and exclude the employees serving in such positions and the positions from the overtime provisions.

To be excluded from such overtime provisions, the positions or classes of positions must clearly and reasonably be management positions. In approving positions or classes of positions for exclusion from the overtime provisions, the personnel commission, when applicable, or the governing board of a school district shall certify, in writing, that the duties, flexibility of hours, salary, benefit structure, and authority of the positions or classes of positions are of such a nature that they should be set apart from those positions which are subject to the overtime provisions, and that employees serving in such excluded positions or classes of positions will not be unreasonably discriminated against as a result of the exclusion.

Notwithstanding the provisions of this section, if a person serving in an excluded

position is required to work on a holiday, as provided for in this **code**, or by action of a governing board, he shall be paid, in addition to his regular pay for the holiday, compensation, or given compensating time off, at a rate not less than his normal rate of pay.

§45131/88030 - Overtime; Length of Workday

Notwithstanding the provisions of Section 45127, the workweek shall consist of not more than five consecutive working days for any employee having an average workday of four hours or more during the workweek. Such an employee shall be compensated for any work required to be performed on the sixth or seventh day following the commencement of the workweek at the rate equal to 11/2 times the regular rate of pay of the employee designated and authorized to perform the work.

An employee having an average workday of less than four hours during a workweek shall, for any work required to be performed on the seventh day following the commencement of his workweek, be compensated for at a rate equal to 11/2 times the regular rate of pay of the employee designated and authorized to perform the work.

Positions and employees excluded from overtime compensation pursuant to Section **45130** shall likewise be excluded from the provisions of this section.

This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

Identifying Overtime Hours - Example 1
Classified 4 hour Employee

Workweek is Monday – Sunday Based on 40 hour Week
Collective Bargaining Agreement pays overtime based on Education Code Provisions

August	Reported Hours	Straight Time	1 ½ OT Hours	NOTES
1 Mon	4	4		HOLIDAY
2 Tue	4	4		
3 Wed	4	4		
4 Thur	4	4		
5 Fri	5	5		
6 Sat	6		6	Ed Code 45131- 6th day
7 Sun	4		4	Ed Code 45131- 7th day
Total Weekly	**31**	**21**	**10**	
8 Mon	4	4		
9 Tues	8	8		
10 Wed	8	8		
11 Thur	8	8		
12 Fri	8	8		
13 Sat	6		6	Ed Code 45131- 6th day
14 Sun				
Total Weekly	**42**	**36**	**6**	
15 Mon	4	4		
16 Tue	9	8	1	Ed code 45128- over 8 hrs
17 Wed	9	8	1	Ed code 45128- over 8 hrs
18 Thur	5	5		
19 Fri	4 Sick	4		Paid 4 hours sick leave
20 Sat				
21 Sun				
Total Weekly	**31**	**29**	**2**	
22 Mon	4	4		
23 Tues	4	4		
24 Wed	4	4		
25 Thur	4	4		
26 Fri	4	4		
27 Sat				
28 Sun				
Total Weekly	**20**	**20**		
Monthly Total	**124**	**106**	**18**	

Under the Education Code, this employee is entitled to overtime when working more than 8 hours a day or 40 hours in a work week. Employee is also entitled to overtime for any hours worked on the 6th or 7th day.

Identifying Overtime Hours - Example 2

Classified 3 hour employee

Workweek is Monday – Sunday Based on 40 hour Week
Collective Bargaining Agreement provides overtime based on Education Code Provisions

February	**Reported Hours**	**Straight Time**	**1 ½ OT Hours**	**NOTES**
8 Mon	3	3		
9 Tue	3	3		
10 Wed	3	3		
11 Thur	3	3		
12 Fri	5	5		
13 Sat	6	6		
14 Sun	4		4	Ed Code 45131- 7th day
Total Weekly	**27**	**21**	**4**	
15 Mon	3	3		
16 Tues	8	8		
17 Wed	8	8		
18 Thur	8	8		
19 Fri	8	8		
20 Sat	7	5	2	Over 40 hours a week
21 Sun				
Total Weekly	**42**	**40**	**2**	
22 Mon	3	3		
23 Tue	9	8	1	Over 8 Hours
24 Wed	9	8	1	Over 8 Hours
25 Thur	4	4		
26 Fri	3	3		
27 Sat				
28 Sun				
Total Weekly	**28**	**26**	**2**	
29 Mon	3	3		
01 Tues	3	3		
02 Wed	3	3		
03 Thur	3	3		
04 Fri	3	3		
05 Sat				
06 Sun				
Total Weekly	**15**	**15**		
Monthly Total	**112**	**102**	**8**	

Under the Education Code, this employee is entitled to overtime when working more than 8 hours a day or 40 hours in a work week. Since the employee works less than a 4 hour assignment, overtime for the 6th day follows the rules of Ed Code 45128.
Ed Code 45131 provides for overtime for all hours worked on the 7th day..

Identifying Overtime Hours - Example 3
Short Term- Substitute Employee

July	Reported Hours	Straight Time	1 ½ OT Hours	NOTES
4 Mon	5	5		
5 Tue	5	5		
6 Wed	5	5		
7 Thur	5	5		
8 Fri	5	5		
9 Sat	5	5		
10 Sun	3	3		
Total Weekly	**33**	**33**		
11 Mon	7	7		
12 Tues	7	7		
13 Wed	7	7		
14 Thur	7	7		
15 Fri	7	7		
16 Sat	6	5	1	FLSA over 40 hours
17 Sun				
Total Weekly	**41**	**40**	**1**	
18 Mon	7	7		
19 Tue	9	9		
20 Wed	9	9		
21 Thur	7	7		
22 Fri	7	7		
23 Sat				
24 Sun				
Total Weekly	**39**	**39**		
25 Mon	7	7		
26 Tues	7	7		
27 Wed	7	7		
28 Thur	SICK			Not Paid When Absent
29 Fri	7	7		
30 Sat				
31 Sun				
Total Weekly	**28**	**28**		
Monthly Hours	**141**	**140**	**1**	

Under Ed. Code 45103, a short-term or substitute employee is not considered a "classified" employee for Education Code benefits such as sick leave and overtime. They are not covered under the Education codes for coverage of overtime. However, under the FLSA, they are considered "employees" and must be paid for any time worked over 40 hours in a week.

Fact Sheet: Final Rule to Update the Regulations Defining and Delimiting the Exemption for Executive, Administrative, and Professional Employees

In 2014, President Obama directed the Department of Labor to update and modernize the regulations governing the exemption of executive, administrative, and professional ("EAP") employees from the minimum wage and overtime pay protections of the Fair Labor Standards Act ("FLSA" or "Act"). The Department published a notice of proposed rulemaking on July 6, 2015, and received more than 270,000 comments. On May 18, 2016, the Department announced that it will publish a Final Rule to update the regulations. The full text of the Final Rule will be available at the Federal Register Site.

Although the FLSA ensures minimum wage and overtime pay protections for most employees covered by the Act, some workers, including bona fide EAP employees, are exempt from those protections. Since 1940, the Department's regulations have generally required each of three tests to be met for the FLSA's EAP exemption to apply: (1) the employee must be paid a predetermined and fixed salary that is not subject to reduction because of variations in the quality or quantity of work performed ("salary basis test"); (2) the amount of salary paid must meet a minimum specified amount ("salary level test"); and (3) the employee's job duties must primarily involve executive, administrative, or professional duties as defined by the regulations ("duties test"). The Department last updated these regulations in 2004, when it set the weekly salary level at $455 ($23,660 annually) and made other changes to the regulations, including collapsing the short and long duties tests into a single standard duties test and introducing a new exemption for highly compensated employees.

This Final Rule updates the salary level required for exemption to ensure that the FLSA's intended overtime protections are fully implemented, and to simplify the identification of overtime-protected employees, thus making the EAP exemption easier for employers and workers to understand and apply. Without intervening action by their employers, it extends the right to overtime pay to an estimated 4.2 million workers who are currently exempt. It also strengthens existing overtime protections for 5.7 million additional white collar salaried workers and 3.2 million salaried blue collar workers whose entitlement to overtime pay will no longer rely on the application of the duties test.

* Key Provisions of the Final Rule *

The Final Rule focuses primarily on updating the salary and compensation levels needed for EAP workers to be exempt. Specifically, the Final Rule:

1. Sets the standard salary level at the 40th percentile of earnings of full-time salaried workers in the lowest-wage Census Region, currently the South, which is $913 per week or $47,476 annually for a full-year worker;

2. Sets the total annual compensation requirement for highly compensated employees (HCE) subject to a minimal duties test to the annual equivalent of the 90th percentile of full-time salaried workers nationally, which is $134,004; and

3. Establishes a mechanism for automatically updating the salary and compensation levels every three years to maintain the levels at the above percentiles and to ensure that they continue to provide useful and effective tests for exemption.

Additionally, the Final Rule amends the salary basis test to allow employers to use nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the new standard salary level. The Final Rule makes no changes to the duties tests.

Effective Date

The effective date of the Final Rule is December 1, 2016. The initial increases to the standard salary level (from $455 to $913 per week) and HCE total annual compensation requirement (from $100,000 to $134,004 per year) will be effective on that date. Future automatic updates to those thresholds will occur every three years, beginning on January 1, 2020.

Standard Salary Level

The Final Rule sets the standard salary level at the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region, currently the South ($913 per week, equivalent to $47,476 per year for a full-year worker).

The standard salary level set in this Final Rule addresses our conclusion that the salary level set in 2004 was too low given the Department's elimination of the more rigorous long duties test. For many decades the long duties test—which limited the amount of time an exempt employee could spend on nonexempt duties and was paired with a lower salary level—existed in tandem with a short duties test—which did not contain a specific limit on the amount of nonexempt work and was paired with a salary level that was approximately 130 to 180 percent of the long test salary level. In 2004, the long and short duties tests were eliminated and the new standard duties test was created based on the short duties test and was paired with a salary test based on the long test.

The effect of the 2004 Final Rule's pairing of a standard duties test based on the short duties test (for higher paid employees) with a salary test based on the long test (for lower paid employees) was to exempt from overtime many lower paid workers who performed few EAP duties and whose work was otherwise indistinguishable from their overtime-eligible colleagues. This has resulted in the inappropriate classification of employees as EAP exempt who pass the standard duties test but would have failed the long duties test.

The Final Rule's salary level represents the most appropriate line of demarcation between overtime-protected employees and employees who may be EAP exempt and works appropriately with the current duties test, which does not limit non-EAP work.

The Department also is updating the special salary level for employees in American Samoa (to $767 per week) and the special "base rate" for employees in the motion picture industry (to $1,397 per week).

HCE Total Annual Compensation Requirement

The Final Rule sets the HCE total annual compensation level equal to the 90th percentile of earnings of full-time salaried workers nationally ($134,004 annually). To be exempt as an HCE, an employee must also receive at least the new standard salary amount of $913 per week on a salary or fee basis and pass a minimal duties test. The HCE annual compensation level set in this Final Rule brings this threshold more in line with the level established in 2004 and will avoid the unintended exemption of large numbers of employees in high-wage areas who are clearly not performing EAP duties.

Automatic Updating

The Final Rule includes a mechanism to automatically update the standard salary level requirement every three years to ensure that it remains a meaningful test for distinguishing between overtime-protected white collar workers and bona fide EAP workers who may not be entitled to overtime pay and to provide predictability and more graduated salary changes for employers. Specifically, the standard salary level will be updated to maintain a threshold equal to the 40th percentile of weekly earnings of full-time salaried workers in the lowest-wage Census Region. Similarly, the Final Rule includes a mechanism for automatically updating the HCE compensation level to maintain the threshold equal to the 90th percentile of annual earnings of full-time salaried workers nationally. The Final Rule will also automatically update the special salary level test for employees in American Samoa and the base rate test for motion picture industry employees. The Department will publish all updated rates in the Federal Register at least 150 days before their effective date, and also post them on the Wage and Hour Division's website.

Regularly updating the salary and compensation levels is the best method to ensure that these tests continue to provide an effective means of distinguishing between overtime-eligible white collar employees and those who may be bona fide EAP employees. Experience has shown that these earning thresholds are only effective measures of exempt status if they are kept up to date.

Inclusion of Nondiscretionary Bonuses and Incentive Payments

For the first time, employers will be able to use nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10 percent of the standard salary level. Such payments may include, for example, nondiscretionary incentive bonuses tied to productivity and profitability. For employers to credit nondiscretionary bonuses and incentive payments toward a portion of the standard salary level test, the Final Rule requires such payments to be paid on a quarterly or more frequent basis and permits the employer to make a "catch-up" payment. The Department recognizes that some businesses pay significantly larger bonuses; where larger bonuses are paid, however, the amount attributable toward the standard salary level is capped at 10 percent of the required salary amount.

The Final Rule continues the requirement that HCEs must receive at least the full standard salary amount each pay period on a salary or fee basis without regard to the payment of nondiscretionary bonuses and incentive payments, and continues to permit nondiscretionary bonuses and incentive payments (including commissions) to count toward the total annual compensation requirement. The Department concludes that permitting employers to use nondiscretionary bonuses and incentive payments to satisfy the standard salary amount for HCEs is not appropriate because employers are already permitted to fulfill almost two-thirds of the total annual compensation requirement with commissions, nondiscretionary bonuses, and other forms of nondiscretionary deferred compensation.

Duties Tests

The Final Rule is not changing any of the existing job duty requirements to qualify for exemption. The Department expects that the standard salary level set in this Final Rule and automatic updating will work effectively with the duties test to distinguish between overtime-eligible workers and those who may be exempt. As a result of the change to the salary level, the number of workers for whom employers must apply the duties test to determine exempt status is reduced, thus simplifying the exemption. Both the standard duties test and the HCE duties test remain unchanged.

For additional information, visit our Wage and Hour Division Website: www.wagehour.dol.gov and/or call our toll-free information and helpline, available 8 a.m. to 5 p.m. in your time zone, 1-866-4-USWAGE (1-866-487-9243).

This publication is for general information and is not to be considered in the same light as official statements of position contained in the regulations.

U.S. Department of Labor
Frances Perkins Building
200 Constitution Avenue, NW
Washington, DC 20210

1-866-4-USWAGE
TTY: 1-866-487-9243
Contact Us

California State Teachers'
Retirement System
Executive Office
PO Box 15275
Sacramento, CA 95851-0275
www.CalSTRS.com

August 28, 2013

TO: All County Superintendents of Schools
District Superintendents of Schools
Community College Districts and
Other Employing Agencies

FROM: Jack Ehnes
Chief Executive Officer

SUBJECT: Employer Directive 2013-04
Supersedes Administrative Directive 89-5 Amended, dated March 9, 1994
CalSTRS No Longer Performs Change of Base Calculations

PURPOSE

The purpose of this directive is to inform employers that CalSTRS no longer performs change of base calculations.

SCOPE

This directive applies to all county superintendents of schools, school districts, community college districts, and other employing agencies that employ persons to perform creditable service under the CalSTRS Defined Benefit Program, Defined Benefit Supplement Program and Cash Balance Benefit Program.

DISCUSSION

A change of base is a manual calculation that CalSTRS performed when a member changed positions in a school year that require different base days to fulfill the requirements of full time. While the member may have worked the entire school year, the member did not work the full complement of base days to earn a full year of service credit. For example, a teacher begins the school year working in a full-time position that requires 185 days. That teacher worked 100 of the 185 days and then is hired in a new full-time position that requires 215 days. Since the second position has a higher base day requirement and the teacher started the position late, the teacher cannot fulfill the higher base day requirement. The change of base calculation would modify the compensation earnable to grant the member a full year of service credit.

Upon review of Education Code sections 22701, “Computation of service to be credited”, 22115, “Compensation earnable”, and 22138.5, “Full-time minimum standard”, CalSTRS does not have the authority to grant service credit for which service has not been performed nor compensation paid. Therefore, CalSTRS has discontinued processing change of base requests.

ACTION

Please refer questions concerning this directive to your CalSTRS Member Account Services Representative.

Section 4: Pay Deductions

Section 4
PAYROLL DEDUCTIONS

PAYROLL DEDUCTIONS

A. VOLUNTARY DEDUCTIONS

Voluntary deductions are deductions that employees may choose to have deducted from their paychecks. Authorization in writing should be received from the employee before setting up the vendor deduction. Employees should also put in writing any changes or termination of the deduction. Districts have a choice in whether to set up a new vendor for a voluntary deduction in most cases. In the case of a Section 125 plan or a 403 (b) and 457 (b) plan, specific documentation may be required.

While 403 (b) (TSA) deductions are voluntary, state law requires a district who offers TSA's to allow any vendor participation that meets the district's vendor requirements. District requirements may include following solicitation rules on campus for enrolling employees and providing a hold harmless agreement.

Voluntary deductions may include but are not limited to:

- insurance premiums
- credit union
- 403 (b) and 457 (b)
- Section 125 Plan
- savings bonds
- charitable contributions
- association dues
- income protection plans
- union dues

B. STATUTORY DEDUCTIONS

Statutory deductions are deductions that are required to be taken from an employee's pay according to federal or state laws or collective bargaining. Districts do not have a choice in allowing or disallowing statutory deductions.

Statutory deductions for membership in CalSTRS and CalPERS will occur when the employee has met certain qualifications as set by the retirement systems. Social Security and Medicare deductions also have a set of qualifications that must be followed to determine if they apply to an employee. California state disability (SDI) deductions will apply to a district that has entered into a voluntary agreement to provide this benefit to their employees. Any employees in the coverage group of the plan would be required to have deductions taken from their paychecks.

PAYROLL DEDUCTIONS

Statutory deductions may include but are not limited to:

- Federal and State income taxes
- State Disability
- Social Security/Medicare
- CalSTRS or CalPERS
- Alternative Retirement Systems
- Union Dues for employees covered under collective bargaining

C. INVOLUNTARY DEDUCTIONS

Wage deduction has proven to be an effective way for federal and state agencies to collect money that it owed them by employees. Creditors may also go to court to have an employee served with a garnishment to collect on a debt or obligation that is delinquent. Employees with child support or spousal obligations may also be required through court orders to have a deduction made through their paycheck. Over two-thirds of all child support orders are now collected through payroll deductions.

Involuntary deductions are regulated by federal and state laws as to the amount that can be deducted from the employee. Each type of order has their own requirements for calculating deductions and meeting remittal timelines. In California, most county offices process involuntary deductions for their school districts. In any case, the processor must know and follow all the requirements associated with the involuntary deduction. Schools and county offices must process and withhold on all orders until the time they receive a follow up termination form from the agency. Employees that do not agree with the order will need to contact the agency and work through them for a release to the district. Districts and county offices that do not process the involuntary deductions correctly are liable for any payments due.

Involuntary deductions may include but are not limited to:

- IRS Levies
- Franchise Tax Board Levies
- Child Support and Spousal Support Orders
- Medical Support Orders
- Bankruptcy Orders
- Student Loans
- DMV
- Creditor Garnishments
- Administrative Wage Garnishments

PAYROLL DEDUCTIONS

D. PAYROLL DEDUCTIONS FOR MONEY OWED TO THE EMPLOYER

The California Labor Codes along with court decisions set the requirements for when an employer can deduct money owed to them through a deduction of an employee's paycheck. An employer can lawfully withhold amounts from an employee's wages only when:
(1) Required or empowered to do so by state or federal law;

(2) When a deduction is expressly authorized in writing by the employee to cover insurance premiums, benefit plan contributions or other deductions not amounting to a rebate on the employee's wages; or

(3) When a deduction to cover health, welfare or pension contributions is expressly authorized by a wage or collective bargaining agreement. (Labor Code §§ 221, 224)

Although a wage garnishment is a lawful deduction from wages under Labor Code § 224, an employer cannot discharge an employee because a garnishment of wages has been threatened or if the employee's wages have been subjected to garnishment for the payment of one judgment. (Labor Code § 2929(a))

The ability of employers to deduct amounts from an employee's wages due to cash shortage, breakage, or loss of equipment is specifically regulated by the Industrial Welfare Commission Orders and limited by court decisions (*Kerr's Catering v. Department of Industrial Relations* (1962) 56 Cal.2d 319). Districts should check with legal counsel before making any of these payroll deductions.

In addition, there have been several court decisions that significantly restrict an employer's ability to take a deduction from an employee's wages for overpayments without written approval from the employee; (*Barnhill v. Sanders* (1981) 125 Cal.App.3d 1.)

Labor Code Section 224 clearly prohibits any deduction from an employee's wages which is not either authorized by the employee in writing or permitted by law. Court cases have also concluded that the balloon (lump sum) payment of an outstanding balance cannot be taken all at once because the employment relationship ends, even when the employee has given his or her written consent to such a payment; C*SEA v. State of California* (1988) 198 Cal.App.3d 374

California State Employees' Assn. v. State Of California (1988) 198 CA3d 374

[A037963
Court of Appeals of California, First Appellate District, Division Five
Feb., 2, 1988]

CALIFORNIA STATE EMPLOYEES' ASSOCIATION et al., Plaintiffs and Appellants, v. THE STATE OF CALIFORNIA et al., Defendants and Respondents

Opinion by Haning, J., with Low, P. J., and King, J., concurring.

COUNSEL

Christine A. Bologna and Edmund K. Brehl for Defendants and Respondents.

Robert L. Mueller and Gary P. Reynolds for Plaintiffs and Appellants.

OPINION

HANING, J.

Plaintiffs/appellants California State Employees' Association et al., appeal from a judgment denying their petition for writ of mandate to compel respondents State of California et al., to make full salary payments to their employees without deductions to recoup prior alleged overpayments. fn. 1 We conclude that the challenged salary deductions violate the attachment and wage garnishment laws, and reverse.

In August 1986 an audit report of the California Medical Facility at Vacaville reported 731 outstanding erroneous salary advances totalling $463,113. In mid-October 1986 respondents began notifying affected employees by form letter of the amount of and reason for the individual overpayments. fn. 2 The letter set out a repayment plan to deduct up to $400 from the net salary warrant and 40 percent of net overtime pay beginning {Page 198 Cal.App.3d 376} with the October pay period. Employees were given seven days within which to negotiate a modification of the repayment schedule due to undue hardship, and any other questions were directed to the business office. At least one employee received a memorandum from the personnel office in mid-October entitled "Accounts Receivable," which specified the amount of and reason for the overpayment and gave the name of a contact person to call if there were questions.

[1a] Respondents contend that Government Code section 17051 authorizes the salary withholding method utilized herein, and rely on Geftakys v. State Personnel Board (1982) 138 Cal.App.3d 844 [188 Cal.Rptr. 305] as authority for their position.

Appellants contend that the general provisions of Government Code section 17051 must give way to the specific statutory scheme of the attachment law (Code Civ. Proc., § 481.010 et seq.) and the wage garnishment law (Code Civ. Proc., § 706.010 et seq.), and that respondents' recoupment procedure constitutes an unlawful attachment or garnishment in violation thereof, or an unlawful setoff in contravention of the policies underlying the attachment and wage garnishment statutes.

Government Code section 17051, states: "Whenever any warrant is drawn in favor of a payee having a claim against the State and is delivered to a State agency for delivery to a payee, and prior to delivery to the payee any facts or circumstances exist which would affect the validity or alter the amount of the claim, the person authorized to make payments out of any funds under the direct control of the State agency may indorse and deposit the warrant in the treasury to the credit of the fund or appropriation upon which it was drawn or deposit it to the credit of the appropriate account under his control. Where such a warrant is deposited to the account under the control of the State agency, it shall, when necessary, pay the portion of the claim then due and payable and return the balance to the treasury to the credit of the fund or appropriation upon which the warrant was drawn."

In Geftakys v. State Personnel Board, supra, 138 Cal.App.3d 844, a state hearing officer who had been overpaid challenged the state's recoupment of the overpayment by means of salary deductions under Government Code section 17051. The Court of Appeal held that the deductions were authorized by Government Code section 17051, but it was not confronted with and thus did not decide the issues raised in the instant case. Geftakys was decided in 1982, but was dealing with a salary dispute which arose in 1973-1974. The current attachment law did not become operative until 1977, and the wage garnishment law became operative July 1, 1983. As a {Page 198 Cal.App.3d 377} consequence, Geftakys lends no support for respondents' position. (See, e.g.,9 Witkin, Cal. Procedure (3d ed. 1985) Appeal, §§ 783-784.)

Both the wage garnishment law and the attachment law protect wages from creditors. The wage garnishment law provides the exclusive judicial procedure by which a judgment creditor can execute against the wages of a judgment debtor, except for cases of judgments or orders for support. (Code Civ. Proc., § 706.020.) fn. 3 It limits the amount of earnings which may be garnished in satisfaction of a judgment and establishes certain exemptions from earnings which may not be garnished. (See Code Civ. Proc., §§ 706.050-706.052.) The attachment law expressly prohibits any prejudgment attachment or levy of execution against wages. (Code Civ. Proc., § 487.020, subd. (c).)

Insofar as the attachment law and wage garnishment law reflect or establish public policy, it is obvious that they provide substantial protection for wages against both pretrial attachments and enforcement of judgments. [2] "The policy underlying the state's wage exemption statutes is to insure that regardless of the debtor's improvidence, the debtor and his or her family will retain enough money to maintain a basic standard of living, so that the debtor may have a fair chance to remain a productive member of the community. [Citation.] Moreover, fundamental due process considerations underlie the prejudgment attachment exemption. Permitting appellant to reach respondent's wages by setoff would let it accomplish what neither it nor any other creditor could do by attachment and would defeat the legislative policy underlying that exemption. We conclude that an employer is not entitled to a setoff of debts owing it by an employee against any wages due that employee." (Barnhill v. Robert Saunders & Co. (1981) 125 Cal.App.3d 1, 6 [177 Cal.Rptr. 803].)

In Barnhill, a private employer deducted from an employee's final paycheck the balance of a promissory note which the employee owed to the employer. No statute authorized the deduction, and the Labor Code required immediate payment of unearned wages at the time of discharge. Despite these distinctions from the instant case however, the Barnhill court's statement of public policy is correct. {Page 198 Cal.App.3d 378}

[1b] We agree with appellants that the specific provisions of the attachment and wage garnishment laws take precedence over the general provisions of Government Code section 17051. (See Code Civ. Proc., § 1859; Agricultural Labor Relations Bd. v. Superior Court (1976) 16 Cal.3d 392, 420 [128 Cal.Rptr. 183, 546 P.2d 687].) Government Code section 17051 deals generally with "claim[s] against the State," and refers merely to "facts or circumstances ... which would affect the validity or alter the amount of the claim." (Italics ours.) It also requires the agency in question to "pay the portion of the claim then due and payable." (Italics ours.) Presumably, wages actually earned during the current pay period are due, and the fact that the employee owed a debt to the state, even for a prior overpayment, does not "affect the validity or alter the amount of the [current] claim" for wages earned. We conclude that this general language is superseded by the specific provisions of the attachment and wage garnishment laws protecting earnings from such extra-judicial seizures. (See also Randone v. Appellate Department (1971) 5 Cal.3d 536 [96 Cal.Rptr. 709, 488 P.2d 13].)

In light of our resolution of this issue it is not necessary to reach appellants' remaining contentions.

The judgment is reversed. The matter is remanded with instructions to issue the writ commanding respondents to make normal salary payments to the affected parties without the deductions at issue herein.

Low, P. J., and King, J., concurred.

FN 1 Also appealing are Local 1000 of Service Employees International Union, AFL-CIO; Lois Jennings; Lisa Shepherd; and Joyce Thomas on behalf of themselves and others similarly situated. Also responding are California Department of Corrections and its director, Daniel McCarthy; and Eddie Ylst, Superintendent of the California Medical Facility.

FN 2 Appellants allege at least one employee suffered pay deductions without receiving prior notice. Since appellants did not raise this issue in their petition for writ of mandate or to the trial court, we need not consider this contention on appeal. (Estate of Westerman (1968) 68 Cal.2d 267, 278-279 [66 Cal.Rptr. 29, 437 P.2d 517].)

FN 3 Code of Civil Procedure section 706.020 states: "Except for a wage assignment for support, the earnings of an employee shall not be required to be withheld by an employer for payment of a debt by means of any judicial procedure other than pursuant to this chapter." "Earnings" is defined as "compensation payable by an employer to an employee for personal services performed by such employee, whether denominated as wages, salary, commission, bonus, or otherwise." (Code Civ. Proc., § 706.011, subd. (a).)

The wage garnishment law applies to public employees. (Code Civ. Proc., § 708.720, subd. (b).)

Section 5: Withholding
Federal and State Taxes

Section 5
WITHHOLDING FEDERAL & STATE TAXES

WITHOLDING FEDERAL & STATE TAXES

Income Tax Withholding

Statutory tax withholdings are mandatory taxes that are contributed by the employee to the taxing agency. Withholdings made by the employee go to his/her individual employee record and are reported annually on Form W-2. The employer matches social security taxes paid, as well as Medicare contributions. The employer is responsible for state unemployment contributions. In most cases, employees pay the contributions for State Disability Insurance unless the district has an agreement to pay these contributions on behalf of the employee. Districts are not required by state regulation to participate in the State Disability Insurance Program.

Federal Form W-4 Employee Withholding Allowance Certificate

The Form W-4 is the federal document that informs employers of their employee's tax status for purposes of withholding federal income taxes. Employees are required by federal law to complete and submit a Form W-4 to their employer. Form W-4 information includes the employee's name, address, social security number, marital status and the number of withholding allowances the employee is claiming.

Employees can file a new Form W-4 at anytime. A Form W-4 remains in effect until the employee submits a new form. An exception would be employees who claim exempt from federal income tax withholding. Claiming exempt from withholding requires the filing of a new Form W-4 no later than February 15 of each year.

The employer should have on file a signed Form W-4 for all newly hired employees on or before the first day of employment. The form is effective with the employee's first pay period. If a new employee fails to submit a Form W-4, the employer is required to withhold at the single, with no allowances, withholding rate.

When requested by the IRS, you must make original Forms W-4 available for inspections by an IRS employee. You may also be directed to send certain Forms W-4 to the IRS.

If the IRS notifies you in writing an employee isn't entitled to claim exemption from withholding or a claimed number of withholding allowances, you must withhold federal income tax based on the effective date, marital status, and maximum number of withholding allowances specified in the IRS notice (commonly referred to as a "lock in letter"). Employees cannot change their exemptions if the employer has received a lock-in letter from the IRS.

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Exemption from Federal Income Tax Withholding

An employee may claim exempt from withholding if:

- There was not federal income tax liability due in the previous year and ;
- Expects no liability in the current year and
- Has not been limited to the number of exemptions by the IRS through a notice to the employer. (Note that the exemption applies to both federal and state income tax withholding)
- The exemption is good for one year.

If the employee's status remains exempt for the following year, a new exempt Form W-4 must be filed by February 15 of that applicable year. For an upcoming tax year, employees that can no longer claim the exempt status have until December 1 of the current year to file a new Form W-4. The employer is required to withhold as single with no allowances if an employee fails to submit a new Form W-4 for the above situations.

Students are not automatically exempt from federal income tax withholding. Students claimed as a dependent by another individual or who have total earned income that exceeds $950 or unearned income that exceeds $300.00 may not claim exempt.

Invalid Forms W-4

Employers have a responsibility not to accept and withhold on any invalid Forms W-4. A Form W-4 is invalid when:

- The language or format of the form has been altered including additions and deletions
- The form is not signed or completed properly
- The employee indicates to the employer that the information on the form is incorrect
- A flat dollar amount or percentage is requested for withholding.

The employee should be informed by the employer that a new form is required for any invalid Forms W-4. If the employee fails to submit a new form, withholding must be based on the employee's last valid Form W-4. When a previous Form W-4 does not exist, the employer is required to withhold on the employee as single with no allowances.

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Employer Reporting Requirements
Effective April 14, 2005, the requirement to submit copies of Forms W-4 (*Employee's Withholding Allowance Certificate*) that show withholding of more than 10 allowances or that show an exempt filing was eliminated. IRS [70 F.R. 19694, 4-14-05]. Regulations now require an employer to submit copies of Forms W-4 to the IRS only after the service requests them in writing.

Do not send W-4 forms to the Franchise Tax Board that have more than 10 allowances or when an employee files exempt. If the IRS instructs you to withhold federal income tax based on a certain withholding status, you are required to use the same withholding status for state income tax withholding.

IRS Notice to the Employer (The "Lock-in Letter")
Employers may receive a notice from the IRS (commonly referred to as a "lock-in letter") specifying the maximum number of withholding exemptions permitted for a specific employee. Lock-in letters are to take effect no earlier than the first pay period beginning at least 60 days after the date of the letter. During this period, the employee can challenge the lock-in letter by providing a new Form W-4 and written statement in support directly to the IRS.

If the employee gives a new Form W-4 to the employer, the employer should disregard it until notified by the IRS to withhold based on that form. However, if, at any time, the employee furnishes the employer with a Form W-4 that claims *fewer* withholding exemptions than the maximum number specified in the lock-in letter, then the employer should withhold based on that Form W-4.

In addition to the lock-in letter, the IRS will provide the employer with an "employee notice" (the IRS will also mail a similar notice to the employee's last known address). If the employee is still employed by the employer when the lock-in letter and notice are received, the employer must give the notice to the employee within 10 business days of receipt. If the employee is no longer employed by the employer, the employer must send a written response stating that fact to the IRS office designated in the notice.

The withholding instructions in the lock in letter also applies to state income tax withholding, you are required to use the same withholding that is stated in the lock in letter.

Assisting Employees in Completing Form W-4
Employers should refrain from assisting or giving tax advice to employees in regards to complete Form W-4. Providing information to your employees such as when a change should be made, or when you must submit Forms W-4 to the Internal Revenue Service is acceptable. However, be aware not to advise your employees of how many allowances they should take or how much they should withhold.

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A worksheet is attached to Form W-4 that will guide employees through the steps to calculate eligible allowances. Employers can also refer employees to IRS publications:

- Publication 919, “Is My Withholding Correct?”
- Publication 505, “Tax Withholding and Estimated Tax

Wage Withholding For Nonresident Alien Employees IRS Notice 2005-76

The IRS has specific procedures for determining the amount employers must withhold from nonresident alien employees' wages for services performed in the U.S. There are also specific rules for how a nonresident alien employee must complete Form W-4 (Employee's Withholding Allowance Certificate).

Income tax withholding is required to be calculated on wages of nonresident alien employees (except for students and business apprentices from India) by adding an amount to the wages of the nonresident alien employee solely for purposes of calculating their income tax withholding for each payroll period. The specific amount depends on the payroll period. Employers will determine income tax withheld by applying the tables to the sum of the wages paid for the payroll period plus the additional amount.

Beginning with wages paid on or after January 1, 2010, employers are required to calculate income tax withholding under section 3402 of the Code on wages of nonresident alien employees by making two modifications rather than the one modification described in the table above. First, employers need to add an amount to wages before determining withholding under the wage bracket or percentage method in order to offset the standard deduction built into the withholding tables. Second, employers need to determine an additional amount of withholding from a separate table applicable only to nonresident alien employees to offset the effect of the Making Work Pay Tax Credit built into the withholding tables. The specific steps for each of these two modifications are set forth in Publication 15 and other IRS forms or publications.

$151.00 for a weekly payroll period;
$301.90 for a biweekly payroll period;
$327.10 for a semimonthly payroll period;
$654.20 for a monthly payroll period;
$7850.00 for an annually payroll period;

Non- Resident Alien Employee's W-4

Nonresident alien employees are required to:

- Not claim exemption from withholding;
- Request withholding as if single, regardless of actual marital status;

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- Claim only one allowance. However, residents of Canada, Mexico, or South Korea may claim more than one allowance; and
- Write "Nonresident Alien" or "NRA" above the dotted line on line 6 of Form W-4.

Earned Income Credit-Employee Required Notification

Employers are obligated to inform certain employees that they may be eligible for the credit. Employers must furnish a written notice explaining the earned income credit to all employees who have no income tax withheld and did not claim exemption from withholding on the Form W-4. The Internal Revenue Service provides Notice 797 "You May Be Eligible for a Refund on Your Federal Income Tax Return Because of the Earned Income Credit". Employers must furnish this notice to employees within one week before or after the date they give their employees Form W-2. If the notice isn't given out with the Form W-2, the written notice must be furnished by direct hand deliver to each employee, or it must be sent to the employees' home by first class mail. Employers won't meet the requirements for notification if the notice is sent through inter-office mail or posted on a bulletin board. Employers can satisfy the notification requirement by printing the notice on the reverse of the employee's W-2 form.

Effective January 1, 2008, a new California law (AB 650) requires that employers with employees covered under California Unemployment Insurance Code provide all such employees a special notice of their possible eligibility to take advantage of the federal Earned Income Tax Credit (AEIC). The notice is to be either hand-delivered or mailed within one week of the date the IRS Form W-2 is sent to employees.

While an employer can create its own notice, it must contain substantially the same language as the statutory language, so there is not much reason, other then to augment the statutory notice, to use anything other than the statutory language which reads as follows:

BASED ON YOUR ANNUAL EARNINGS, YOU MAY BE ELIGIBLE TO RECEIVE THE EARNED INCOME TAX CREDIT FROM THE FEDERAL GOVERNMENT. THE EARNED INCOME TAX CREDIT IS A REFUNDABLE FEDERAL INCOME TAX CREDIT FOR LOW-INCOME WORKING INDIVIDUALS AND FAMILIES. THE EARNED INCOME TAX CREDIT HAS NO EFFECT ON CERTAIN WELFARE BENEFITS. IN MOST CASES, EARNED INCOME TAX CREDIT PAYMENTS WILL NOT BE USED TO DETERMINE ELIGIBILITY FOR MEDICAID, SUPPLEMENTAL SECURITY INCOME, FOOD STAMPS, LOW-INCOME HOUSING OR MOST TEMPORARY ASSISTANCE FOR NEEDY FAMILY PAYMENTS. EVEN IF YOU DO NOT OWE FEDERAL TAXES, YOU MUST FILE A TAX RETURN TO RECEIVE THE EARNED INCOME TAX CREDIT. BE SURE TO FILL OUT THE EARNED INCOME TAX CREDIT FORM IN THE FEDERAL INCOME TAX RETURN BOOKLET. FOR INFORMATION

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REGARDING YOUR ELIGIBILITY TO RECEIVE THE EARNED INCOME TAX CREDIT, INCLUDING INFORMATION ON HOW TO OBTAIN THE IRS NOTICE 797 OR ANY OTHER NECESSARY FORMS AND INSTRUCTIONS, CALL THE INTERNAL REVENUE SERVICE BY CALLING 1 800 829 3676 OR THROUGH ITS WEBSITE AT WWW.IRS.GOV.

Social Security Tax – OASDI

Prior to 1986, employees of state and local governments weren't subject to social security or Medicare tax unless covered under a voluntary agreement (§218 agreement) with the Department of Health and Human Services(HHS). Effective April 1, 1986, certain employees were mandated to be covered for Medicare purposes only. The 1990 Omnibus Budget Reconciliation Act of 1990 (OBRA '90) extended Social Security and Medicare coverage for state and local government employees who were not members of a qualified public employee retirement system.

Districts may have employees that do not qualify to contribute to Social Security but may qualify for Medicare under the regulations or a separate 218 Agreement for Medicare only. If an employee qualifies for Social Security coverage they must also pay into Medicare.

For 2018, it is the employer's responsibility to withhold 6.2% on the first $128,400 of Social Security taxable wages of its employees. Employers are required to contribute 6.2% of Social Security taxable wages. If the employer fails to withhold or collect Social Security, they are also responsible for the employee's share.

What is a Section 218 Agreement?

A Section 218 Agreement is a written voluntary agreement between a state and the SSA pursuant to the provisions of Section 218 of the Act to provide social security and Medicare or Medicare-only coverage for state and local government employees. The term refers to the original agreement and all subsequent modifications. These agreements can cover services of employees who are covered by a public retirement system as well as those who are not. To determine whether your entity is covered under a Section 218 Agreement, or needs to execute one, contact your State Social Security Administrator on-line at www.ncsssa.org.

Employees Subject to Social Security Coverage

All full-time and part-time, temporary, and seasonal employees who are not participating in a qualified retirement system are subject to social security and Medicare coverage. Part-time, seasonal, and temporary employees must be fully vested in a plan to avoid social security coverage. To be fully vested, an employee upon separation from employment must have constructive receipt of a payment equal to 7.5% (plus interest)

of the compensation earned while participating in the plan. The contribution can come entirely from the employer or employee or a combination of both.

Many employees are covered under Social Security because the retirement system they are a member of provides a Section 218 agreement with Social Security that mandates their coverage. This is very common for CalPERS employees but not CalSTRS employees.

Rehired Annuitant

OBRA '90 specifically excludes a qualified retired annuitant from mandatory social security coverage if they are rehired with an employer that participates in the same retirement plan from which they retired. To be considered a qualified retired annuitant, the employee must be receiving retirement benefits or has reached normal retirement age under the retirement plan.

> **Example:**
> A teacher retires from a school district that participates in the State Teachers Retirement System and begins receiving retirement benefits from the plan. The retiree is hired to substitute teach in a school district that also participates in the State Teachers Retirement System. The retiree is considered a qualified rehired annuitant and is not required to be covered by the OBRA 90' provisions of social security. The retiree would however qualify for Medicare coverage being hired after March 31, 1986.

Student Social Security Exclusions

K-12 Students

Generally, Students are exempt from social security and Medicare coverage if their services are performed in a public or private educational institution where they are enrolled and regularly attending classes. The service must be performed concurrently with attending classes. Students who work during the summer break who are not attending classes would qualify for social security coverage until they returned to school. The school for which the work is being done does not have to be the same school the student is attending if both are considered the same employing entity.

> **Example:**
> A student attending a high school in school district X works after school in an elementary school also in school district X. Both schools are an integral part of school district X, so the student would be exempt from coverage.

WITHOLDING FEDERAL & STATE TAXES

Community College Students

Internal Revenue Procedure 98-16 has clarified the standards for determining when and if community college students will be exempt from social security coverage. The revenue procedure states that the student must be attending classes at least on a half-time basis of what is required of a full time student. For example, if the college requirement to be a full time student is taking 12 units, the half-time requirement would be taking 6 units. Also eligible are students who are in their last semester and enrolled for the number of hours needed to complete their study even if enrolled for less than the half-time requirements.

During a normal school break period the student can still work at the college and qualify for a social security exemption if the following occurs:

1) The student was exempt from social security on the last day of classes or exams prior to the school break;

2) And will be enrolled for the first academic period following the break;

3) And will be on semester break for no longer than 5 weeks.

The determination of student status should be made at the end of the drop-add period and may be adjusted thereafter at the college's option. If the student is placed on the payroll before the drop-add period, the college can base the qualifications on the hours the student is currently registered until the drop-add period occurs.

Career Employees - A student of the community college may not be exempt from social security if considered a career employee. A career employee is someone whose employment cannot generally be considered to be incident to and for the purpose of pursuing a course of study. A career employee is also defined as someone who is eligible to participate in any 401(a) retirement plan of the community college.

If a student is working in multiple positions and any one of the positions meet the above requirements as a "career position", the student looses the social security exemption for all positions.

Required SSA Form 1945

The Social Security Protection Act of 2004 requires school districts, to provide a statement to new employees hired in a job not covered under Social Security. The

statement explains how a pension from that job could affect future Social Security benefits to which they may become entitled.

Form SSA-1945, Statement Concerning Your Employment in a Job Not Covered by Social Security is the document that employers should use to meet the requirements of the law. The SSA-1945 explains the potential effects of two provisions in the Social Security law for workers who also receive a pension based on their work in a job not covered by Social Security.

The completed form will be sent by the district directly to the retirement plan agency that covers the employee for retirement purposes.

Who Is Exempt from Completing the Form SSA-1945?

- Employees hired before January 1, 2005.
- Employees who contribute into Social Security through their employment with the school district.
- Students who are employed by the district and do not qualify for membership in the retirement system, and do not pay into Social Security under the Social Security student provision.

District Action:

- Prior to the start of employment, give the statement to all newly hired employees not contributing into Social Security.
- Verify that the employee has signed the form and filled in their Social Security Number.
- Keep a copy of the signed form in the employee's personnel file.
- Submit a copy of the signed form directly to the appropriate retirement plan agency.

Procedures for Obtaining SSA-1945 Forms

Copies of the SSA-1945 are available online at the Social Security website, www.socialsecurity.gov/form1945. Paper copies can be requested by email at oplm.oswm.rqct.orders@ssa.gov or by fax at 410-965-2037.

- The request must include the name, complete address, telephone number and contact person of the employer.
- Forms will not be sent to a post office box. Use the district's street address.
- Refer to Inventory Control Number (ICN) 276950 when placing the order.

Medicare Tax: Coverage for Public Schools

Section 13205 of the Consolidated Omnibus Budget Reconciliation Act of 1985 (OBRA 85) amended Section 3121 of the Internal Revenue Code. In general, the amendment applies

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Sections 3101(b) and 3111(b) the hospital insurance (Medicare) tax portion of the Federal Insurance Contribution Act (FICA), to wages for services rendered after March 31, 1986, of newly hired employees of states political subdivisions. Previously, most employees of state and political subdivisions were not covered under FICA, as their services were accepted from the term "employment" by Section 3121(b) (7); (IRS Notice 767, July 1986.)

The Medicare tax only coverage applies to employees not already covered under a State's Social Security Agreement. Implementation of this law requires that both school districts and employees must pay the Medicare tax portion of the FICA payroll tax. The rate and maximum earnings are set by the Federal Government (payments for Medicare and social security must be kept separate).

Effective July 1, 1990 school districts may bargain to make Medicare coverage optional for members of the State Teachers' Retirement System who were hired prior to April 1, 1986. Elections will need to be held.

Medicare Coverage for Employees

An employee hired before April 1, 1986 (and exempt from Medicare coverage under prior law) isn't subject to Medicare coverage if he or she is participating in a qualified retirement system and is performing regular and substantial services for the employer. All workers hired after April 1, 1986 continue to be subject to Medicare, even if they participate in a qualified retirement system.

It is the employer's responsibility to withhold 1.45% for Medicare contributions from taxable wages of its employees. There is no wage base limit on the taxable wages. Employers are required to match employee contributions at the same rate as employees contribute. If the employer fails to withhold or collect Medicare, they are also responsible for the employee's share.

State Form DE-4 Employee Withholding Allowance Certificate

The employee must complete the DE-4 Employee's Withholding Allowance Certificate for state tax withholding if he/she wants the number of allowances for California personal income tax withholding to be different from the number of allowances claimed for federal income tax withholding purposes.

Changing the DE-4: When an employee wants to change any of his/her state withholding data, (to be different from the federal withholding data), he/she must complete a new DE-4 Employee's Withholding Allowance Certificate to supersede the previously filed DE-4.

A person cannot file exempt from state withholding unless they are filing exempt from federal withholding except if they meet the conditions under the Service Member Civil Relief Act.

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If the federal and state withholding data are the same, only the Federal W-4 form needs to be filed by the employee.

State Unemployment Insurance - SUI
The California Unemployment Insurance is an employer paid tax. The tax rate is set through the School Employers Fund. The schools regular unemployment insurance rate applies to all employees except the following:

- Board members
- Elected Officials
- Students who are enrolled and are regularly attending classes at the school district, college or university where they are employed
- Students under 22 years of age enrolled in a non-profit or public educational institution in a program, which combines academic instruction with work experience

The Unemployment Rate is determined in accordance with the rate formula specified by Section 823(b) of the California Unemployment Insurance Code. The rate for all participants of the School Employees Fund is established annually.

State Disability Insurance - SDI
California's disability insurance program is to help protect the labor force against wage loss because of unemployment resulting primarily from a non-occupational illness or injury.

Who is covered?

Most wage earners under the unemployment insurance provisions of the California Unemployment Insurance Code are covered under the disability provisions of the CUIC.

Exceptions are public school employees; employees of state funded institutions of higher education, other governmental entities, and individuals that file religious exemption certificates, both with the Department and their employers, declaring they rely upon prayer in the practice of religion.

Application for SDI Insurance Coverage
Before districts can offer SDI coverage, an application has to be completed and filed with the Employment Development Department for an identification number.

SDI is withheld by bargaining unit in some school districts and as a district benefit option in other school districts.

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Who Pays?
Employees pay for disability insurance and its administration. Some employers may be paying the SDI tax for their employees. For 2017 the SDI tax rate is 1.0 percent of wages up to $114,967.

CALCULATING TAXES

Introduction
Wages become taxable when they are paid not when they are earned. Wages are considered paid when the employee receives the paycheck or when it is constructively received. When the money is made available to the employee (payday) it is then considered constructively received.

Taxable Income
When employees contribute to certain benefits and voluntary deductions with "pretax" dollars, the contribution reduces taxable wages.

PRE-TAX DEDUCTION	FEDERAL WAGE REDUCTIONS	STATE WAGE REDUCTIONS	SOCIAL SECURITY /MEDICARE WAGE REDUCTIONS
CalSTRS	YES	YES	NO
CalPERS	YES	YES	NO
Qualified Alternative Retirement Plan	YES	YES	NO
403 (b) & 457 (b)	YES	YES	NO
Café. Section 125	YES	YES	YES
Ca. Qualified Ride Share	NO	YES	NO

Tax Charts

Calculating the withholding of taxes is done by determining the taxable wages and using the applicable tax charts provided by the IRS (federal taxes) and the Employment Development Department (state taxes). The method most commonly used by school districts in computerized payroll systems is the Percentage Method based on the Annual

WITHOLDING FEDERAL & STATE TAXES

Tax Rate Chart. Some payroll systems may also use the Percentage Method Monthly, Bi-weekly, or Semi-Monthly tax charts.

The following are examples of federal and state withholding calculation procedures:

Supplemental Wage Withholding

A supplemental tax rate can be used instead of the tax charts when employees are paid supplemental wages. For 2018 the federal supplemental tax rate is 22% and the California supplemental tax rate is 6.6% and 10.23% on bonuses.

Examples of supplemental wages include:

- Retroactive wage increases
- Bonuses, prizes, and awards
- Severance or dismissal pay
- Overtime pay
- Reimbursement for nondeductible moving expenses
- Payment for unused, accumulated sick leave or vacation payoff

Where an employee has no income taxes withheld from regular wages, the supplemental withholding rate may not be used. Instead, the supplemental payment must be added to the regular wages and withholding computed under the aggregate method.

One option calls for withholding to be computed at a 25 percent rate in 2017; the other requires aggregation of the supplemental and regular wages, with withholding computed by normal methods. (Using the supplemental wage withholding rate set at 25 percent, is likely to result in more taxes withheld than the aggregate method for most workers. Only the more highly-paid employees in the 28 percent tax bracket and above will benefit from supplemental wage withholding).

EXAMPLE: Monica is entitled to a payment of $100 for a retroactive pay increase. If the $100 is paid in a separate check, the employer may simply withhold $25 for payment of federal income taxes and $6.60 for state taxes.

If the $100 is included with her regular paycheck of $800, and the pay stub specifically notes that the check includes $800 in regular wages and $100 in retroactive wages, withholding includes the normal amount of withholding for an $800 payment (based on Monica's payroll period, marital status, and allowances) plus $25.

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2018 FEDERAL TAX WITHHOLDING—GENERAL CALCULATION PROCEDURES

The following is provided as a general explanation of how tax withholding is calculated for a basic payment situation using the Percentage Method Annual Tax Charts.

Step 1. Determine *gross earnings* for pay period.

Step 2. Determine *salary reductions* for pay period.

Step 3. Subtract salary reductions from gross earnings. This result equals *period taxable earnings*.

Step 4. Multiply period taxable earnings by the calendar number of months (10, 11, or 12) of the job. The result equals federal/state *annual taxable earnings*.

Step 5. Annual taxable earnings less $4,150 times the number of W-4 exemptions claimed = adjusted wages.

Step 6. Refer to the appropriate percentage table

Step 7. Adjusted wages – excess allowed = Excess amount

Step 8. Amount of tax + (Excess amount X Percentage) = total annual withholding

Step 9. Divide total annual withholding by pay calendar months to arrive at taxes withheld for the pay period.

FEDERAL CALCULATION

EXAMPLE:	Monthly Salary:	$6,301.42
	Pay Frequency:	12 months/ Monthly pay
	W-4 Status	Married, 1
	CalSTRS	$504.11
	TSA	$308.00
	Caf/125	$156.70

$6,301.42 (monthly salary) – $504.11 (CalSTRS) – $308.00 (TSA) – $156.70 (caf/ 125) = $5,332.61 (monthly taxable earnings)

$5,332.61 (monthly taxable earnings) x 12 (pay frequency) = $63,991.32 (annual taxable earnings)

$63,991.32 (annual taxable earnings) - $4,150 (one W-4 exemption) = $59,841.32 (adjusted wages)

$59,841.32 (adjusted wages) – $30,600 (excess over from tax chart) = $29,241.32 (excess amount)

$1,905.00 (amount of tax) + ($29,241.32 x 12% = $**3,508.96**) = $5,413.96 (total annual withholding)

$5,413.96 (total annual withholding) ÷ 12 months = $451.16 (pay period taxes).

WITHOLDING FEDERAL & STATE TAXES

Percentage Method—2018 Amount for One Withholding Allowance

Payroll Period	One Withholding Allowance
Weekly	$ 79.80
Biweekly	159.60
Semimonthly	172.90
Monthly	345.80
Quarterly	1,037.50
Semiannually	2,075.00
Annually	4,150.00
Daily or miscellaneous (each day of the payroll period)	16.00

Percentage Method Tables for Income Tax Withholding
(For Wages Paid in 2018)

TABLE 7—ANNUAL Payroll Period

(a) SINGLE person (including head of household)—				(b) MARRIED person—			
If the amount of wages (after subtracting withholding allowances) is:		The amount of income tax to withhold is:		If the amount of wages (after subtracting withholding allowances) is:		The amount of income tax to withhold is:	
Not over $3,700		$0		Not over $11,550		$0	
Over—	But not over—		of excess over—	Over—	But not over—		of excess over—
$3,700	—$13,225	$0.00 plus 10%	—$3,700	$11,550	—$30,600	$0.00 plus 10%	—$11,550
$13,225	—$42,400	$952.50 plus 12%	—$13,225	$30,600	—$88,950	$1,905.00 plus 12%	—$30,600
$42,400	—$86,200	$4,453.50 plus 22%	—$42,400	$88,950	—$176,550	$8,907.00 plus 22%	—$88,950
$86,200	—$161,200	$14,089.50 plus 24%	—$86,200	$176,550	—$326,550	$28,179.00 plus 24%	—$176,550
$161,200	—$203,700	$32,089.50 plus 32%	—$161,200	$326,550	—$411,550	$64,179.00 plus 32%	—$326,550
$203,700	—$503,700	$45,689.50 plus 35%	—$203,700	$411,550	—$611,550	$91,379.00 plus 35%	—$411,550
$503,700		$150,689.50 plus 37%	—$503,700	$611,550		$161,379.00 plus 37%	—$611,550

WITHOLDING FEDERAL & STATE TAXES

CALIFORNIA WITHHOLDING SCHEDULES FOR 2018
METHOD B-EXACT CALCULATION METHOD

This method is based upon applying a given percentage to the wages (after deductions) which fall within a taxable income class, adding to this product the accumulated tax for all lower tax brackets; and then subtracting a tax credit based upon the number of allowances claimed on the Employee's Withholding Allowance Certificate (Form W-4 or DE 4). **This method also takes into consideration the special treatment of additional allowances for estimated deductions.**

The steps in computing the amount of tax to be withheld are as follows:

Step 1 Determine if the employee's gross wages are less than, or equal to, the amount shown in "TABLE 1 - LOW INCOME EXEMPTION TABLE." If so, no income tax is required to be withheld.

Step 2 If the employee claims any additional withholding allowances for estimated deductions on a DE 4, subtract the amount shown in "TABLE 2 - ESTIMATED DEDUCTION TABLE" from the gross wages.

Step 3 Subtract the standard deduction amount shown in "TABLE 3 - STANDARD DEDUCTION TABLE" to arrive at the employee's taxable income.

Step 4 Use "TABLE 5 - TAX RATE TABLE" for the payroll period and marital status to find the applicable line on which the taxable income is located. Perform the indicated calculations to arrive at the computed tax liability.

Step 5 Subtract the tax credit shown in "TABLE 4 - EXEMPTION ALLOWANCE TABLE"* from the computed tax liability to arrive at the amount of tax to be withheld.

*If the employee uses additional allowances claimed for estimated deductions, such allowances **MUST NOT** be used in the determination of tax credits to be subtracted.

EXAMPLE A: Weekly earnings of $210, single, and claiming one withholding allowance on a Form W-4 or DE 4.

Step 1 Earnings for the weekly payroll period are LESS than the amount shown in "TABLE 1 - LOW INCOME EXEMPTION TABLE" ($270); therefore, no income tax is to be withheld.

EXAMPLE B: Biweekly earnings of $1,250, married, and claiming three withholding allowances, one of which is for estimated deductions.

Step 1 Earnings for the biweekly payroll period are GREATER than the amount shown in "TABLE 1 - LOW INCOME EXEMPTION TABLE" ($1,081); therefore, income tax should be withheld.

Step 2	Earnings for biweekly payroll period.	$1,250.00
	Subtract amount from "TABLE 2 - ESTIMATED DEDUCTION TABLE."	-38.00
	Salaries and wages subject to withholding.	$1,212.00
Step 3	Subtract amount from "TABLE 3 - STANDARD DEDUCTION TABLE."	-326.00
	Taxable income.	$886.00
Step 4	Tax computation from "TABLE 5 - TAX RATE TABLE:"	
	Entry covering $886 (over $632 but not over $1,500).	
	• 2.2% amount over $632 (.022 x [$886 – $632]).	$ 5.59
	• Plus the marginal amount.	+6.95
	• Computed tax.	12.54
Step 5	Subtract amount from "TABLE 4 - EXEMPTION ALLOWANCE TABLE."	
	for two regular withholding allowances.	-9.65
	Net amount of tax to be withheld.	$ 2.89

NOTE: Table 5 provides a method comparable to the federal alternative method for percentage calculation of withholding. This method is a minor simplification of the exact calculation method described above in that the tax rate applies to the total taxable income with the excess amount subtracted.

WITHOLDING FEDERAL & STATE TAXES

CALIFORNIA WITHHOLDING SCHEDULES FOR 2018
METHOD B-EXACT CALCULATION METHOD (CONT.)

EXAMPLE C: Monthly earnings of $3,800, married, and claiming five withholding allowances on a Form W-4 or DE 4.

Step 1	Earnings for the monthly payroll period are GREATER than the amount shown in "TABLE 1 - LOW INCOME EXEMPTION TABLE" ($2,341); therefore, income tax should be withheld.	
	Earnings for monthly payroll period.	$3,800.00
Step 2	Not applicable - no estimated deduction allowance claimed.	
Step 3	Subtract amount from "TABLE 3 - STANDARD DEDUCTION TABLE"	-706.00
	Taxable income	$3,094.00
Step 4	Tax computation from "TABLE 5 - TAX RATE TABLE:"	
	• Entry covering $3,094 (over $1,372 but not over $3,248).	
	• 2.2% of amount over $1,372 (.022 x [$3,094 - $1,372]).	$ 37.88
	• Plus marginal tax amount.	+15.09
	• Computed tax.	$ 52.97
Step 5	Subtract amount from "TABLE 4 – EXEMPTION ALLOWANCE TABLE" for 5 regular withholding allowances.	-52.25
	Net amount of tax to be withheld.	$ 0.72

EXAMPLE D: Weekly earnings of $800, unmarried head of household, three withholding allowances on a Form W-4 or DE 4.

Step 1	Earnings for the weekly payroll period are GREATER than the amount shown in "TABLE 1 - LOW INCOME EXEMPTION TABLE" ($540); therefore, income tax should be withheld.	
	Earnings for weekly payroll period.	$ 800.00
Step 2	Not applicable - no estimated deduction allowance claimed.	
Step 3	Subtract amount from "TABLE 3 - STANDARD DEDUCTION TABLE"	-163.00
	Taxable income	$ 637.00
Step 4	Tax computation from "TABLE 5 - TAX RATE TABLE:"	
	• Entry covering $637 (over $316 but not over $750).	
	• 2.2% of amount over $316 (.022 x [$637 - $316]).	$ 7.06
	• Plus marginal tax amount.	+ 3.48
	• Computed tax.	$ 10.54
Step 5	Subtract amount from "TABLE 4 - EXEMPTION ALLOWANCE TABLE" for 3 regular withholding allowances.	- 7.23
	Net amount of tax to be withheld.	$ 3.31

EXAMPLE E: Semi-monthly earnings of $1,800, married, and claiming four allowances on a Form W-4 or DE 4.

Step 1	Earnings for the semi-monthly payroll period are GREATER than the amount shown in "TABLE 1 - LOW INCOME EXEMPTION TABLE" ($1,171); therefore, income tax should be withheld.	
	Annualized wages and salary (24 x $1,800).	$43,200.00
Step 2	Not applicable - no estimated deduction allowance claimed.	
Step 3	Subtract amount from "TABLE 3 - STANDARD DEDUCTION TABLE."	-8,472.00
	Taxable income.	$34,728.00
Step 4	Tax computation from "TABLE 5 - TAX RATE TABLE":	
	• Entry covering $34,728 (over $16,446 but not over $38,990).	
	• 2.2% of amount over $34,728 (.022 x [$34,728 - $16,446]).	$ 402.20
	• Plus marginal tax amount.	+180.91
	• Computed annual tax.	$ 583.11
Step 5	Subtract amount from "TABLE 4 - EXEMPTION ALLOWANCE TABLE" for 4 regular withholding allowances.	-501.60
	Annual amount of tax to be withheld.	$ 81.51
	Divide by number of payroll periods in year (24).	$ 3.40

NOTE: Employers may determine the amount of income tax to be withheld for an annual payroll period and prorate the tax back to the payroll period. This method may be useful to employers who have employees being paid for more than one payroll period and want to conserve computer memory by storing only the annual tax rates, wage brackets, deduction values, and tax credits.

WITHOLDING FEDERAL & STATE TAXES

CALIFORNIA WITHHOLDING SCHEDULES FOR 2018
METHOD B-EXACT CALCULATION METHOD (CONT.)

EXAMPLE F: Annual earnings of $45,000, monthly pay period, married, and claiming four allowances on a Form W-4 or DE 4.

Step 1	Earnings for the annual payroll period are GREATER than the amount shown in "TABLE 1 - LOW INCOME EXEMPTION TABLE" ($28,095); therefore, income tax should be withheld.	
	Annualized wages and/or monthly salary (12 x $3,750).	$45,000.00
Step 2	Not applicable - no estimated deduction allowance claimed.	
Step 3	Subtract amount from "TABLE 3 - STANDARD DEDUCTION TABLE."	-8,472.00
	Taxable income.	$36,528.00
Step 4	Tax computation from "TABLE 5 - TAX RATE TABLE":	
	• Entry covering $36,528 (over $16,446 but not over $38,990)	
	• 2.2% of amount over $16,446 (.022 x [$36,528 - $16,446]).	$ 441.80
	• Plus marginal tax amount.	+180.91
	• Computed annual tax.	$ 622.71
Step 5	Subtract amount from "TABLE 4 - EXEMPTION ALLOWANCE TABLE" for 4 regular withholding allowances.	-501.60
	Annual amount of tax to be withheld.	$ 121.11
	Divide by number of payroll periods in year (12).	$ 10.09

NOTE: Employers may determine the amount of income tax to be withheld for an annual payroll period and figure the tax for the payroll period. This method may be useful to employers who have employees being paid for a lump sum, or a yearly amount not withheld on; and want to conserve computer memory by storing only the annual tax rates, wage brackets, deduction values, and tax credits.

WITHOLDING FEDERAL & STATE TAXES

STATE CALCULATION

EXAMPLE:	Monthly Salary:	$6,301.42
	Pay Frequency:	12 months/ Monthly pay
	W-4 Status	Married, 1
	CalSTRS	$504.11
	TSA	$308.00
	Caf/125	$156.70

$6,301.42 (monthly salary) – $504.11 (CalSTRS) –$308.00 (TSA) – $156.70 (caf/ 125) = $5,332.61 (monthly taxable earnings)

$5,332.61 (monthly taxable earnings) x 12 (pay frequency) = $63,991.32 (annual taxable earnings)

$63,991.32 (annual taxable earnings) - $4,236.00 (one W-4 exemption) = $59,755.32 (adjusted wages)

$59,755.32 (adjusted wages) – $38,990 (excess over from tax chart) = $20,765.32 (excess amount)

$676.88 (amount of tax) + ($20,765.32 x 4.4% = $913.67) = $1,590.55

$1,590.55 – $125.40 (one personal allowance credit) = $1,465.15 (total annual withholding)

$1,465.15(total annual withholding) ÷ 12 months = **$122.10** (pay period taxes).

WITHOLDING FEDERAL & STATE TAXES

CALIFORNIA WITHHOLDING SCHEDULES FOR 2018

METHOD B—EXACT CALCULATION METHOD

TABLE 1 - LOW INCOME EXEMPTION TABLE

PAYROLL PERIOD	SINGLE, DUAL INCOME MARRIED OR MARRIED WITH MULTIPLE EMPLOYERS	MARRIED ALLOWANCES ON DE 4 OR W-4 '0' OR '1'	MARRIED ALLOWANCES ON DE 4 OR W-4 '2' OR MORE	UNMARRIED HEAD OF HOUSEHOLD
WEEKLY	$270	$270	$540	$540
BIWEEKLY	$540	$540	$1,081	$1,081
SEMI-MONTHLY	$585	$585	$1,171	$1,171
MONTHLY	$1,171	$1,171	$2,341	$2,341
QUARTERLY	$3,512	$3,512	$7,024	$7,024
SEMI-ANNUAL	$7,024	$7,024	$14,048	$14,048
ANNUAL	$14,048	$14,048	$28,095	$28,095
DAILY/MISCELLANEOUS	$54	$54	$108	$108

TABLE 2 - ESTIMATED DEDUCTION TABLE

ADDITIONAL WITHHOLDING ALLOWANCES*	PAYROLL PERIOD WEEKLY	BI-WEEKLY	SEMI-MONTHLY	MONTHLY	QUARTERLY	SEMI-ANNUAL	ANNUAL	DAILY/ MISC.
1	$19	$38	$42	$83	$250	$500	$1,000	$4
2	$38	$77	$83	$167	$500	$1,000	$2,000	$8
3	$58	$115	$125	$250	$750	$1,500	$3,000	$12
4	$77	$154	$167	$333	$1,000	$2,000	$4,000	$15
5	$96	$192	$208	$417	$1,250	$2,500	$5,000	$19
6	$115	$231	$250	$500	$1,500	$3,000	$6,000	$23
7	$135	$269	$292	$583	$1,750	$3,500	$7,000	$27
8	$154	$308	$333	$667	$2,000	$4,000	$8,000	$31
9	$173	$346	$375	$750	$2,250	$4,500	$9,000	$35
10**	$192	$385	$417	$833	$2,500	$5,000	$10,000	$38

* Number of Additional Withholding Allowances for Estimated Deductions claimed on Form DE 4 or W-4.

** If the number of Additional Withholding Allowances for Estimated Deductions claimed is greater than 10, multiply the amount shown for one Additional Allowance by the number claimed.

WITHOLDING FEDERAL & STATE TAXES

CALIFORNIA WITHHOLDING SCHEDULES FOR 2018

METHOD B---EXACT CALCULATION METHOD

TABLE 3 - STANDARD DEDUCTION TABLE

PAYROLL PERIOD	SINGLE, DUAL INCOME MARRIED OR MARRIED WITH MULTIPLE EMPLOYERS	MARRIED		UNMARRIED HEAD OF HOUSEHOLD
		ALLOWANCES ON DE 4 OR W-4		
		"0" OR "1"	"2" OR MORE	
WEEKLY	$81	$81	$163	$163
BIWEEKLY	$163	$163	$326	$326
SEMI-MONTHLY	$177	$177	$353	$353
MONTHLY	$353	$353	$706	$706
QUARTERLY	$1,059	$1,059	$2,118	$2,118
SEMI-ANNUAL	$2,118	$2,118	$4,236	$4,236
ANNUAL	$4,236	$4,236	$8,472	$8,472
DAILY/MISCELLANEOUS	$16	$16	$33	$33

TABLE 4 - EXEMPTION ALLOWANCE TABLE

ALLOWANCES ON DE 4 OR W-4	PAYROLL PERIOD							
	WEEKLY	BI-WEEKLY	SEMI-MONTHLY	MONTHLY	QUARTERLY	SEMI-ANNUAL	ANNUAL	DAILY/ MISC.
0	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
1	$2.41	$4.82	$5.23	$10.45	$31.35	$62.70	$125.40	$0.48
2	$4.82	$9.65	$10.45	$20.90	$62.70	$125.40	$250.80	$0.96
3	$7.23	$14.47	$15.68	$31.35	$94.05	$188.10	$376.20	$1.45
4	$9.65	$19.29	$20.90	$41.80	$125.40	$250.80	$501.60	$1.93
5	$12.06	$24.12	$26.13	$52.25	$156.75	$313.50	$627.00	$2.41
6	$14.47	$28.94	$31.35	$62.70	$188.10	$376.20	$752.40	$2.89
7	$16.88	$33.76	$36.58	$73.15	$219.45	$438.90	$877.80	$3.38
8	$19.29	$38.58	$41.80	$83.60	$250.80	$501.60	$1,003.20	$3.86
9	$21.70	$43.41	$47.03	$94.05	$282.15	$564.30	$1,128.60	$4.34
10*	$24.12	$48.23	$52.25	$104.50	$313.50	$627.00	$1,254.00	$4.82

* If the number of allowances claimed exceeds 10, you may determine the amount of tax credit to be allowed by multiplying the amount for one allowance by the total number of allowances.

For example, the amount of tax credit for a married taxpayer with 15 allowances, as determined on Form DE 4 or W-4, on a weekly payroll period would be $36.15.

WITHOLDING FEDERAL & STATE TAXES

CALIFORNIA WITHHOLDING SCHEDULES FOR 2018

METHOD B—EXACT CALCULATION METHOD

TABLE 5 - TAX RATE TABLE

TABLE 5 - TAX R

ANNUAL PAYROLL PERIOD

SINGLE PERSONS, DUAL INCOME MARRIED,
OR MARRIED WITH MULTIPLE EMPLOYERS

IF THE TAXABLE INCOME IS...		THE COMPUTED TAX IS...		
OVER	BUT NOT OVER		OF AMOUNT OVER...	PLUS
$0	$8,223 ...	1.100%	$0	$0.00
$8,223	$19,495 ...	2.200%	$8,223	$90.45
$19,495	$30,769 ...	4.400%	$19,495	$338.43
$30,769	$42,711 ...	6.600%	$30,769	$834.49
$42,711	$53,980 ...	8.800%	$42,711	$1,622.66
$53,980	$275,738 ...	10.230%	$53,980	$2,614.33
$275,738	$330,884 ...	11.330%	$275,738	$25,300.17
$330,884	$551,473 ...	12.430%	$330,884	$31,548.21
$551,473	$1,000,000 ...	13.530%	$551,473	$58,967.42
$1,000,000	and over ...	14.630%	$1,000,000	$119,653.12

MARRIED PERSONS

IF THE TAXABLE INCOME IS...		THE COMPUTED TAX IS...		
OVER	BUT NOT OVER		OF AMOUNT OVER...	PLUS
$0	$16,446 ...	1.100%	$0	$0.00
$16,446	$38,990 ...	2.200%	$16,446	$180.91
$38,990	$61,538 ...	4.400%	$38,990	$676.88
$61,538	$85,422 ...	6.600%	$61,538	$1,668.99
$85,422	$107,960 ...	8.800%	$85,422	$3,245.33
$107,960	$551,476 ...	10.230%	$107,960	$5,228.67
$551,476	$661,768 ...	11.330%	$551,476	$50,600.36
$661,768	$1,000,000 ...	12.430%	$661,768	$63,096.44
$1,000,000	$1,102,946 ...	13.530%	$1,000,000	$105,138.68
$1,102,946	and over ...	14.630%	$1,102,946	$119,067.26

UNMARRIED/HEAD OF HOUSEHOLD

IF THE TAXABLE INCOME IS...		THE COMPUTED TAX IS...		
OVER	BUT NOT OVER		OF AMOUNT OVER...	PLUS
$0	$16,457 ...	1.100%	$0	$0.00
$16,457	$38,991 ...	2.200%	$16,457	$181.03
$38,991	$50,264 ...	4.400%	$38,991	$676.78
$50,264	$62,206 ...	6.600%	$50,264	$1,172.79
$62,206	$73,477 ...	8.800%	$62,206	$1,960.96
$73,477	$375,002 ...	10.230%	$73,477	$2,952.81
$375,002	$450,003 ...	11.330%	$375,002	$33,798.82
$450,003	$750,003 ...	12.430%	$450,003	$42,296.43
$750,003	$1,000,000 ...	13.530%	$750,003	$79,586.43
$1,000,000	and over ...	14.630%	$1,000,000	$113,411.02

WITHOLDING FEDERAL & STATE TAXES

IRS Answers Questions on Public Employer Social Security/Medicare Tax Issues (The following is an excerpt)

In a legal memorandum, Jerry Holmes, branch chief (tax exempt and government entities), has provided answers to 65 questions on employment issues for the public employers' newsletter.

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========== SUMMARY ==========

In a legal memorandum, Jerry Holmes, branch chief (tax exempt and government entities), has provided answers to 65 questions on employment issues for the public employers' newsletter.

In the memorandum, Holmes provides answers to questions involving, among other issues, FICA and Medicare, the continuing employment exemption, the tax treatment of emergency firefighters, section 218 agreements, and exemptions from withholding.

Question: A part-time cafeteria employee has worked for School District A without interruption since 1985. The employee is hired in 2001 by School District A in a second, summer position on a grounds crew. Neither position is covered by a state retirement plan. Do the OASDI and Medicare portions of the FICA Tax apply to these two positions, or is the employee entitled to the continuing employment exception in one or both?

Both portions of the FICA tax apply to both positions. The continuing employment exception to Medicare tax provided in Code section 3121(u)(2)(C) is not available to this employee. It is only available to employees who participate in a public retirement system. Employees who are subject to FICA because they do not participate in a public retirement system must pay both portions of the FICA tax, regardless of when they were hired.

In general the Medicare portion of the FICA tax applies to employees of states and their political subdivisions, unless some exception applies. Section 3121(u)(2)(C) provides

an exception from Medicare tax for continuing employment. To qualify for the exception, the employee must satisfy three conditions: (1) the employee's service would be excluded from the term "employment" for FICA purposes if section 3121(u)(2)(A) did not apply.[1] (2) The employee was hired on or before March 31, 1986, as a bona fide employee, performing regular and substantial services. (3) The employment relationship with that employer has not been terminated after March 31, 1986. Effective for services performed after July 1, 1991, this exception is available only to employees who participate in a public retirement system.

Question: An employee of a school district was covered under the state employees' retirement system. The individual retired in 1999, began receiving a pension and was subsequently rehired by the same school district as a substitute teacher, bus driver, or coach. What taxes should be withheld?

The individual would be subject to Medicare tax, as the continuing employment exception would no longer apply. This would be true in all cases.

The remaining answer to this question depends upon whether the position is covered by an agreement under section 218 of the Social Security Act (section 218 agreement).

An individual in a position covered by a section 218 agreement providing for full coverage is subject to social security tax under the terms of the 218 agreement. The 218 agreement takes precedence over the state-retirement-system rules of section 3121(b)(7)(F), under which the individual might not have to pay social security tax. See section 3121(b)(7)(E), which excludes individuals under a 218 agreement from employment" under section 3121(b)(7).

Thus, if a teacher who was covered under a state retirement system retired and was rehired as a bus driver, a position covered by a 218 agreement, the individual would be subject to social security tax under the terms of the 218 agreement.

Now consider the case of a physical education teacher who retired in 1998 from a full-time teaching position. He was covered by the state retirement system and is now. The teacher is a rehired annuitant, i.e., a former participant in state retirement system who has previously retired and who is either (1) currently receiving retirement benefits or (2) has reached normal retirement age.

The regulations provide that a rehired annuitant is deemed to be a qualified participant in the retirement system without regard to whether he or she continues to accrue a

benefit or whether the distribution of benefits under the retirement system has been suspended pending cessation of services. Section 31.3121(b)(7)-2(d)(4)(ii), Employment Tax Regulations. This rule also applies if the annuitant was rehired by another school district which maintains the same retirement system as the first, for instance a second school district which participates in the same state retirement system under which the teacher is covered.

In other words, contributions do not have to be made to the state retirement system on the retired annuitant's behalf. He is also not subject to the OASDI portion of social security tax. Medicare tax would apply because the employee terminated his employment relationship after April 1, 1986, and no longer qualifies for the continuing employment exception.

Question: A full-time teacher has a second position, working ten hours per week for the employing school district as a bookkeeper. The school district has a 218 agreement covering all employees. Should the district withhold and pay FICA from the teacher's wages as a bookkeeper?

Yes, the wages from the second position are subject to FICA. When a worker is in a position covered by a 218 agreement, the terms of that agreement govern the application of FICA.

Question: Are school board members employees for FICA purposes?

Their compensation is wages subject to FICA tax. A fee-based public official is one who receives compensation in the form of fees directly from the public with whom he does business, for instance, a notary public. Rev. Rul. 74-608, 1974-2 C.B. 275. It does not matter what an official's compensation is called or how often it is paid. If the individual is an employee and receives compensation from a public employer rather than directly from members of the public, his or her compensation is subject to FICA tax. Question: A teacher who is not of retirement age retires from service due to a permanent disability. She was a member of the state teachers' retirement system and begins receiving annuity payments from the system. Later she returns to work for the same school district as a part-time tutor. The school district has no 218 agreement, and the position is not covered by a state retirement plan. Is she subject to OASDI or Medicare taxes?

It is our opinion that the teacher would not be subject to OASDI tax, as she would be regarded as a rehired annuitant. She was a qualified participant in the retirement system, and she is "in pay status" *i.e.*, currently receiving retirement benefits. Consequently, she is deemed to be a qualified participant in the retirement system without regard to whether she continues to accrue a benefit. Section 31.3121(b)(7)2(d)(4)(ii), Employment Tax Regulations. The teacher's remuneration as a part-time tutor would be subject to the Medicare tax if she was rehired after April 1, 1986.

Statement Concerning Your Employment in a Job Not Covered by Social Security

Employee Name _____ **Employee ID#** _____

Employer Name _____ **Employer ID#** _____

Your earnings from this job are not covered under Social Security. When you retire, or if you become disabled, you may receive a pension based on earnings from this job. If you do, and you are also entitled to a benefit from Social Security based on either your own work or the work of your husband or wife, or former husband or wife, your pension may affect the amount of the Social Security benefit you receive. Your Medicare benefits, however, will not be affected. Under the Social Security law, there are two ways your Social Security benefit amount may be affected.

Windfall Elimination Provision

Under the Windfall Elimination Provision, your Social Security retirement or disability benefit is figured using a modified formula when you are also entitled to a pension from a job where you did not pay Social Security tax. As a result, you will receive a lower Social Security benefit than if you were not entitled to a pension from this job. For example, if you are age 62 in 2013, the maximum monthly reduction in your Social Security benefit as a result of this provision is $395.50. This amount is updated annually. This provision reduces, but does not totally eliminate, your Social Security benefit. For additional information, please refer to Social Security Publication, “Windfall Elimination Provision.”

Government Pension Offset Provision

Under the Government Pension Offset Provision, any Social Security spouse or widow(er) benefit to which you become entitled will be offset if you also receive a Federal, State or local government pension based on work where you did not pay Social Security tax. The offset reduces the amount of your Social Security spouse or widow(er) benefit by two-thirds of the amount of your pension.

For example, if you get a monthly pension of $600 based on earnings that are not covered under Social Security, two-thirds of that amount, $400, is used to offset your Social Security spouse or widow(er) benefit. If you are eligible for a $500 widow(er) benefit, you will receive $100 per month from Social Security ($500 - $400=$100). Even if your pension is high enough to totally offset your spouse or widow(er) Social Security benefit, you are still eligible for Medicare at age 65. For additional information, please refer to Social Security Publication, “Government Pension Offset.”

For More Information

Social Security publications and additional information, including information about exceptions to each provision, are available at www.socialsecurity.gov. You may also call toll free 1-800-772-1213, or for the deaf or hard of hearing call the TTY number 1-800-325-0778, or contact your local Social Security office.

I certify that I have received Form SSA-1945 that contains information about the possible effects of the Windfall Elimination Provision and the Government Pension Offset Provision on my potential future Social Security Benefits.

Signature of Employee _____ **Date** _____

Information about Social Security Form SSA-1945 Statement Concerning Your Employment in a Job Not Covered by Social Security

New legislation [Section 419(c) of Public Law 108-203, the Social Security Protection Act of 2004] requires State and local government employers to provide a statement to employees hired January 1, 2005 or later in a job not covered under Social Security. The statement explains how a pension from that job could affect future Social Security benefits to which they may become entitled.

Form SSA-1945, **Statement Concerning Your Employment in a Job Not Covered by Social Security,** is the document that employers should use to meet the requirements of the law. The SSA-1945 explains the potential effects of two provisions in the Social Security law for workers who also receive a pension based on their work in a job not covered by Social Security. The Windfall Elimination Provision can affect the amount of a worker's Social Security retirement or disability benefit. The Government Pension Offset Provision can affect a Social Security benefit received as a spouse, surviving spouse, or an ex-spouse.

Employers must:

- Give the statement to the employee prior to the start of employment;
- Get the employee's signature on the form; and
- Submit a copy of the signed form to the pension paying agency.

Social Security will not be setting any additional guidelines for the use of this form.

Copies of the SSA-1945 are available online at the Social Security website, www.socialsecurity.gov/online/ssa-1945.pdf. Paper copies can be requested by email at ofsm.oswm.rqct.orders@ssa.gov or by fax at 410-965-2037. The request must include the name, complete address and telephone number of the employer. Forms will not be sent to a post office box. Also, if appropriate, include the name of the person to whom the forms are to be delivered. The forms are available in packages of 25. Please refer to Inventory Control Number (ICN) 276950 when ordering.

Employment Development Department
State of California

This form can be used to manually compute your withholding allowances, or you can electronically compute them at **www.taxes.ca.gov/de4.pdf**.

EMPLOYEE'S WITHHOLDING ALLOWANCE CERTIFICATE

Type or Print Your Full Name	Your Social Security Number
Home Address (Number and Street or Rural Route)	Filing Status Withholding Allowances ☐ SINGLE or MARRIED (with two or more incomes) ☐ MARRIED (one income) ☐ HEAD OF HOUSEHOLD
City, State, and ZIP Code	

1. Number of allowances for Regular Withholding Allowances, Worksheet A _____
   Number of allowances from the Estimated Deductions, Worksheet B _____
   Total Number of Allowances (A + B) when using the California Withholding Schedules for 2018 _____
   OR
2. Additional amount of state income tax to be withheld each pay period (if employer agrees), Worksheet C _____
   OR
3. I certify under penalty of perjury that I am not subject to California withholding. I meet the conditions set forth under the Service Member Civil Relief Act, as amended by the Military Spouses Residency Relief Act. (Check box here) ☐

Under the penalties of perjury, I certify that the number of withholding allowances claimed on this certificate does not exceed the number to which I am entitled or, if claiming exemption from withholding, that I am entitled to claim the exempt status.

Signature _____ Date _____

Employer's Name and Address	California Employer Payroll Tax Account Number

cut here

Give the top portion of this page to your employer and keep the remainder for your records.

YOUR CALIFORNIA PERSONAL INCOME **TAX MAY BE UNDERWITHHELD** IF YOU DO NOT FILE THIS DE 4 FORM.

IF YOU RELY ON THE FEDERAL FORM W-4 FOR YOUR CALIFORNIA WITHHOLDING ALLOWANCES, YOUR CALIFORNIA STATE PERSONAL INCOME TAX MAY BE UNDERWITHHELD AND YOU MAY OWE MONEY AT THE END OF THE YEAR.

PURPOSE: This certificate, DE 4, is for **California Personal Income Tax (PIT) withholding** purposes only. The DE 4 is used to compute the amount of taxes to be withheld from your wages, by your employer, to accurately reflect your state tax withholding obligation.

You should complete this form if either:

(1) You claim a different marital status, number of regular allowances, or different additional dollar amount to be withheld for California PIT withholding than you claim for federal income tax withholding or,

(2) You claim additional allowances for estimated deductions.

THIS FORM WILL NOT CHANGE YOUR FEDERAL WITHHOLDING ALLOWANCES.

The federal Form W-4 is applicable for California withholding purposes if you wish to claim the same marital status, number of regular allowances, and/or the same additional dollar amount to be withheld for state and federal purposes. However, federal tax brackets and withholding methods do not reflect state PIT withholding tables. **If you rely on the number of withholding allowances you claim on your Form W-4 withholding allowance certificate for your state income tax withholding, you may be significantly underwithheld.** This is particularly true if your household income is derived from more than one source.

CHECK YOUR WITHHOLDING: After your Form W-4 and/or DE 4 takes effect, compare the state income tax withheld with your estimated total annual tax. For state withholding, use the worksheets on this form.

EXEMPTION FROM WITHHOLDING: If you wish to claim exempt, complete the federal Form W-4. You may claim exempt from withholding California income tax if you did not owe any federal income tax last year and you do not expect to owe any federal income tax this year. The exemption is good for one year. If you continue to qualify for the exempt filing status, a new Form W-4 designating EXEMPT must be submitted by February 15 each year to continue your exemption. If you are not having federal income tax withheld this year but expect to have a tax liability next year, you are required to give your employer a new Form W-4 by December 1.

EXEMPTION FROM WITHHOLDING (continued): Under the Service Member Civil Relief Act, as amended by the Military Spouses Residency Relief Act, you may be exempt from California income tax on your wages if (i) your spouse is a member of the armed forces present in California in compliance with military orders; (ii) you are present in California solely to be with your spouse; and (iii) you maintain your domicile in another state. If you claim exemption under this act, check the box on Line 3. You may be required to provide proof of exemption upon request.

IF YOU NEED MORE DETAILED INFORMATION, SEE THE INSTRUCTIONS THAT CAME WITH YOUR LAST CALIFORNIA RESIDENT INCOME TAX RETURN OR CALL THE FRANCHISE TAX BOARD (FTB).

IF YOU ARE CALLING FROM WITHIN THE UNITED STATES	1-800-852-5711 (voice) 1-800-822-6268 (TTY)
IF YOU ARE CALLING FROM OUTSIDE THE UNITED STATES (Not Toll Free)	1-916-845-6500

The *California Employer's Guide,* DE 44, provides the income tax withholding tables. This publication may be found on the Employment Development Department (EDD) website at **www.edd.ca.gov/Payroll_Taxes/Forms_and_Publications.htm**. To assist you in calculating your tax liability, please visit the FTB website at **www.ftb.ca.gov/individuals/index.shtml**.

NOTIFICATION: If the IRS instructs your employer to withhold federal income tax based on a certain withholding status, your employer is required to use the same withholding status for state income tax withholding.

The burden of proof rests with the employee to show the correct California Income Tax Withholding. Pursuant to Section 4340-1(e) of Title 22, California Code of Regulations (CCR), the FTB or the EDD may, by special direction in writing, require an employer to submit a Form W-4 or DE 4 when such forms are necessary for the administration of the withholding tax programs.

PENALTY: You may be fined $500 if you file, with no reasonable basis, a DE 4 that results in less tax being withheld than is properly allowable. In addition, criminal penalties apply for willfully supplying false or fraudulent information or failing to supply information requiring an increase in withholding. This is provided by Section 13101 of the California Unemployment Insurance Code and Section 19176 of the Revenue and Taxation Code.

INSTRUCTIONS — 1 — ALLOWANCES*

When determining your withholding allowances, you must consider your personal situation:
— Do you claim allowances for dependents or blindness?
— Will you itemize your deductions?
— Do you have more than one income coming into the household?

TWO-EARNERS/MULTIPLE INCOMES: When earnings are derived from more than one source, underwithholding may occur. If you have a working spouse or more than one job, it is best to check the box "SINGLE or MARRIED (with two or more incomes)." Figure the total number of allowances you are entitled to claim on all jobs using only one DE 4 form. Claim allowances with **one** employer. Do **not** claim the same allowances with more than one employer. Your withholding will usually be most accurate when all allowances are claimed on the DE 4 or Form W-4 filed for the highest paying job and zero allowances are claimed for the others.

MARRIED BUT NOT LIVING WITH YOUR SPOUSE: You may check the "Head of Household" marital status box if you meet all of the following tests:
(1) Your spouse will not live with you **at any time** during the year;
(2) You will furnish over half of the cost of maintaining a home for the entire year for yourself and your child or stepchild who qualifies as your dependent; **and**
(3) You will file a separate return for the year.

HEAD OF HOUSEHOLD: To qualify, you must be unmarried or legally separated from your spouse and pay more than 50% of the costs of maintaining a home for the **entire** year for yourself and your dependent(s) or other qualifying individuals. Cost of maintaining the home includes such items as rent, property insurance, property taxes, mortgage interest, repairs, utilities, and cost of food. It does not include the individual's personal expenses or any amount which represents value of services performed by a member of the household of the taxpayer.

WORKSHEET A — REGULAR WITHHOLDING ALLOWANCES

(A)	Allowance for yourself — enter 1	(A) _____
(B)	Allowance for your spouse (if not separately claimed by your spouse) — enter 1	(B) _____
(C)	Allowance for blindness — yourself — enter 1	(C) _____
(D)	Allowance for blindness — your spouse (if not separately claimed by your spouse) — enter 1	(D) _____
(E)	Allowance(s) for dependent(s) — do not include yourself or your spouse	(E) _____
(F)	Total — add lines (A) through (E) above	(F) _____

INSTRUCTIONS — 2 — ADDITIONAL WITHHOLDING ALLOWANCES

If you expect to itemize deductions on your California income tax return, you can claim additional withholding allowances. Use Worksheet B to determine whether your expected estimated deductions may entitle you to claim one or more additional withholding allowances. Use last year's FTB Form 540 as a model to calculate this year's withholding amounts.

Do not include deferred compensation, qualified pension payments, or flexible benefits, etc., that are deducted from your gross pay but are not taxed on this worksheet.

You may reduce the amount of tax withheld from your wages by claiming one additional withholding allowance for each $1,000, or fraction of $1,000, by which you expect your estimated deductions for the year to exceed your allowable standard deduction.

WORKSHEET B — ESTIMATED DEDUCTIONS

1.	Enter an estimate of your itemized deductions for California taxes for this tax year as listed in the schedules in the FTB Form 540		1. _____
2.	Enter $8,472 if married filing joint with two or more allowances, unmarried head of household, or qualifying widow(er) with dependent(s) or $4,236 if single or married filing separately, dual income married, or married with multiple employers	–	2. _____
3.	Subtract line 2 from line 1, enter difference	=	3. _____
4.	Enter an estimate of your adjustments to income (alimony payments, IRA deposits)	+	4. _____
5.	Add line 4 to line 3, enter sum	=	5. _____
6.	Enter an estimate of your nonwage income (dividends, interest income, alimony receipts)	–	6. _____
7.	If line 5 is greater than line 6 (if less, see below); Subtract line 6 from line 5, enter difference	=	7. _____
8.	Divide the amount on line 7 by $1,000, round any fraction to the nearest whole number Enter this number on line 1 of the DE 4. Complete Worksheet C, if needed.		8. _____
9.	If line 6 is greater than line 5; Enter amount from line 6 (nonwage income)		9. _____
10.	Enter amount from line 5 (deductions)		10. _____
11.	Subtract line 10 from line 9, enter difference **Complete Worksheet C**		11. _____

*Wages paid to registered domestic partners will be treated the same for state income tax purposes as wages paid to spouses for California PIT withholding and PIT wages. This law does not impact federal income tax law. A registered domestic partner means an individual partner in a domestic partner relationship within the meaning of Section 297 of the Family Code. For more information, please call our Taxpayer Assistance Center at 1-888-745-3886.

WORKSHEET C **TAX WITHHOLDING AND ESTIMATED TAX**

1. Enter estimate of total wages for tax year 2018 . . . . . 1. _____
2. Enter estimate of nonwage income (line 6 of Worksheet B) . . . . . 2. _____
3. Add line 1 and line 2. Enter sum . . . . . 3. _____
4. Enter itemized deductions or standard deduction (line 1 or 2 of Worksheet B, whichever is largest) . . . . . 4. _____
5. Enter adjustments to income (line 4 of Worksheet B) . . . . . 5. _____
6. Add line 4 and line 5. Enter sum . . . . . 6. _____
7. Subtract line 6 from line 3. Enter difference . . . . . 7. _____
8. Figure your tax liability for the amount on line 7 by using the 2018 tax rate schedules below . . . . . 8. _____
9. Enter personal exemptions (line F of Worksheet A x $125.40) . . . . . 9. _____
10. Subtract line 9 from line 8. Enter difference . . . . . 10. _____
11. Enter any tax credits. (See FTB Form 540) . . . . . 11. _____
12. Subtract line 11 from line 10. Enter difference. This is your total tax liability . . . . . 12. _____
13. Calculate the tax withheld and estimated to be withheld during 2018. Contact your employer to request the amount that will be withheld on your wages based on the marital status and number of withholding allowances you will claim for 2018. Multiply the estimated amount to be withheld by the number of pay periods left in the year. Add the total to the amount already withheld for 2018 . . . . . 13. _____
14. Subtract line 13 from line 12. Enter difference. If this is less than zero, you do not need to have additional taxes withheld . . . . . 14. _____
15. Divide line 14 by the number of pay periods remaining in the year. Enter this figure on line 2 of the DE 4 . . . 15. _____

NOTE: Your employer is not required to withhold the additional amount requested on line 2 of your DE 4. If your employer does not agree to withhold the additional amount, you may increase your withholdings as much as possible by using the "single" status with "zero" allowances. If the amount withheld still results in an underpayment of state income taxes, you may need to file quarterly estimates on Form 540-ES with the FTB to avoid a penalty.

THESE TABLES ARE FOR CALCULATING WORKSHEET C AND FOR 2018 ONLY

SINGLE PERSONS, DUAL INCOME MARRIED WITH MULTIPLE EMPLOYERS

IF THE TAXABLE INCOME IS		COMPUTED TAX IS		
OVER	BUT NOT OVER	OF AMOUNT OVER . . .		PLUS
$0	$8,223 ...	1.100%	$0	$0.00
$8,223	$19,495 ...	2.200%	$8,223	$90.45
$19,495	$30,769 ...	4.400%	$19,495	$338.43
$30,769	$42,711 ...	6.600%	$30,769	$834.49
$42,711	$53,980 ...	8.800%	$42,711	$1,622.66
$53,980	$275,738 ...	10.230%	$53,980	$2,614.33
$275,738	$330,884 ...	11.330%	$275,738	$25,300.17
$330,884	$551,473 ...	12.430%	$330,884	$31,548.21
$551,473	$1,000,000 ...	13.530%	$551,473	$58,967.42
$1,000,000	and over...	14.630%	$1,000,000	$119,653.12

MARRIED FILING JOINT OR QUALIFYING WIDOW(ER) TAXPAYERS

IF THE TAXABLE INCOME IS		COMPUTED TAX IS		
OVER	BUT NOT OVER	OF AMOUNT OVER . . .		PLUS
$0	$16,446 ...	1.100%	$0	$0.00
$16,446	$38,990 ...	2.200%	$16,446	$180.91
$38,990	$61,538 ...	4.400%	$38,990	$676.88
$61,538	$85,422 ...	6.600%	$61,538	$1,668.99
$85,422	$107,960 ...	8.800%	$85,422	$3,245.33
$107,960	$551,476 ...	10.230%	$107,960	$5,228.67
$551,476	$661,768 ...	11.330%	$551,476	$50,600.36
$661,768	$1,000,000 ...	12.430%	$661,768	$63,096.44
$1,000,000	$1,102,946 ...	13.530%	$1,000,000	$105,138.68
$1,102,946	and over	14.630%	$1,102,946	$119,067.26

UNMARRIED HEAD OF HOUSEHOLD

IF THE TAXABLE INCOME IS		COMPUTED TAX IS		
OVER	BUT NOT OVER	OF AMOUNT OVER . . .		PLUS
$0	$16,457 ...	1.100%	$0	$0.00
$16,457	$38,991 ...	2.200%	$16,457	$181.03
$38,991	$50,264 ...	4.400%	$38,991	$676.78
$50,264	$62,206 ...	6.600%	$50,264	$1,172.79
$62,206	$73,477 ...	8.800%	$62,206	$1,960.96
$73,477	$375,002 ...	10.230%	$73,477	$2,952.81
$375,002	$450,003 ...	11.330%	$375,002	$33,798.82
$450,003	$750,003 ...	12.430%	$450,003	$42,296.43
$750,003	$1,000,000 ...	13.530%	$750,003	$79,586.43
$1,000,000	and over	14.630%	$1,000,000	$113,411.02

IF YOU NEED MORE DETAILED INFORMATION, SEE THE INSTRUCTIONS THAT CAME WITH YOUR LAST CALIFORNIA RESIDENT INCOME TAX RETURN OR CALL THE FTB:

IF YOU ARE CALLING FROM WITHIN THE UNITED STATES 1-800-852-5711 (voice)
1-800-822-6268 (TTY)

IF YOU ARE CALLING FROM OUTSIDE THE UNITED STATES
(Not Toll Free) 1-916-845-6500

The DE 4 information is collected for purposes of administering the PIT law and under the authority of Title 22, CCR, Section 4340-1, and the California Revenue and Taxation Code, including Section 18624. The Information Practices Act of 1977 requires that individuals be notified of how information they provide may be used. Further information is contained in the instructions that came with your last California resident income tax return.

Section 6: Paying Employees

Section 6
PAYING EMPLOYEES

PAYING EMPLOYEES

OVERVIEW

Individual states control how and when employees are paid. It is the employer's choice of the methods of payments they provide for the employee. However, once a method has been made available, the state's regulations regarding those methods must be followed. California allows employees to be paid by cash, check, direct deposit, or payroll cards.

Direct Deposit allows employees to have their paychecks electronically deposited into their bank account. California Labor and Employee Regulation Code Section 213 allow California employers to provide direct deposit, **provided the employee has voluntarily authorized such deposit.** Employers in California cannot mandate direct deposit to their employees.

California also has specific laws under Labor Code Section 226 in regards to paycheck information that must be provided to employees. Legislation passed in 2004 provided that California school districts and community colleges must also adhere to Labor Code Section 226 beginning on January 1, 2007.

The California Education Code sets when payments to school district and community college employees must be completed. Different Education Codes apply to Classified and Certificated Payments. In addition, the Education Code also provides for alternative payment procedures including procedures to be set by unified school districts with ADA of 100,000 or more and county departments of education.

Effective January 1, 2000, payments to K-12 certificated employees under Education Codes 45048 and 45049 are subject to interest penalties when proper payment timelines are not met. Districts should contact their respective county offices for guidance on this legislative change.

PAYING EMPLOYEES

DIRECT DEPOSIT

Direct Deposit allows employees to have their paychecks electronically deposited into their bank account. There are four primary participants in the Electronic Fund Transfer (EFT) process.

- Employees authorize electronic payments to be credited to their bank accounts on payday.

- Employers originate the electronic payment entries for the payment system. This is done by creating a magnetic tape, electronic transmission, or PC generated program. If the employer can't prepare transactions in computer readable format, they can be prepared by an outside source. The financial institution that initiates the ACH entries is known as the Originating Depository Financial Institution (ODFI).

- Automated Clearing House (ACH) is the central clearing facility that distributes the entries to the receiving financial institutions. It also performs the required settlement functions.

- Receiving depository financial institutions (RDFI) receive the individual transactions and post the funds to the accounts of depositors (employees).

Authorizations
A direct deposit authorization is an agreement to allow the electronic transfer of funds to an employee's bank account. Employee authorization does not have to be in writing but is recommended to provide recovering funds in the event of overpayments.

The authorization form should provide the following information:

- The employee's bank routing number
- The type of account (checking/share draft/ or savings)
- The account number

The most accurate way to receive the above information is to have the employee attach a cancelled check to the authorization form. Savings account slips are not recommended as they may not provide accurate information for direct deposit purposes. Routing numbers should only contain nine digits. If the first digit is a "2" or "3" the financial institution is a credit union or savings and loan.

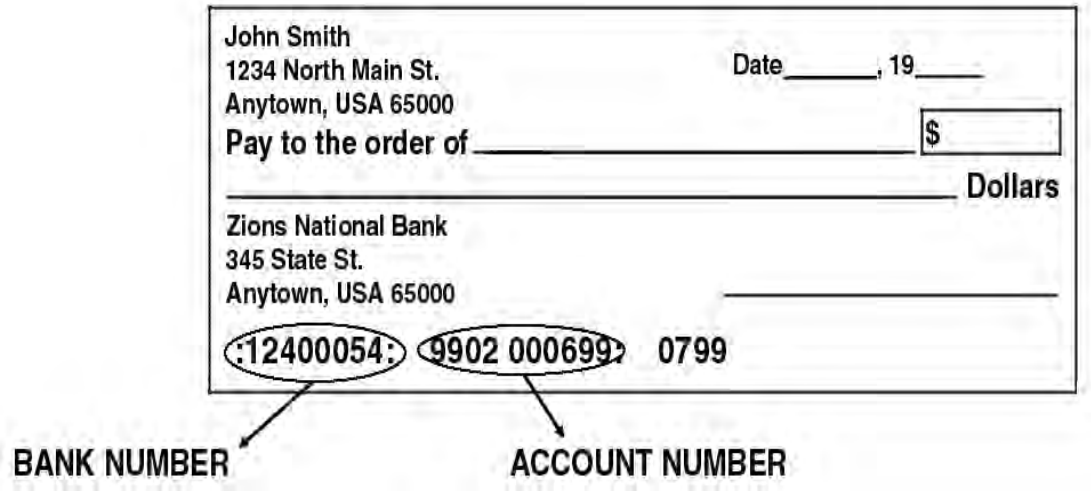
The authorization form should also include information about termination procedures and effective dates for implementing the direct deposit. Also include language that indicates the employee understands procedures for recovering errors or overpayments into their account.

PAYING EMPLOYEES

Pre-Notification Process
Employers have the option to "pre-note" or test the information provided for direct deposit. Pre-notification is no longer required by the Automated Clearing House but is highly recommended to ensure the employee's money is properly credited to the correct account.

The Direct Deposit Authorization Agreement form (Attachment II) can be used to prepare a pre-notification test for routing account information with zero dollars to the employee's bank through ACH (Automated Clearing House) to confirm the validity of the account. The pre-notification test file can be combined on the same file as direct deposits that are currently active or a separate file can be submitted.
The pre-notification process is executed as follows:

- The employer receives an authorization form along with a cancelled check from the employee.
- The employer uses the employee's account number and the bank's transit routing number from the cancelled check for data entry.
- The employer prepares a pre-notification record as a test with zero dollars and cents. This is transmitted to the ACH for routing to the employee's bank to confirm the validity of the account. The employer may have the option of including the pre-notification data on the same file as direct deposits currently depositing dollars to employee accounts.
- If the pre-notification is not returned to the employer within 6 banking days, the first live payroll entry can be processed for deposit.
- If the pre-notification entry is returned through the ODFI within 6 days, the testing process must begin again. This may require the employee to complete a new pre-notification form with valid information.



PAYING EMPLOYEES

Returned Items
Direct deposits may be returned through the ACH process when there are invalid accounts or routing numbers or an employee's account is closed. Bank mergers may also cause a return item to be generated. A Return Resolution Report should accompany the returned item which gives an explanation for the return.

Direct Deposit Corrections
If a mistake is made, employers can generate a "single entry reversal" through ACH within five banking days from the settlement date of the original direct deposit.

Handling Late Deposits
If an employee contacts the payroll department that their funds are not in their account on payday the following steps should be followed:

- Assure the employee that their money is safe and the issue will be resolved.
- Ask the employee if they are basing not seeing their deposit on information obtained from the ATM machine. Direct deposits may not have yet been posted for ATM purposes by the employee's financial institution. Ask the employee to contact their banking representative to see if their deposit has been credited to their account.
- If the employee's financial institution did not receive the deposit verify the account number with the employee.
- Check the RDFI's routing number and inquire into any possible mergers that may have occurred.
- If a solution still has not been found, contact the ODFI financial institution and speak to your contact representative.

PAYING EMPLOYEES

PAY STATEMENTS

California Labor Code Section 226

226. (a) Every employer shall, semimonthly or at the time of each payment of wages, furnish each of his or her employees, either as a detachable part of the check, draft, or voucher paying the employee's wages, or separately when wages are paid by personal check or cash, an accurate itemized statement in writing showing (1) gross wages earned, (2) total hours worked by the employee, except for any employee whose compensation is solely based on a salary and who is exempt from payment of overtime under subdivision (a) of Section 515 or any applicable order of the Industrial Welfare Commission, (3) the number of piece-rate units earned and any applicable piece rate if the employee is paid on a piece-rate basis, (4) all deductions, provided that all deductions made on written orders of the employee may be aggregated and shown as one item, (5) net wages earned, (6) the inclusive dates of the period for which the employee is paid, (7) the name of the employee and his or her social security number, except that by January 1, 2008, only the last four digits of his or her social security number or an employee identification number other than a social security number may be shown on the itemized statement, (8) the name and address of the legal entity that is the employer, and (9) all applicable hourly rates in effect during the pay period and the corresponding number of hours worked at each hourly rate by the employee. The deductions made from payments of wages shall be recorded in ink or other indelible form, properly dated, showing the month, day, and year, and a copy of the statement or a record of the deductions shall be kept on file by the employer for at least three years at the place of employment or at a central location within the State of California.

(b) An employer that is required by this **code** or any regulation adopted pursuant to this **code** to keep the information required by subdivision (a) shall afford current and former employees the right to inspect or copy the records pertaining to that current or former employee, upon reasonable request to the employer. The employer may take reasonable steps to assure the identity of a current or former employee. If the employer provides copies of the records, the actual cost of reproduction may be charged to the current or former employee.

(c) An employer who receives a written or oral request to inspect or copy records pursuant to subdivision (b) pertaining to a current or former employee shall comply with the request as soon as practicable, but no later than 21 calendar days from the date of the request. A violation of this subdivision is an infraction.

Impossibility of performance, not caused by or a result of a violation of law shall be an affirmative defense for an employer in any action alleging a violation of this subdivision. An employer may designate the person to whom a request under this subdivision will be made.

(d) This section does not apply to any employer of any person employed by the owner or occupant of a residential dwelling whose duties are incidental to the ownership, maintenance, or use of the dwelling, including the care and supervision of children, or whose duties are personal and not in the course of the trade, business, profession, or occupation of the owner or occupant.

(e) An employee suffering injury as a result of a knowing and intentional failure by an employer to comply with subdivision (a) is entitled to recover the greater of all actual damages or fifty dollars ($50) for the initial pay period in which a violation occurs and one hundred dollars ($100) per employee for each violation in a subsequent pay period, not exceeding an aggregate penalty of four thousand dollars ($4,000), and is entitled to an award of costs and reasonable attorney's fees.

(f) A failure by an employer to permit a current or former employee to inspect or copy records within the time set forth in subdivision (c) entitles the current or former employee or the **Labor** Commissioner to recover a seven-hundred-fifty-dollar ($750) penalty from the employer.

(g) An employee may also bring an action for injunctive relief to ensure compliance with this section, and is entitled to an award of costs and reasonable attorney's fees.

(h) **This section does not apply to the state, to any city, county, city and county, district, or to any other governmental entity, except that if the state or a city, county, city and county, district, or other governmental entity furnishes its employees with a check, draft, or voucher paying the employee's wages, the state or a city, county, city and county, district, or other governmental entity shall, by January 1, 2008, use no more than the last four digits of the employee's social security number or shall use an employee identification number other than the social security number on the itemized statement provided with the check, draft, or voucher.**

226.**3**. Any employer who violates subdivision (a) of Section **226** shall be subject to a civil penalty in the amount of two hundred fifty dollars ($250) per employee per violation in an initial citation and one thousand dollars ($1,000) per employee for each violation in a subsequent citation, for which the employer fails to provide the employee a wage deduction statement or fails to keep the records required in subdivision (a) of Section **226**. The civil penalties provided for in this section are in addition to any other penalty provided by law. In enforcing this section, the **Labor** Commissioner shall take into consideration whether the violation was inadvertent, and in his or her discretion, may decide not to penalize an employer for a first violation when that violation was due to a clerical error or inadvertent mistake.

PAYING EMPLOYEES

TIME OF PAYMENTS

Classified Time of Payment of Compensation
Education Code 45166
45166. Orders for the payment of wages and payroll orders and warrants for the payment of wages of employees a part of the classified service in any public school system shall be drawn at least once during each calendar month, for those districts not using the provisions of Sections 42644, 42645, or 42646 of this code. Such payment shall be made on the last working day of the month in which the employee was in paid status.

This section shall not prohibit a school district from making a payment of earned salary prior to the last working day of the pay period or of the month.

This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

Classified Time of Payment of Wages of Full Time Non-Certificated Employees
Education Code 42644
42644. Orders for the payment of wages and payroll orders for the payment of wages of employees employed full time in positions not requiring certification qualifications shall be drawn twice during each calendar month on days designated in advance by the governing board of each school district to which this section is made applicable. Labor performed between the 1st and 15th days, inclusive, of any calendar month shall be paid for between the 16th and 26th day of the month during which the labor was performed, and labor performed between the 16th and the last day inclusive, of any calendar month, shall be paid for between the 1st and 10th day of the following month.

The governing board of each school district which has an average daily attendance of 5,000 or more, and the governing board of each school district with an average daily attendance of less than 5,000 in a county with a population in excess of 4,000,000 persons as determined by the 1960 federal census, shall make the provisions of this section applicable to the board, whenever a majority of the employees of the district employed full time in positions not requiring certification qualifications petition the board in writing to do so.

The governing board of a school district which has an average daily attendance of less than 5,000, other than such a school district situated in a county with a population in excess of 4,000,000 persons as determined by the 1960 federal census, may, on the petition in writing of a majority of the employees of the district employed full time in positions not requiring certification qualifications, make the provisions of this section applicable to the board.

PAYING EMPLOYEES

Certificated Time of Payment
Education Code 45048

45048. (a) Each salary payment for any calendar month may be made on the last working day of the month and shall be paid not earlier than the last working day of the month and not later than the fifth day of the succeeding calendar month except that teachers employed for less than full time in classes for adults, in a day or evening high school, or in a special day or evening class maintained in connection with an elementary school shall be paid on or before the 10th day of the succeeding calendar month for services performed during the preceding calendar month.

(b) If the school district provides for the payment of the salary of employees employed in positions requiring certification qualifications once each two weeks, twice a month, or once each four weeks, pursuant to Section 45038, each salary payment may be made on the last working day of the regular payroll period and shall be made no earlier than the last working day of the regular payroll period and not later than the eighth working day of the following regular payroll period.

(c) If a salary payment is not made timely as required by this section, the amount of the salary payment due shall be increased by an amount of interest on the unpaid amount for each day of delay.

(d) A certificated employee of a school district who qualifies for a salary increase shall be paid the increased salary not later than three regular pay periods or three months, whichever is longer, after the employee files proper documentation where required for the salary increase. The district shall additionally pay the employee daily interest on the amount owed to the employee calculated from the date that the employee was entitled to the salary increase if the school district does not pay the employee his or her salary increase within three regular pay periods or three months, whichever period is longer, after the employee files proper documentation where required for the salary increase. All amounts due the employee resulting from the salary increase and not paid to the employee at the time that the employee actually receives the salary increase shall be paid to the employee within 20 business days of the date that the employee actually received the salary increase. The district shall additionally pay the employee daily interest on the amount owed to the employee calculated from the date that the employee was entitled to the salary increase if the district does not pay the employee all amounts due the employee resulting from the salary increase within 20 business days following the date that the employee actually received the salary increase.

(e) The amount of interest required by subdivisions (c) and (d) shall be determined by the method established in Section 19521 of the Revenue and Taxation Code.

(f) This section shall not prohibit a school district from making a payment of earned salary before the last working day of the month or regular payroll period.

PAYING EMPLOYEES

Certificated Time of Payment for Additional Activities
Education Code 45049

45049. (a) When any school district employs a certificated employee to perform teaching or other services in addition to his or her regular teaching duties, or when a school district employs a certificated employee to perform teaching or other services at a summer school maintained by the district, the district shall pay the employee for the services either in one lump sum or at an hourly, daily, biweekly, quadric-weekly, or monthly rate of pay. If the pay is in one lump sum, the district shall pay the employee within 10 days after the termination of the services. If the pay is at an hourly, daily, biweekly, quadric-weekly or monthly rate, the district shall pay the employee within 10 days after the end of each calendar month or regular pay period during which the services are performed.

(b) If a salary payment is not made timely as required by this section, the amount of the salary payment due shall be increased by an amount of interest on the unpaid amount for each day of delay.

(c) A certificated employee of a school district who qualifies for a salary increase shall be paid the increased salary not later than three regular pay periods or three months, whichever is longer, after the employee files proper documentation where required for the salary increase. The district shall additionally pay the employee daily interest on the amount owed to the employee calculated from the date that the employee was entitled to the salary increase if the school district does not pay the employee his or her salary increase within three regular pay periods or three months, whichever is longer, after the employee files proper documentation where required for the salary increase. All amounts due the employee resulting from the salary increase and not paid to the employee at the time that the employee actually receives the salary increase shall be paid to the employee within 20 business days of the date that the employee actually received the salary increase. The district shall the employee calculated from the date that the employee was entitled to the salary increase if the district does not pay the employee all amounts due the employee resulting from the salary increase within 20 business days following the date that the employee actually received the salary increase.

(d) The amount of interest required by subdivisions (b) and (c) shall be determined by the method established in Section 19521 of the of the Revenue and Taxation Code

PAYING EMPLOYEES

Alternative Payroll Procedure

Education Code 42646

42646. In any county, the county superintendent of schools, with the approval of the Superintendent of Public Instruction, the county board of education, and the county auditor, may prescribe a payroll procedure, to be followed by designated districts in the county, under which the school district governing boards, by use of payroll orders, shall authorize and direct the county superintendent of schools and the county auditor to draw separate payroll warrants in the names of the individual district employees for the respective amounts set forth therein to the end that each employee may be furnished with a statement of the amount earned and an itemization of the amounts withheld there from under requirements of the law or by direction of the employee.

The payroll warrants shall show the closing date of the pay period for which issued and the date of issue and a statement that it is drawn by order of the governing board of the district and shall bear the signature of the county auditor.

To obtain the advantage of a uniform pay period and pay date within school districts, the payroll procedure may specify the ending date of the pay period and, notwithstanding Sections 42644, 45040, and 45048, the date of issue for payroll warrants, except that the issue date shall be on or before the 10th calendar day following the end of the pay period. The payroll procedure may provide for salary payments, including salary advances, more frequently than once a month.

The payroll procedure may provide for payroll orders authorizing salary payments to individual employees on a continuing basis until notifications of changes or adjustments are submitted by the school districts, provided that an itemized listing of payments made under this procedure is furnished to the school district on or before the date of issue of the payroll warrants.

The payroll order may direct the transfer from the districts' funds to a clearing fund in the county treasury, to be known as the schools payroll revolving fund, of the total of the amount of the payroll warrants to be issued under the order to the end that payroll warrants for all districts may be drawn against a single revolving fund. The payroll order may further direct the transfer from the districts' funds of the totals of the various deductions set forth therein to the trust funds in the county treasury entitled to receive credit for them and may further direct the proper disbursement of such trust amounts.

When the payroll procedure provides for payment of salary once each month the payment shall be made on the last working day of the month as required by Section 45166.

PAYING EMPLOYEES

Payment of Terminating Employees
California Labor Code Section 220 exempts school districts and community colleges from California Labor Code 201 which provides for immediate payment of terminated employees by California employers. Terminated employees may be paid their final pay on the next scheduled payroll cycle.

Salary Corrections
Education Code Section 45167/88166 addresses the timeline for correcting errors for classified salary payments.

Error in Salary
Education Code 45167
Whenever it is determined that an error has been made in the calculation or reporting in any classified employee payroll or in the payment of any classified employee's salary, the appointing authority shall, within five workdays following such determination, provide the employee with a statement of the correction and a supplemental payment drawn against any available funds.

Classified Salary Payments
Education Codes 45166,42644,42646

SALARY TYPES	PAYMENT SCHEDULE	NOTES
All Classified Employees (EC 45166) K-12 (EC 88165) Comm. College	Shall be paid on the last working day of the current month which the employee was in paid status	For districts not using the provisions of Sections 42644, 42645, or 42646
Full-time Classified Employees (EC 42644) K-12 (EC 85244) Comm. College	Labor performed between the 1st and 15th shall be paid between the 16th and 26th day of the month during which the labor was performed; labor performed between the 16th and last day of the month shall be paid between the 1st and 10th day of the following month	
Alternative Payroll Procedure (EC 42646) K-12 (EC 85260) Comm. College	Issue date shall be on or before the 10th calendar day following the end of the payroll period. If employee is paid once a month, payment is due on the last working day of the month	Payroll Periods may be established by County Offices. Can be used in place of Education Code 42644
Error In Salary (EC 45167) K-12 (EC 88166) Comm. College	Supplemental payment shall be made within 5 workdays of time error was discovered	

Certificated Salary Payments K-12
Education Codes 45048 & 45049

SALARY TYPES	PAYMENT SCHEDULE	ISSUES TO ADDRESS
Monthly Contract & Substitute Certificated Employees (EC 45048)	Shall be paid on the last working day of the current month; no later than the fifth (5th) calendar day of the succeeding month.	Watch new hires that may miss monthly payroll cycle cutoff.
Monthly Part-time Adult School Employees (EC 45048)	Shall be paid on or before the tenth (10th) of the following month.	
Extra Assignments based on: Hourly, Daily, Monthly, Biweekly, Semimonthly, or Once Every Four (4) Weeks (EC 45049)	For performing teaching (including summer school) or other services outside normal teaching duties; shall be paid within ten (10) calendar days after the end of each calendar month or pay period during which services are performed.	
Extra Assignments based on: Lump-Sum Payments (EC 45049)	Shall be paid within ten (10) days after termination of the services. (Assignment completion date)	Watch stipends/summer school payments. Problematic if assignment completion outside of ten (10) days before a payroll issue date, i.e., coaching assignment ending fifteenth (15th) of the month. Must be paid by the twenty-fifth (25th) of the month.
Retroactive Pay Increases (EC 45049)	Salary changes shall be made no later than three (3) regular pay periods or	Coordinate salary change on payroll no more than twenty (20) business days

SALARY TYPES	PAYMENT SCHEDULE	ISSUES TO ADDRESS
	three (3) months, whichever is longer, after the date the agreement is ratified. Retroactive payments must be paid within twenty (20) business days of the date employees actually receive the salary increases.	before paying retro payments.
Column Movement (EC 45049)	Salary changes shall be made no later than three (3) regular pay periods or three (3) months, whichever is longer after the employee files proper documentation.	Gray Area: Three (3) regular pay periods or three (3) months may begin from dates set by language in bargaining unit contract.

NOTES OF INTEREST DUE

Any interest payment due must be calculated through the date of receipt, and paid at the same time the employee receives his/her late salary payment. The interest payment is not considered salary and should be made through a "B" warrant payment. Any interest paid to an employee totaling more than six hundred dollars ($600) within a calendar year is reportable to the IRS on "Form 1099-INT." Interest payments are not reportable on Form W-2.

Section 7: Illness/Injury Leaves

Section 7
ILLNESS & INJURY LEAVES

ILLNESS & INJURY LEAVES

LEAVES OF ABSENCE

The Education Code entitles certificated and classified employees to leaves of absences for various reasons. Collective bargaining and school boards can extend these leaves for a better benefit. In this section we have provided the Education Code references and copies of the most used codes for leaves.

Leaves are also provided by the California Government and Labor Code as well as the federal law providing for Family Medical leave. Below are leaves that are provided in addition to the Education Code Leaves:

Pregnancy Disability Leave Act
California Government Code Section 12945

12945. In addition to the provisions that govern pregnancy, child birth, or related medical conditions in Sections 12926 and 12940, it shall be an unlawful employment practice, unless based upon a bona fide occupational qualification:

(a) For an employer to refuse to allow a female employee disabled by pregnancy, childbirth, or related medical conditions to take a leave for a reasonable period of time not to exceed four months and thereafter return to work, as set forth in the commission's regulations. The employee shall be entitled to utilize any accrued vacation leave during this period of time. Reasonable period of time means that period during which the female employee is disabled on account of pregnancy, childbirth, or related medical conditions.

An employer may require an employee who plans to take a leave pursuant to this subdivision to give the employer reasonable notice of the date the leave shall commence and the estimated duration of the leave.

(b) (1) For an employer to refuse to provide reasonable accommodation for an employee for conditions related to pregnancy, child birth, or related medical conditions, if she so requests, with the advice of her health care provider.

(2) For an employer who has a policy, practice, or collective bargaining agreement requiring or authorizing the transfer of temporarily disabled employees to less strenuous or hazardous positions for the duration of the disability to refuse to transfer a pregnant female employee who so requests.

(3) For an employer to refuse to temporarily transfer a pregnant female employee to a less strenuous or hazardous position for the duration of her pregnancy if she so requests, with the advice of her physician, where that transfer can be reasonably accommodated.

However, no employer shall be required by this section to create additional employment that the employer would not otherwise have created, nor shall the employer be required to discharge any employee, transfer any employee with more seniority, or promote any employee who is not qualified to perform the job.

(c) This section shall not be construed to affect any other provision of law relating to sex discrimination or pregnancy, or in any way to diminish the coverage of pregnancy, childbirth, or medical conditions related to pregnancy or childbirth under any other provisions of this part, including subdivision (a) of Section 12940.

California Family Rights Act
California Government Code Section 12945.2

The California Family Rights Act (CFRA) along with the federal Family Medical Leave Act (FMLA), provide unpaid leaves of absences to employees for their own serious illnesses, child rearing, and to care for specified family members with serious illnesses or injuries. The FMLA and CFRA) leave may run concurrently with paid leave, if the employer notifies the employee in writing of the intention to do so. Notification must occur within two business days of learning the reason for the leave or when responding to an advanced leave request. The CFRA leave does not run concurrently with paid or unpaid pregnancy or related disability leave.

12945.2. (a) Except as provided in subdivision (b), it shall be an unlawful employment practice for any employer, as defined in paragraph (2) of subdivision (c), to refuse to grant a request by any employee with more than 12 months of service with the employer, and who has at least 1,250 hours of service with the employer during the previous 12-month period, to take up to a total of 12 workweeks in any 12-month period for family care and medical leave. Family care and medical leave requested pursuant to this subdivision shall not be deemed to have been granted unless the employer provides the employee, upon granting the leave request, a guarantee of employment in the same or a comparable position upon the termination of the leave. The commission shall adopt a regulation specifying the elements of a reasonable request.

(b) Notwithstanding subdivision (a), it shall not be an unlawful employment practice for an employer to refuse to grant a request for family care and medical leave by an employee if the employer employs less than 50 employees within 75 miles of the worksite where that employee is employed.

(c) For purposes of this section:

(1) "Child" means a biological, adopted, or foster child, a stepchild, a legal ward, or a child of a person standing in loco parentis who is either of the following:

(A) Under 18 years of age.

(B) An adult dependent child.

(2) "Employer" means either of the following:

(A) Any person who directly employs 50 or more persons to perform services for a wage or salary.

(B) The state, and any political or civil subdivision of the state and cities.

(3) "Family care and medical leave" means any of the following:

(A) Leave for reason of the birth of a child of the employee, the placement of a child with an employee in connection with the adoption or foster care of the child by the employee, or the serious health condition of a child of the employee.

(B) Leave to care for a parent or a spouse who has a serious health condition.

(C) Leave because of an employee's own serious health condition that makes the employee unable to perform the functions of the position of that employee, except for leave taken for disability on account of pregnancy, childbirth, or related medical conditions.

(4) "Employment in the same or a comparable position" means employment in a position that has the same or similar duties and pay that can be performed at the same or similar geographic location as the position held prior to the leave.

(5) "FMLA" means the federal Family and Medical Leave Act of 1993 (P.L. 103-3).

(6) "Health care provider" means any of the following:

(A) An individual holding either a physician's and surgeon's certificate issued pursuant to Article 4 (commencing with Section 2080) of Chapter 5 of Division 2 of the Business and Professions **Code**, an osteopathic physicians and surgeons certificate issued pursuant to Article 4.5 (commencing with Section 2099.5) of Chapter 5 of Division 2 of the Business and Professions **Code**, or an individual duly licensed as a physician, surgeon, or osteopathic physician or surgeon in another state or jurisdiction, who directly treats or supervises the treatment of the serious health condition.

(B) Any other person determined by the United States Secretary of Labor to be capable of providing health care services under the FMLA.

(7) "Parent" means a biological, foster, or adoptive parent, a stepparent, a legal guardian, or other person who stood in loco parentis to the employee when the employee was a child.

(8) "Serious health condition" means an illness, injury, impairment, or physical or mental condition that involves either of the following:

(A) Inpatient care in a hospital, hospice, or residential health care facility.

(B) Continuing treatment or continuing supervision by a health care provider.

(d) An employer shall not be required to pay an employee for any leave taken pursuant to subdivision (a), except as required by subdivision (e).

(e) An employee taking a leave permitted by subdivision (a) may elect, or an employer may require the employee, to substitute, for leave allowed under subdivision (a), any of the employee's accrued vacation leave or other accrued time off during this period or any other paid or unpaid time off negotiated with the employer. If an employee takes a leave because of the employee's own serious health condition, the employee may also elect, or the employer may also require the employee, to substitute accrued sick leave during the period of the leave. However, an employee shall not use sick leave during a period of leave in connection with the birth, adoption, or foster care of a child, or to care for a child, parent, or spouse with a serious health condition, unless mutually agreed to by the employer and the employee.

(f) (1) During any period that an eligible employee takes leave pursuant to subdivision (a) or takes leave that qualifies as leave taken under the FMLA, the employer shall maintain and pay for coverage under a "group health plan," as defined in Section 5000(b)
(1) Of the Internal Revenue **Code** of 1986, for the duration of the leave, not to exceed 12 workweeks in a 12-month period, commencing on the date leave taken under the FMLA commences, at the level and under the conditions coverage would have been provided if the employee had continued in employment continuously for the duration of the leave. Nothing in the preceding sentence shall preclude an employer from maintaining and paying for coverage under a "group health plan" beyond 12 workweeks. An employer may recover the premium that the employer paid as required by this subdivision for maintaining coverage for the employee under the group health plan if both of the following conditions occur:

(A) The employee fails to return from leave after the period of leave to which the employee is entitled has expired.

(B) The employee's failure to return from leave is for a reason other than the continuation, recurrence, or onset of a serious health condition that entitles the employee to leave under subdivision (a) or other circumstances beyond the control of the employee.

(2) Any employee taking leave pursuant to subdivision (a) shall continue to be entitled to participate in employee health plans for any period during which coverage is not provided by the employer under paragraph (1), employee benefit plans, including life, short-term, or long-term disability or accident insurance, pension and retirement plans, and supplemental unemployment benefit plans to the same extent and under the same conditions as apply to an unpaid leave taken for any purpose other than those described in subdivision (a). In the absence of these conditions an employee shall continue to be entitled to participate in these plans and, in the case of health and welfare employee benefit plans, including life, short-term, or long-term disability or accident insurance, or other similar plans, the employer may, at his or her discretion, require the employee to pay premiums, at the group rate, during the period of leave not covered by any accrued vacation leave, or other accrued time off, or any other paid or unpaid time off negotiated with the employer, as a condition of continued coverage during the leave period. However, the nonpayment of premiums by an employee shall not constitute a break in service, for purposes of longevity, seniority under any collective bargaining agreement, or any employee benefit plan.

For purposes of pension and retirement plans, an employer shall not be required to make plan payments for an employee during the leave period, and the leave period shall not be required to be counted for purposes of time accrued under the plan. However, an employee covered by a pension plan may continue to make contributions in accordance with the terms of the plan during the period of the leave.

(g) During a family care and medical leave period, the employee shall retain employee status with the employer, and the leave shall not constitute a break in service, for purposes of longevity, seniority under any collective bargaining agreement, or any employee benefit plan. An employee returning from leave shall return with no less seniority than the employee had when the leave commenced, for purposes of layoff, recall, promotion, job assignment, and seniority-related benefits such as vacation.

(h) If the employee's need for a leave pursuant to this section is foreseeable, the employee shall provide the employer with reasonable advance notice of the need for the leave.

(i) If the employee's need for leave pursuant to this section is foreseeable due to a planned medical treatment or supervision, the employee shall make a reasonable effort to schedule the treatment or supervision to avoid disruption to the operations of the employer, subject to the approval of the health care provider of the individual requiring the treatment or supervision.

(j) (1) An employer may require that an employee's request for leave to care for a child, a spouse, or a parent who has a serious health condition be supported by a certification issued by the health care provider of the individual requiring care. That certification shall be sufficient if it includes all of the following:

(A) The date on which the serious health condition commenced.

(B) The probable duration of the condition.

(C) An estimate of the amount of time that the health care provider believes the employee needs to care for the individual requiring the care.

(D) A statement that the serious health condition warrants the participation of a family member to provide care during a period of the treatment or supervision of the individual requiring care.

(2) Upon expiration of the time estimated by the health care provider in subparagraph (C) of paragraph (1), the employer may require the employee to obtain recertification, in accordance with the procedure provided in paragraph (1), if additional leave is required.

(k) (1) An employer may require that an employee's request for leave because of the employee's own serious health condition be supported by a certification issued by his or her health care provider. That certification shall be sufficient if it includes all of the following:

(A) The date on which the serious health condition commenced.

(B) The probable duration of the condition.

(C) A statement that, due to the serious health condition, the employee is unable to perform the function of his or her position.

(2) The employer may require that the employee obtain subsequent recertification regarding the employee's serious health condition on a reasonable basis, in accordance with the procedure provided in paragraph (1), if additional leave is required.

(3) (A) In any case in which the employer has reason to doubt the validity of the certification provided pursuant to this section, the employer may require, at the employer's expense, that the employee obtain the opinion of a second health care provider, designated or approved by the employer, concerning any information certified under paragraph (1).

(B) The health care provider designated or approved under subparagraph (A) shall not be employed on a regular basis by the employer.

(C) In any case in which the second opinion described in subparagraph (A) differs from the opinion in the original certification, the employer may require, at the employer's expense, that the employee obtain the opinion of a third health care provider, designated or approved jointly by the employer and the employee, concerning the information certified under paragraph (1).

(D) The opinion of the third health care provider concerning the information certified under paragraph (1) shall be considered to be final and shall be binding on the employer and the employee.

(4) As a condition of an employee's return from leave taken because of the employee's own serious health condition, the employer may have a uniformly applied practice or policy that requires the employee to obtain certification from his or her health care provider that the employee is able to resume work. Nothing in this paragraph shall supersede a valid collective bargaining agreement that governs the return to work of that employee.

(l) It shall be an unlawful employment practice for an employer to refuse to hire, or to discharge, fine, suspend, expel, or discriminate against, any individual because of any of the following:

(1) An individual's exercise of the right to family care and medical leave provided by subdivision (a).

(2) An individual's giving information or testimony as to his or her own family care and medical leave, or another person's family care and medical leave, in any inquiry or proceeding related to rights guaranteed under this section.

(m) This section shall not be construed to require any changes in existing collective bargaining agreements during the life of the contract, or until January 1, 1993, whichever occurs first.

(n) The amendments made to this section by the act adding this subdivision shall not be construed to require any changes in existing collective bargaining agreements during the life of the contract, or until February 5, 1994, whichever occurs first.

(o) The provisions of this section shall be construed as separate and distinct from those of Section **12945**.

(p) Leave provided for pursuant to this section may be taken in one or more periods. The 12-month period during which 12 workweeks of leave may be taken under this section shall run concurrently with the 12-month period under the FMLA, and shall commence the date leave taken under the FMLA commences.

(q) In any case in which both parents entitled to leave under subdivision (a) are employed by the same employer, the employer shall not be required to grant leave in connection with the birth, adoption, or foster care of a child that would allow the parents family care and medical leave totaling more than the amount specified in subdivision (a).

(r) (1) Notwithstanding subdivision (a), an employer may refuse to reinstate an employee returning from leave to the same or a comparable position if all of the following apply:

(A) The employee is a salaried employee who is among the highest paid 10 percent of the employer's employees who are employed within 75 miles of the worksite at which that employee is employed.

(B) The refusal is necessary to prevent substantial and grievous economic injury to the operations of the employer.

(C) The employer notifies the employee of the intent to refuse reinstatement at the time the employer determines the refusal is necessary under subparagraph (B).

(2) In any case in which the leave has already commenced, the employer shall give the employee a reasonable opportunity to return to work following the notice prescribed by subparagraph (C).

(s) Leave taken by an employee pursuant to this section shall run concurrently with leave taken pursuant to the FMLA, except for any leave taken under the FMLA for disability on account of pregnancy, childbirth, or related medical conditions. The aggregate amount of leave taken under this section or the FMLA, or both, except for leave taken for disability on account of pregnancy, childbirth, or related medical conditions, shall not exceed 12 workweeks in a 12-month period. An employee is entitled to take, in addition to the leave provided for under this section and the FMLA, the leave provided for in Section **12945**, if the employee is otherwise qualified for that leave.

Using Sick Leave for Family Care
California Labor Code Section 233

Labor Code 233. (a) Any employer who provides sick leave for employees shall permit an employee to use in any calendar year the employee's accrued and available sick leave entitlement, in an amount not less than the sick leave that would be accrued during six months at the employee's then current rate of entitlement, to attend to an illness of a child, parent, spouse, or domestic partner of the employee. All conditions and restrictions placed by the employer upon the use by an employee of sick leave also shall apply to the use by an employee of sick leave to attend to an illness of his or her child, parent, spouse, or domestic partner. This section does not extend the maximum period of leave to which an employee is entitled under Section 12945.2 of the Government **Code** or under the federal Family and Medical Leave Act of 1993 (29 U.S.C. Sec. 2606 et seq.), regardless of whether the employee receives sick leave compensation during that leave.

(b) As used in this section:

(1) "Child" means a biological, foster, or adopted child, a stepchild, a legal ward, a child of a domestic partner, or a child of a person standing in loco parentis.

(2) "Employer" means any person employing another under any appointment or contract of hire and includes the state, political subdivisions of the state, and municipalities.

(3) "Parent" means a biological, foster, or adoptive parent, a stepparent, or a legal guardian.

(4) "Sick leave" means accrued increments of compensated leave provided by an employer to an employee as a benefit of the employment for use by the employee during an absence from the employment for any of the following reasons:

(A) The employee is physically or mentally unable to perform his or her duties due to illness, injury, or a medical condition of the employee.

(B) The absence is for the purpose of obtaining professional diagnosis or treatment for a medical condition of the employee.

(C) The absence is for other medical reasons of the employee, such as pregnancy or obtaining a physical examination.

"Sick leave" does not include any benefit provided under an employee welfare benefit plan subject to the federal Employee
Retirement Income Security Act of 1974 (Public Law 93-406, as amended) and does not include any insurance benefit, workers' compensation benefit, unemployment compensation disability benefit, or benefit not payable from the employer's general assets.

(c) No employer shall deny an employee the right to use sick leave or discharge, threaten to discharge, demote, suspend, or in any manner discriminate against an employee for using, or attempting to exercise the right to use, sick leave to attend to an illness of a child, parent, spouse, or domestic partner of the employee.

(d) Any employee aggrieved by a violation of this section shall be entitled to reinstatement and actual damages or one day's pay, whichever is greater, and to appropriate equitable relief.

(e) Upon the filing of a complaint by an employee, the **Labor**
Commissioner shall enforce the provisions of this section in accordance with the provisions of Chapter 4 (commencing with Section 79) of Division 1, including, but not limited to, Sections 92, 96.7, 98, and 98.1 to 98.8, inclusive. Alternatively, an employee may bring a civil action for the remedies provided by this section in a court of competent jurisdiction. If the employee prevails, the court may award reasonable attorney's fees.

(f) The rights and remedies specified in this section are cumulative and nonexclusive and are in addition to any other rights or remedies afforded by contract or under other provisions of law.

FMLA – Time Off for Military Family Member

On January 28, 2008, President Bush signed the first significant amendments in 15 years to the federal Family and Medical Leave Act.

Effective February 2008, the Family and Medical Leave Act of 1993 provides up to 26 workweeks of medical leave to the immediate relatives (spouse, son, daughter, parent, or next of kin) to care for members of the Armed Forces who are seriously injured or ill. This is more than double the 12 workweeks of medical leave otherwise provided to employees under FMLA.

It also made provisions to allow families of members of the National Guard and Reserves manage their affairs while the member is on active duty in support of a contingency operation. This provision makes the normal 12 workweeks of FMLA job-protected leave available to eligible employees with a covered military member serving in the National Guard or Reserves to use for "any qualifying exigency" arising out of the fact that a covered military member is on active duty or called to active duty status in support of a contingency operation. The Department's final rule defines qualifying exigency by referring to a number of broad categories for which employees can use FMLA leave: (1) Short-notice deployment; (2) Military events and related activities; (3) Childcare and school activities; (4) Financial and legal arrangements; (5) Counseling; (6) Rest and recuperation; (7) Post-deployment activities; and (8) Additional activities not encompassed in the other categories, but agreed to by the employer and employee.

The amendments enacted in February 2008 have changed effective immediately.

President Obama signed into law the Fiscal Year 2010 National Defense Authorization Act, which provides, in part, for additional exigency and caregiver leave provisions for military families. The Act amends the military leave provisions of the FMLA, which were adopted in 2008. The changes took effect immediately.

The exigency leave benefit (of up to 12 weeks) now will be available to family members of active duty service members in the Armed Forces who are deployed to a foreign country. Formerly, this exigency leave was available only to family members of National Guard members and reservists.

In addition, under the Act, the caregiver leave benefit (of up to 26 weeks) now includes leave to take care of a child, spouse, parent or next of kin who (1) is a veteran, (2) is undergoing medical treatment, recuperation or therapy for serious injury or illness, and (3) was a member of the Armed Forces (including a member of the National Guard or Reserves) at any time during the five years preceding the date of treatment. The medical treatment must be related to a serious injury or illness incurred while in the line of duty on active duty in the Armed Forces or which existed before the beginning of military service, and which was aggravated by service in the line of duty while on active duty.

Employers should revise their FMLA policies and notices to reflect these new amendments and comply immediately.

California AB392 – Military Spouse Leave

Effective October 9, 2007, California employers with 25 or more employees must allow an employee who is a spouse of a member of the Armed Forces, National Guard, or Reserves to take up to 10 days of unpaid leave during a "qualified leave period."

Assembly Bill No. 392
CHAPTER 361
The people of the State of California do enact as follows:
SECTION1. Section 395.10 is added to the Military and Veterans Code, to read:

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395.10. (a) Notwithstanding any other provision of law, a qualified employer shall allow a qualified employee to take up to 10 days of unpaid leave during a qualified leave period.
(b) For purposes of this section:
(1) “Period of military conflict” means either of the following:
(A) A period of war declared by the United States Congress.
(B) A period of deployment for which a member of a reserve component is ordered to active duty pursuant to either of the following:
(i) Sections 12301 and 12302 of Title 10 of the United States Code.
(ii) Title 32 of the United States Code.
(2) “Qualified employee” means a person who satisfies all of the following:
(A) Is the spouse of a qualified member.
(B) Performs service for hire for an employer for an average of 20 or more hours per week, but does not include an independent contractor.
(C) Provides the qualified employer with notice, within two business days of receiving official notice that the qualified member will be on leave 93 from deployment, of his or her intention to take the leave provided for in subdivision (a).
(D) Submits written documentation to the qualified employer certifying that the qualified member will be on leave from deployment during the time the leave provided for in subdivision (a) is requested.
(3) “Qualified employer” includes any individual, corporation, company, firm, state, city, county, city and county, municipal corporation, district, public authority, or any other governmental subdivision, that employs 25 or more employees.
(4) “Qualified member” means a person who is any of the following:
(A) A member of the Armed Forces of the United States who has been deployed during a period of military conflict to an area designated as a combat theater or combat zone by the President of the United States.
(B) A member of the National Guard who has been deployed during a period of military conflict.
(C) A member of the Reserves who has been deployed during a period of military conflict.
(5) “Qualified leave period” means the period during which the qualified member is on leave from deployment during a period of military conflict.
(c) A qualified employer shall not retaliate against a qualified employee for requesting or taking the leave provided for in this section.
(d) The leave provided for in this section shall not affect or prevent a qualified employer from allowing a qualified employee to take a leave that the qualified employee is otherwise entitled to take.
(e) This section shall not affect a qualified employee’s rights with respect to any other employee benefit provided for in other laws.
SEC.2. This act is an urgency statute necessary for the immediate preservation of the public peace, health, or safety within the meaning of Article IV of the Constitution and shall go into immediate effect. The facts constituting the necessity are: In order to serve the families of those troops currently serving in military conflicts in Iraq and Afghanistan, and to assure that these families are able to spend time together during the qualified member’s leave from deployment, it is necessary that this act take effect immediately.

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California AB2393-Parental Leave effective January 1, 2017

SECTION 1.

Section 44977.5 of the Education Code is amended to read:

44977.5.

(a) (1) Notwithstanding any other law, during each school year, a person employed in a position requiring certification qualifications may use his or her sick leave for purposes of parental leave for a period of up to 12 workweeks.

(2) In school districts that use the differential pay system described in Section 44977, when a person employed in a position requiring certification qualifications has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of parental leave pursuant to Section 12945.2 of the Government Code, the amount deducted from the salary due him or her for any of the remaining portion of the 12-workweek period in which the absence occurs shall not exceed the sum that is actually paid a substitute employee employed to fill his or her position during his or her absence or, if no substitute employee was employed, the amount that would have been paid to a substitute had he or she been employed. The school district shall make every reasonable effort to secure the services of a substitute employee.

(3) In school districts that use the differential pay system described in Section 44983, when a person employed in a position requiring certification qualifications has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of parental leave pursuant to Section 12945.2 of the Government Code, the person shall be compensated at no less than 50 percent of his or her regular salary for the remaining portion of the 12-workweek period of parental leave.

(b) For purposes of subdivision (a), all of the following apply:

(1) The 12-workweek period shall be reduced by any period of sick leave, including accumulated sick leave, taken during a period of parental leave.

(2) A person employed in a position requiring certification qualifications shall not be provided more than one 12-week period for parental leave during any 12-month period.

(3) Parental leave taken pursuant to this section shall run concurrently with parental leave taken pursuant to Section 12945.2 of the Government Code. The aggregate amount of parental leave taken pursuant to this section and Section 12945.2 of the Government Code shall not exceed 12 workweeks in a 12-month period.

(c) This section shall be applicable whether or not the absence from duty is by reason of a leave of absence granted by the governing board of the employing school district.

(d) Notwithstanding subdivision (a) of Section 12945.2 of the Government Code, a person employed in a position requiring certification qualifications is not required to have 1,250 hours of service with the employer during the previous 12-month period in order to take parental leave pursuant to this section.

(e) Nothing in this section shall be construed to diminish the obligation of a public school employer to comply with any collective bargaining agreement entered into by a public school employer and an exclusive bargaining representative pursuant to Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code that provides greater parental leave rights to employees than the rights established under this section.

(f) For purposes of this section, "parental leave" means leave for reason of the birth of a child of the employee, or the placement of a child with an employee in connection with the adoption or foster care of the child by the employee.

SEC. 2.

Section 45196.1 is added to the Education Code, to read:

45196.1.

(a) (1) Notwithstanding any other law, during each school year, a classified employee may use his or her sick leave for purposes of parental leave for a period of up to 12 workweeks.

(2) In school districts that use the differential pay system described in the first paragraph of Section 45196, when a employee has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of parental leave pursuant to Section 12945.2 of the Government Code, the amount deducted from the salary due him or her for any of the remaining portion of the 12-workweek period in which the absence occurs shall not exceed the sum that is actually paid a substitute employee employed to fill his or her position during his or her absence.
(3) In school districts that use the differential pay system described in the last paragraph of Section 45196, when an employee has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of parental leave pursuant to Section 12945.2 of the Government Code, the employee shall be compensated at no less than 50 percent of the employee's regular salary for the remaining portion of the 12-workweek period of parental leave.
(b) For purposes of subdivision (a), all of the following apply:
(1) The 12-workweek period of parental leave shall be reduced by any period of sick leave, including accumulated sick leave, taken during a period of parental leave.
(2) An employee shall not be provided more than one 12-workweek period for parental leave during any 12-month period.
(3) Parental leave taken pursuant to this section shall run concurrently with parental leave taken pursuant to Section 12945.2 of the Government Code. The aggregate amount of parental leave taken pursuant to this section and Section 12945.2 of the Government Code shall not exceed 12 workweeks in a 12-month period.
(c) This section shall be applicable whether or not the absence from duty is by reason of a leave of absence granted by the governing board of the employing school district.
(d) Notwithstanding subdivision (a) of Section 12945.2 of the Government Code, a classified employee is not required to have 1,250 hours of service with the employer during the previous 12-month period in order to take parental leave pursuant to this section.
(e) Nothing in this section shall be construed to diminish the obligation of a public school employer to comply with any collective bargaining agreement entered into by a public school employer and an exclusive bargaining representative pursuant to Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code that provides greater parental leave rights to employees than the rights established under this section.
(f) For purposes of this section, "parental leave" means leave for reason of the birth of a child of the employee, or the placement of a child with an employee in connection with the adoption or foster care of the child by the employee.

SEC. 3.

Section 87780.1 is added to the Education Code, to read:

87780.1.

(a) (1) Notwithstanding any other law, during each school year, a person employed in an academic position may use his or her sick leave for purposes of parental leave for a period of up to 12 workweeks.
(2) In community college districts that use the differential pay system described in Section 87780, when a employee has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of parental leave pursuant to Section 12945.2 of the Government Code, the amount deducted from the salary due him or her for any of the remaining portion of the 12-workweek period in which the absence occurs shall not exceed the sum that is actually paid a temporary employee employed to fill his or her position during his or her absence or, if no temporary employee was employed, the amount that would have been paid to the temporary employee had he or she been employed.
(3) In community college districts that use the differential pay system described in Section 87786, when an employee has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of parental leave pursuant to Section 12945.2 of the Government Code, the employee shall be compensated at no less than 50 percent of the employee's regular salary for the remaining portion of the 12-workweek period of parental leave.

(b) For purposes of subdivision (a), all of the following apply:
(1) The 12-workweek period shall be reduced by any period of sick leave, including accumulated sick leave, taken during a period of parental leave.
(2) An employee shall not be provided more than one 12-workweek period for parental leave during any 12-month period.
(3) Parental leave taken pursuant to this section shall run concurrently with parental leave taken pursuant to Section 12945.2 of the Government Code. The aggregate amount of parental leave taken pursuant to this section and Section 12945.2 of the Government Code shall not exceed 12 workweeks in a 12-month period.
(c) This section shall be applicable whether or not the absence from duty is by reason of a leave of absence granted by the governing board of the employing community college district.
(d) Notwithstanding subdivision (a) of Section 12945.2 of the Government Code, a person employed in an academic position is not required to have 1,250 hours of service with the employer during the previous 12-month period in order to take parental leave pursuant to this section.
(e) Nothing in this section shall be construed to diminish the obligation of a public school employer to comply with any collective bargaining agreement entered into by a public school employer and an exclusive bargaining representative pursuant to Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code that provides greater parental leave rights to employees than the rights established under this section.
(f) For purposes of this section,"parental leave" means leave for reason of the birth of a child of the employee, or the placement of a child with an employee in connection with the adoption or foster care of the child by the employee.

SEC. 4.

Section 88196.1 is added to the Education Code, to read:

88196.1.

(a) (1) Notwithstanding any other law, during each school year, a classified employee may use his or her sick leave for purposes of parental leave for a period of up to 12 workweeks.
(2) In the community college districts that use the differential pay system described in the first paragraph of Section 88196, when a employee has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of parental leave pursuant to Section 12945.2 of the Government Code, the amount deducted from the salary due him or her for any of the remaining portion of the 12-workweek period in which the absence occurs shall not exceed the sum that is actually paid a substitute employee employed to fill his or her position during his or her absence.
(3) In community college districts that use the differential pay system described in the last paragraph of Section 88196, when an employee has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of parental leave pursuant to Section 12945.2 of the Government Code, the employee shall be compensated at no less than 50 percent of the employee's regular salary for the remaining portion of the 12-workweek period of parental leave.
(b) For purposes of subdivision (a), all of the following apply:
(1) The 12-workweek period of parental leave shall be reduced by any period of sick leave, including accumulated sick leave, taken during a period of parental leave.
(2) An employee shall not be provided more than one 12-workweek period for parental leave during any 12-month period.
(3) Parental leave taken pursuant to this section shall run concurrently with parental leave taken pursuant to Section 12945.2 of the Government Code. The aggregate amount of parental leave taken pursuant to this section and Section 12945.2 of the Government Code shall not exceed 12 workweeks in a 12-month period.
(c) This section shall be applicable whether or not the absence from duty is by reason of a leave of absence granted by the governing board of the employing community college district.

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(d) Notwithstanding subdivision (a) of Section 12945.2 of the Government Code, a classified employee is not required to have 1,250 hours of service with the employer during the previous 12-month period in order to take parental leave pursuant to this section.
(e) Nothing in this section shall be construed to diminish the obligation of a public school employer to comply with any collective bargaining agreement entered into by a public school employer and an exclusive bargaining representative pursuant to Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code that provides greater parental leave rights to employees than the rights established under this section.
(f) For purposes of this section, "parental leave" means leave for reason of the birth of a child of the employee, or the placement of a child with an employee in connection with the adoption or foster care of the child by the employee.

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Community College Districts
CLASSIFIED

EDUCATION CODE
Section

88190	Leave of absence and vacations
88191	Leave of absence for illness or injury
88192	Industrial accident and illness leaves for classified employees
88193	Leave of absence for pregnancy
88194	Bereavement leave of absence
88195	Additional leave for non-industrial accident or illness; re-employment preference
88196	Absences due to illness or accident; deductions from salary; payment of substitutes; sick leave entitlement
88196.5	Deduction from salary; amounts payable under insurance policy
88197	Annual vacations
88198	Power of Board to grant leaves of absence
88199	Power of governing board to grant leave of absence compensation for accident or illness
88200	Interruption or termination of vacation leave
88201	Resignations; effective date
88202	Transfer of accumulated sick leave and other benefits
88203	Paid holidays
88204	Exclusive weekend or holiday employment
88205	Holiday in lieu of specified holiday
88206	Substitute holiday
88205.5	Admission day
88207	Personal necessity

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Community College Districts
CERTIFICATED

EDUCATION CODE
Section

87763	Leaves of Absence
87764	Power to grant leaves of absence
87765	Power to grant leave of absence in case of illness, accident, or quarantine
87766	Power to grant leaves of absence for pregnancy
87767	Leaves of absence for study and travel
87768	Time qualifications for community college employees
87769	Service and compensation during leaves of absence for travel and study
87769.5	Agreement not to receive compensation during leave of absence
87770	Manner of payment for leave of absence time
87774	Reinstatement after leave of absence
87775	Liability for death or injury during leave of absence
87776	Effect of leave of absence on contract employee
87779	Rights to leaves of absence when school or place of employment transferred between districts
87780	Salary deductions due to absence from duties
87781	Leave for illness or injury; paid leave; accumulation
87781.5	Use of sick leave for personal reasons
87782	Transfer of accumulated sick leave
87783	Transfer of accumulated leave for injury or illness
87784	Leave of absence for personal necessity
87785	Transfer of accumulated leave of absence
87786	Exception to sick leave when district adopts specific rule
87787	Required rules for industrial accident and illness leaves of absence
87788	Leave of absence due to death in immediate family
87789	Applicant for disability allowance

ILLNESS & INJURY LEAVES

CERTIFICATED – Education Code

CERTIFICATED – Education Code 44963

General Leave Authority

When any provision of this code expressly authorizes or requires the governing board of a school district to grant a leave of absence for any purpose or for any period of time to persons employed in positions requiring certification qualifications, that express authorization or requirement does not deprive the governing board of the power to grant leaves of absence with or without pay to such employees for other purposes or for other periods of time, so long as the governing board does not deprive any employee of any leave of absence to which he is entitled by law.

CERTIFICATED – Education Code 44977

5 School Months – Sub Pay Deduct

(a) During each school year, when a person employed in a position requiring certification qualifications has exhausted all available sick leave, including all accumulated sick leave, and continues to be absent from his or her duties on account of illness or accident for an additional period of five school months, whether or not the absence arises out of or in the course of the employment of the employee, the amount deducted from the salary due him or her for any of the additional five months in which the absence occurs shall not exceed the sum that is actually paid a substitute employee employed to fill his or her position during his or her absence or, if no substitute employee was employed, the amount that would have been paid to the substitute had he or she been employed. The school district shall make every reasonable effort to secure the services of a substitute employee.

(b) For purposes of subdivision (a):

(1) The sick leave, including accumulated sick leave, and the five-month period shall run consecutively.

(2) An employee shall not be provided more than one five-month period per illness or accident. However, if a school year terminates before the five-month period is exhausted, the employee may take the balance of the five-month period in a subsequent school year.

(c) The governing board of every school district shall adopt a salary schedule for substitute employees. The salary schedule shall indicate a salary for a substitute for all categories or classes of certificated employees of the district.

(d) Excepting in a district the governing board of which has adopted a salary schedule for substitute employees of the district, the amount paid the substitute employee during any month shall be less than the salary due the employee absent from his or her duties.

(e) When a person employed in a position requiring certification qualifications is absent from his or her duties on account of illness for a period of more than five school months, or when a person is absent from his or her duties for a cause other than illness, the amount deducted from the salary due him or her for the month in which the absence occurs shall be determined according to the rules and regulations established by the governing board of the district. The rules and regulations shall not conflict with rules and regulations of the State Board of Education.

(f) Nothing in this section shall be construed so as to deprive any district, city, or city and county of the right to make any reasonable rule for the regulation of accident or sick leave or cumulative accident or sick leave without loss of salary for persons acquiring certification qualifications.

(g) This section shall be applicable whether or not the absence from duty is by reason of a leave of absence granted by the governing board of the employing district.

CERTIFICATED – Education Code 44978

10 Days Current Sick Leave

Every certificated employee employed five days a week by a school district shall be entitled to 10 days' leave of absence for illness or injury and additional days in addition thereto as the governing board may allow for illness or injury, exclusive of all days he or she is not required to render service to the district, with full pay for a school year of service. A certificated employee employed for less than five schooldays a week shall be entitled, for a school year of service, to that proportion of 10 days' leave of absence for illness or injury as the number of days he or she is employed per week bears to five and is entitled to additional days in addition thereto as the governing board may allow for illness or injury to certificated employees employed for less than five schooldays a week. Pay for any day of this absence shall be the same as the pay that would have been received had the employee served during the day. Credit for leave of absence need not be accrued prior to taking the leave by the employee and the leave of absence may be taken at any time during the school year. If the employee does not take the full amount of leave allowed in any school year under this section the amount not taken shall be accumulated from year to year with additional days as the governing board may allow. The governing board of each school district shall adopt rules and regulations requiring and prescribing the manner of proof of illness or injury for the purposes of this section. The rules and regulations shall not discriminate against evidence of treatment and the need therefor by the practice of the religion of any well-recognized church or denomination. Nothing in this section shall be deemed to modify or repeal any provision of law contained in Chapter 3 (commencing with Section 120175) of Part 1 of Division 105 of the Health and Safety Code. Section 44977 relating to compensation, shall not apply to the first 10 days of absence on account of illness or accident of the employee employed five days a week or to the proportion of 10 days of absence to which the employee employed less than five days a week is entitled hereunder on account of illness or accident or to additional days granted by the governing board. Any employee shall have the right to utilize sick leave provided for in this section and the benefit provided by Section 44977 for absences necessitated by pregnancy, miscarriage, childbirth, and recovery therefrom.

CERTIFICATED – Education Code 44978.1

Certificated Leave/Reemployment

When a certificated employee has exhausted all available sick leave, including accumulated sick leave, and continues to be absent on account of illness or accident for a period beyond the five-month period provided pursuant to Section 44977, and the employee is not medically able to resume the duties of his or her position, the employee shall, if not placed in another position, be placed on a reemployment list for a period of 24 months if the employee is on probationary status, or for a period of 39 months if the employee is on permanent status.

When the employee is medically able, during the 24- or 39-month period, the certificated employee shall be returned to employment in a position for which he or she is credentialed and qualified. The 24-month or 39-month period shall commence at the expiration of the five-month period provided pursuant to Section 44977.

CERTIFICATED – Education Code 44979

Transfer of Sick Leave (Employment Change)

Any certificated employee of any school district who has been an employee of that district for a period of one school year or more and who accepts a position requiring certification qualifications in another school district or community college district at any time during the second or any succeeding school year of his or her employment with the first school district, or who, within the school year succeeding the school year in which employment is terminated, signifies acceptance of his or her election or employment in a position requiring certification qualifications in another school district or community college district, shall have transferred with him or her to the second district the total amount of leave of absence for illness or injury to which he or she is entitled under Section 44978. The State Board of Education shall adopt rules and regulations prescribing the manner in which the first district shall certify to the second district the total amount of leave of absence for illness or injury to be transferred. No governing board shall adopt any policy or rule, written or unwritten, which requires any certificated employee transferring to its district to waive any part or all of the leave of absence which he or she may be entitled to have transferred in accordance with this section.

CERTIFICATED – Education Code 44981

Personal Necessity

Any days of leave of absence for illness or injury allowed pursuant to Section 44978 may be used by the employee, at his or her election in cases of personal necessity. The governing board of each school district and each office of county superintendent of schools shall adopt rules and regulations requiring and prescribing the manner of proof of personal necessity for purposes of this section.

The employee shall not be required to secure advance permission for leave taken for any of the following reasons:

(1) Death or serious illness of a member of his or her immediate family.

(2) Accident, involving his or her person or property, or the person or property of a member of his or her immediate family.

No such accumulated leave in excess of seven (7) days may be used in any school year for the purposes enumerated in this section unless a maximum number of days in excess of seven (7) is specified for that purpose in an agreement between the exclusive bargaining representative and the district.

CERTIFICATED – Education Code 44983

5 Months 50% Pay

Section 44977 shall not apply to any school district which adopts and maintains in effect a rule which provides that when a person employed in a position requiring certification qualifications is absent from his duties on account of illness or accident for a period of five school months or less whether or not the absence arises out of or in the course of the employment of the

employee, he shall receive 50 percent or more of his regular salary during the period of such absence and nothing in Section 44977 shall be construed as preventing the governing board of any district from adopting any such rule. Notwithstanding the foregoing, when a person employed in a position requiring certification qualifications is absent from his duties on account of illness for a period of more than five school months, or when a person is absent from his duties for a cause other than illness, the amount deducted from the salary due him for the month in which the absence occurs shall be determined according to the rules and regulations established by the governing board of the district. Such rules and regulations shall not conflict with rules and regulations of the State Board of Education. Nothing in this section shall be construed so as to deprive any district, city, or city and county of the right to make any reasonable rule for the regulation of accident or sick leave or cumulative accident or sick leave without loss of salary for persons requiring certification qualifications. This section shall be applicable whether or not the absence from duty is by reason of a leave of absence granted by the governing board of the employing district.

CERTIFICATED – Education Code 44984

60 Day Industrial Accident and Illness Leave

Governing boards of school districts shall provide by rules and regulations for industrial accident and illness leaves of absence for all certificated employees. The governing board of any district which is created or whose boundaries or status is changed by an action to organize or reorganize districts completed after the effective date of this section shall provide by rules and regulations for such leaves of absence on or before the date on which the organization or reorganization of the district becomes effective for all purposes as provided in Section 4064.
Such rules or regulations shall include the following provisions:

a. Allowable leave shall be for not less than 60 days during which the schools of the district are required to be in session or when the employee would otherwise have been performing work for the district in any one fiscal year for the same accident;

b. Allowable leave shall not be accumulated from year to year;

c. Industrial accident or illness leave shall commence on the first day of absence;

d. When a certificated employee is absent from his duties on account of an industrial accident or illness, he shall be paid such portion of the salary due him for any month in which the absence occurs as, when added to his temporary disability indemnity under Division 4 or Division 4.5 of the Labor Code, will result in a payment to him of not more than his full salary;
The phrase "full salary" as utilized in this subdivision shall be computed so that it shall not be less than the employee's "average weekly earnings" as that phrase is utilized in Section 4453 of the Labor Code. For purposes of this section, however, the maximum and minimum average weekly earnings set forth in Section 4453 of the Labor Code shall otherwise not be deemed applicable.

e. Industrial accident or illness leave shall be reduced by one day for each day of authorized absence regardless of a temporary disability indemnity award;

f. When an industrial accident or illness leave overlaps into the next fiscal year, the employee shall be entitled to only the amount of unused leave due him for the same illness or injury. Upon termination of the industrial accident or illness leave, the employee shall be entitled to the benefits provided in Sections 44977, 44978 and 44983, and for the purposes of

each of these sections, his absence shall be deemed to have commenced on the date of termination of the industrial accident or illness leave, provided that if the employee continues to receive temporary disability indemnity, he may elect to take as much of his accumulated sick leave which, when added to his temporary disability indemnity, will result in a payment to him of not more than his full salary. The governing board may, by rule or regulation, provide for such additional leave of absence for industrial accident or illness as it deems appropriate. During any paid leave of absence, the employee may endorse to the district the temporary disability indemnity checks received on account of his industrial accident or illness. The district, in turn, shall issue the employee appropriate salary warrants for payment of the employee's salary and shall deduct normal retirement, other authorized contributions, and the temporary disability indemnity, if any, actually paid to and retained by the employee for periods covered by such salary warrants. Any employee receiving benefits as a result of this section shall, during periods of injury or illness, remain within the State of California unless the governing board authorizes travel outside the state. In the absence of rules and regulations adopted by the governing board pursuant to this section an employee shall be entitled to industrial accident or illness leave as provided in this section but without limitation as to the number of days of such leave.

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CLASSIFIED– Education Code

CLASSIFIED– Education Code 44043

Temporary Disability – All Employees

Any school employee of a school district who is absent because of injury or illness which arose out of and in the course of the person's employment, and for which the person is receiving temporary disability benefits under the workers' compensation laws of this state, shall not be entitled to receive wages or salary from the district which, when added to the temporary disability benefits, will exceed a full day's wages or salary. During such periods of temporary disability so long as the employee has available for the employee's use sick leave, vacation, compensating time off or other paid leave of absence, the district shall require that temporary disability checks be endorsed payable to the district. The district shall then cause the employee to receive the person's normal wage or salary less appropriate deductions including but not limited to employee retirement contributions. When sick leave, vacation, compensating time off or other available paid leave is used in conjunction with temporary disability benefits derived from workers' compensation, as provided in this section, it shall be reduced only in that amount necessary to provide a full day's wage or salary when added to the temporary disability benefits.

CLASSIFIED– Education Code 44043.5

Catastrophic Leave – All Employees

(a) The governing board of a school district or county office of education may establish a catastrophic leave program to permit employees of that district or county office to donate eligible leave credits to an employee when that employee or a member of his or her family suffers from a catastrophic illness or injury.

For the purposes of this section the following terms are defined as follows:

(1) "Catastrophic illness" or "injury" means an illness or injury that is expected to incapacitate the employee for an extended period of time, or that incapacitates a member of the employee's family which incapacity requires the employee to take time off from work for an extended period of time to care for that family member, and taking extended time off work creates a financial hardship for the employee because he or she has exhausted all of his or her sick leave and other paid time off.

(2) "Eligible leave credits" means vacation leave and sick leave accrued to the donating employee.

(b) Eligible leave credits may be donated to an employee for a catastrophic illness or injury if all of the following requirements are met:

(1) The employee who is, or whose family member is, suffering from a catastrophic illness or injury requests that eligible leave credits be donated and provides verification of catastrophic injury or illness as required by the governing board of the school district or county office in which he or she is employed.

(2) The governing board of the school district or county office determines that the employee is unable to work due to the employee's or his or her family member's catastrophic illness or injury.

(3) The employee has exhausted all accrued paid leave credits.

(c) If the transfer of eligible leave credits is approved by the governing board of the school district or county office, any employee may, upon written notice to the governing board of the district or county office, donate eligible leave credits at a minimum of eight hours, and in hour increments thereafter.
(d) The governing board of a school district or county office that provides a catastrophic leave program pursuant to this section shall adopt rules and regulations for the administration of this section, including, but not limited to, the following:
(1) The maximum amount of time for which donated leave credits may be used, but not to exceed use for a maximum period of 12 consecutive months.
(2) The verification of catastrophic injury or illness required pursuant to paragraph (1) of subdivision (b).
(3) Making all transfers of eligible leave credit irrevocable.
(e) An employee who receives paid leave pursuant to this section shall use any leave credits that he or she continues to accrue on a monthly basis prior to receiving paid leave pursuant to this section.
(f) Notwithstanding the provisions of this section, the governing board of a school district or county office and an exclusive bargaining representative of employees in that district or county may agree to include in any collective bargaining agreement, a provision setting forth requirements for a catastrophic leave program.

CLASSIFIED– Education Code 45190

General Authority or Leaves
Governing boards of school districts may grant leaves of absence and vacations, with or without pay, to persons employed in the classified service of the district. This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

CLASSIFIED– Education Code 45191

12 Days Current Sick Leave
Every classified employee employed five days a week by a school district shall be entitled to 12 days leave of absence for illness or injury and such additional days, in addition thereto, as the governing board may allow for illness or injury, exclusive of all days he is not required to render service to the district, with full pay for a fiscal year of service. A classified employee, employed five days a week, who is employed for less than a full fiscal year is entitled to that proportion of 12 days leave of absence for illness or injury as the number of months he is employed bears to 12 and the proportionate amount, consistent with this formula, of such additional days, in addition thereto, authorized by the governing board for classified employees employed five days a week for a full fiscal year of service. A classified employee employed less than five days per week shall be entitled, for a fiscal year of service, to that proportion of 12 days leave of absence for illness or injury as the number of days he is employed per week bears to five and is entitled to the proportionate amount, consistent with this formula, of such additional days, in addition thereto, authorized by the governing board for classified employees employed five days a week for a full fiscal year of service. When such persons are employed for less than a full fiscal year of service this and the preceding paragraph shall determine that proportion of leave of absence for illness or injury to which they are entitled. Pay for any day

of such absence shall be the same as the pay which would have been received had the employee served during the day. Credit for leave of absence need not be accrued prior to taking such leave by the employee and such leave of absence may be taken at any time during the year. However, a new employee of a district shall not be eligible to take more than six days, or the proportionate amount to which he may be entitled under this section, until the first day of the calendar month after completion of six months of active service with the district. If such employee does not take the full amount of leave allowed in any year under this section the amount not taken shall be accumulated from year to year with such additional days as the governing board may allow. The governing board of each school district shall adopt rules and regulations requiring and prescribing the manner of proof of illness or injury for the purpose of this section. Such rules and regulations shall not discriminate against evidence of treatment and the need therefor by the practice of the religion of any well-recognized religious sect, denomination or organization. The provisions of this section shall not apply to a school district or districts, governed by the same governing board, in which the combined average daily attendance of all districts is in excess of 400,000, provided such districts maintain sick leave policies not less than those in effect in such districts on January 1, 1961. This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

CLASSIFIED– Education Code 45192

60 Days Industrial Accident or Illness Leave

Governing boards of school districts shall provide by rules and regulations for industrial accident or illness leaves of absence for employees who are a part of the classified service. The governing board of any district which is created or whose boundaries or status is changed by an action to organize or reorganize districts completed after the effective date of this section shall provide by rules and regulations for these leaves of absence on or before the date on which the organization or reorganization of the district becomes effective for all purposes as provided in Section 4064.

The rules and regulations shall include the following provisions**:**

(a) Allowable leave shall not be for less than 60 working days in any one fiscal year for the same accident.

(b) Allowable leave shall not be accumulative from year to year.

(c) Industrial accident or illness leave will commence on the first day of absence.

(d) Payment for wages lost on any day shall not, when added to an award granted the employee under the workers' compensation laws of this state, exceed the normal wage for the day.

(e) Industrial accident leave will be reduced by one day for each day of authorized absence regardless of a compensation award made under workers' compensation.

(f) When an industrial accident or illness occurs at a time when the full 60 days will overlap into the next fiscal year, the employee shall be entitled to only that amount remaining at the end of the fiscal year in which the injury or illness occurred, for the same illness or injury. The industrial accident or illness leave of absence is to be used in lieu of entitlement acquired under Section 45191. When entitlement to industrial accident or illness leave has been exhausted, entitlement or other sick leave will then be used; but if an employee is receiving

workers' compensation the person shall be entitled to use only so much of the person's accumulated or available sick leave, accumulated compensating time, vacation or other available leave which, when added to the workers' compensation award, provide for a full day's wage or salary. The governing board may, by rule or regulation, provide for as much additional leave of absence, paid or unpaid, as it deems appropriate and during this leave the employee may return to the person's position without suffering any loss of status or benefits. The employee shall be notified, in writing, that available paid leave has been exhausted, and shall be offered an opportunity to request additional leave. Periods of leave of absence, paid or unpaid, shall not be considered to be a break in service of the employee. During all paid leaves of absence, whether industrial accident leave as provided in this section, sick leave, vacation, compensated time off or other available leave provided by law or the action of a governing board, the employee shall endorse to the district wage loss benefit checks received under the workers' compensation laws of this state. The district, in turn, shall issue the employee appropriate warrants for payment of wages or salary and shall deduct normal retirement and other authorized contributions. Reduction of entitlement to leave shall be made only in accordance with this section. When all available leaves of absence, paid or unpaid, have been exhausted and if the employee is not medically able to assume the duties of the person's position, the person shall, if not placed in another position, be placed on a reemployment list for a period of 39 months. When available, during the 39-month period, the person shall be employed in a vacant position in the class of the person's previous assignment over all other available candidates except for a reemployment list established because of lack of work or lack of funds, in which case the person shall be listed in accordance with appropriate seniority regulations. The governing board may require that an employee serve or have served continuously a specified period of time with the district before the benefits provided by this section are made available to the person provided that this period shall not exceed three years and that all service of an employee prior to the effective date of this section shall be credited in determining compliance with the requirement. Any employee receiving benefits as a result of this section shall, during periods of injury or illness, remain within the State of California unless the governing board authorizes travel outside the state. In the absence of rules and regulations adopted by the governing board, pursuant to this section, an employee shall be entitled to industrial and accident or illness leave as provided in this section but without limitation as to the number of days of this leave and without any requirement of a specified period of service. An employee who has been placed on a reemployment list, as provided herein, who has been medically released for return to duty and who fails to accept an appropriate assignment shall be dismissed. This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

CLASSIFIED– Education Code 45195

Additional Non-Industrial Accident and Illness Leave

A permanent employee of the classified service who has exhausted all entitlement to sick leave, vacation, compensatory overtime, or other available paid leave and who is absent because of non-industrial accident or illness may be granted additional leave, paid or unpaid, not to exceed six months. The employee shall be notified, in writing, that available paid leave has been exhausted, and shall be offered an opportunity to request additional leave. The

board may renew the leave of absence, paid or unpaid, for two additional six-month periods or lesser leave periods that it may provide but not to exceed a total of 18 months. An employee, upon ability to resume the duties of a position within the class to which he or she was assigned, may do so at any time during the leaves of absence granted under this section and time lost shall not be considered a break in service. The employee shall be restored to a position within the class to which the employee was assigned and, if at all possible, to his or her position with all the rights, benefits and burdens of a permanent employee. If at the conclusion of all leaves of absence, paid or unpaid, the employee is still unable to assume the duties of his or her position, the employee shall be placed on a reemployment list for a period of 39 months. At any time, during the prescribed 39 months, the employee is able to assume the duties of his or her position the employee shall be re-employed in the first vacancy in the classification of his or her previous assignment. The employee's reemployment will take preference over all other applicants except for those laid off for lack of work or funds under Section 45298 in which case the employee shall be ranked according to his or her proper seniority. Upon resumption of his or her duties, the break in service will be disregarded and the employee shall be fully restored as a permanent employee. This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

CLASSIFIED– Education Code 45196

5 School Months of Less Sub Pay or 100 Day Alternative Rule

When a person employed in the classified service is absent from his duties on account of illness or accident for a period of five months or less, whether or not the absence arises out of or in the course of employment of the employee, the amount deducted from the salary due him for any month in which the absence occurs shall not exceed the sum which is actually paid a substitute employee employed to fill his position during his absence. Excepting in a district the governing board of which has adopted a salary schedule for substitute employees of the district, the amount paid the substitute employee during any month shall be less than the salary due the employee absent from his duties. Entitlement to sick leave provisions under this section, if any, shall be considered "entitlement to other sick leave" for the purposes of computing benefits under the provisions of Section 45192 if the absence is for industrial accident or illness and shall be used after entitlement to all regular sick leave, accumulated compensating time, vacation or other available paid leave has been exhausted. The foregoing provisions shall not apply to any school district which adopts and maintains in effect a rule which provides that a regular classified employee shall once a year be credited with a total of not less than 100 working days of paid sick leave, including days to which he is entitled under Section 45191. Such days of paid sick leave in addition to those required by Section 45191 shall be compensated at not less than 50 percent of the employee's regular salary. The paid sick leave authorized under such a rule shall be exclusive of any other paid leave, holidays, vacation, or compensating time to which the employee may be entitled. Nothing in this section shall preclude the governing board from adopting such a rule.

CLASSIFIED– Education Code 45202

Transfer of Leave (Employment Change)

Any classified employee of any school district, county superintendent of schools, or community

college district who has been employed for a period of one calendar year or more whose employment is terminated for reasons other than action initiated by the employer for cause and who subsequently accepts employment with a school district or county superintendent of schools within one year of the termination of his or her former employment, shall have transferred with him or her to the school district or county superintendent of schools the total amount of earned leave of absence for illness or injury to which he or she is entitled under Section 45191 or 88191. This transfer shall be in the same manner as is provided for certificated employees. In any case where an employee was terminated as a result of action initiated by the employer for cause, the transfer may be made if agreed to by the governing board of the school district or the county superintendent of schools newly employing the employee. All or any part of the previous service, not separated by a break in service greater than one year as of the last day of paid service, may, if agreed to by the employing entity, be construed to have been served in the school district or county superintendent of schools of employment for seniority purposes, except that the previous service may not be counted, for seniority purposes, when position or personnel reduction is ordered, for any reason, by the board. No governing board of a school district shall adopt any policy or rule, written or unwritten, which requires all classified employees, or any individual classification, or group of classifications of employees transferring to its district to waive any part or all benefits which they may be entitled to have transferred in accordance with this section. This section shall apply to school districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter.

CLASSIFIED– Education Code 45207

Personal Necessity Leave

Any days of absence for illness or injury earned pursuant to Section 45191, may be used by the probationary or permanent employee, at his or her election, in cases of personal necessity, including any of the following:

(a) Death of a member of his or her immediate family when additional leave is required beyond that provided in Section 45194 and that provided, in addition thereto, as a right by the governing board.

(b) Accident, involving his or her person or property, or the person or property of a member of his or her immediate family.

(c) Appearance in any court or before any administrative tribunal as a litigant, party, or witness under subpoena or any order made with jurisdiction.

(d) Such other reasons which may be prescribed by the governing board.

The governing board of each school district shall adopt rules and regulations requiring and prescribing the manner of proof of personal necessity for the purpose of this section. No earned leave in excess of seven days may be used in any school year for the purposes enumerated in this section. Immediate family has the same meaning as provided in Section 45194. This section shall apply to districts that have adopted the merit system in the same manner and effect as if it were a part of Article 6 (commencing with Section 45240) of this chapter. This section shall also apply to school districts that may be exempted from the provisions of Section 45191. Authorized necessity leave shall be deducted from sick leave earned under the provisions of the exemption of Section 45191.

ILLNESS & INJURY LEAVE

Extended Illness Leave

Extended Illness leave or differential pay is provided to certificated and classified employees who have depleted their current and accumulated sick leave. Some bargaining unit contracts may extend or provide for a benefit that exceeds what is provided in the Education Code. Below is the order of applying the extended illness leave according to the appropriate Education Code.

CERTIFICATED - 5 SCHOOL MONTHS
50% SICK PAY
Education Code 44983/87788

- ***5 SCHOOL MONTHS BEGIN***
- Use accumulated sick leave
- 50% pay for balance of 5 school month period

CERTIFICATED COMMUNITY COLLEGE - 5 SCHOOL MONTHS
SUB PAY DEDUCT
Education Code 87780

- ***5 SCHOOL MONTH LEAVE BEGINS***
- Use accumulated sick leave
- Sub pay deduction for balance of 5 school month period

CERTIFICATED K-12 - SUB PAY DEDUCT
Education Code 44977

- Use accumulated sick leave
- ***5 SCHOOL MONTH LEAVE BEGINS***
- Sub Pay Deduction for a five-month period per illness and/or injury
- An employee shall not be provided more than one five month period per illness and/or injury.
- Balance may be used in next school year for same illness and/or injury.

ILLNESS & INJURY LEAVE

CLASSIFIED LEAVE - 50% SICK PAY RULE
Education Code 45196/88196

- Employee is Entitled to 100 **Working Days** of 50% Pay Each Fiscal Year
- ***100 DAYS START***
- Use accumulated sick leave
- 50% pay for balance of 100 day period

CLASSIFIED LEAVE - 5 CALENDAR MONTH
Education Code 45196/88196

- ***BEGIN 5 CALENDAR MONTH***
- Use accumulated sick leave
- Use accrued compensatory time
- Use vacation leave
- Employee is entitled to the difference of his/her salary and that salary ***actually paid*** to a substitute for the balance of 5 calendar month period. *A substitute must be hired to fill the vacancy while employee is out on leave.

RE-EMPLOYMENT LISTS

K-12 CERTIFICATED -EDUCATION CODE 44978.1
Provides for a re-employment list of 39 months for permanent status teachers and 24 months for probationary teachers. When medically able, employee shall be returned to a position for which they are credentialed and qualified.

* Community College Academic Employees do not have an Education Code that addresses what the next step is when they exhaust all paid leaves.

CLASSIFIED – EDUCATION CODES 45195/88185
Once a classified employee exhausts all paid leave, they may apply for additional paid or unpaid leave not to exceed 6 months. Districts may refuse the additional leave. If the leave is approved, it may be renewed for up to two additional six-month periods. Once all leaves have been exhausted the employee is placed on a 39 month rehire list.

When medically able, the employee is entitled to return to a vacant position, “in the classification” of the employee’s previous assignment. If a layoff list is in place, they shall be placed on the layoff reemployment list based on seniority.

ILLNESS & INJURY LEAVES

WORKERS' COMPENSATION

Education Code 44984/87787(Certificated) and 45192/88192 (Classified) grants at least 60 day of fully paid industrial injury/illness leave per injury to employees. The governing board of each district should adopt rules and regulations governing industrial injury and illnesses. The regulations must provide for at least 60 working days of industrial injury/illness leave per accident. The leave is not cumulative from year to year.

When an industrial injury/illness overlaps into the next fiscal year, the employee is entitled to only that amount remaining from the 60 days at the end of the fiscal year, in which the injury or illness occurred, for the same injury or illness. The governing board may provide for any additional leave of absence, paid or unpaid that it deems appropriate. Without board policies in effect, employees may be entitled to unlimited leave.

When the employee completes the 60 days of fully paid industrial injury/illness leave, he/she will be eligible to access sick leave and other paid leave and then continue with the 100 day/five month period of difference pay allowed.

When all available paid time has been calculated, a date is determined when salary continuance ceases. The claims adjuster should be notified immediately if they have been sending payments to the district so they might begin paying the employee directly. Substitute and temporary employees on the job may be eligible for direct payments from the claims adjuster since they are not paid by the district for time not worked.

HANDLING SICK LEAVE DAYS

When using sick days for worker's compensation leave, the current and accumulated sick leave will need to be pro-rated based upon any temporary disability payment made to or on behalf of the employee by the worker's compensation vendor.

The daily rate of pay is	$100.00
The daily w/c rate of pay is	- 40.00
District pay is	$ 60.00

$60.00 divided by daily rate of $100.00 = 60% of a full day's pay

If the employee receives a pay increase or the temporary disability rate changes during the disability period, the inflation rate must be recalculated.

ILLNESS & INJURY LEAVES

CERTIFICATED - 5 SCHOOL MONTHS at 50% SICK PAY
Education Code 44983/87788

- ***60 DAYS WORKER COMPENSATION PAY***
- 5 School Months Begin
- Use accumulated sick leave
- 50% pay for balance of 5 school month period

CERTIFICATED COMMUNITY COLLEGE – 5 SCHOOL MONTHS with SUB PAY DEDUCT
Education Code 87780

- ***60 DAYS WORKER COMPENSATION PAY***
- 5 School Months Leave Begin
- Use accumulated sick leave
- Sub pay deduction for balance of 5 school month period

CERTIFICATED K-12 - SUB PAY DEDUCT
Education Code 44977

- ***60 DAYS WORKER COMPENSATION PAY***
- Use accumulated sick leave
- 5 School Months Leave Begins
- Sub pay deduction for a five-month period per illness and/or injury
- An employee shall not be provided more than one five month period per illness and/or injury.
- Balance may be used in the next year for same illness and/or injury.

CLASSIFIED LEAVE - 50% SICK PAY RULE
Education Code 45196/88196

- ***60 DAYS WORKER COMPENSATION PAY***
- Employee is entitled to 100 **Working Days** of 50% Pay Each Fiscal Year
- 100 Days Start
- Use accumulated sick leave
- 50% pay for balance of 100 day period

CLASSIFIED LEAVE - 5 CALENDAR MONTH
Education Code 45196/88196

- Begin 5 Calendar Month
- ***60 DAYS WORKER COMPENSATION PAY***
- Use accumulated sick leave
- Use accrued compensatory time
- Use vacation leave
- Employee is entitled to the difference of his/her salary and that salary ***actually paid*** to a substitute for the balance of 5 calendar month period. *A substitute must be hired to fill the vacancy while employee is out on leave.

ILLNESS & INJURY LEAVES

WORKERS' COMPENSATION ABATEMENTS

When a third party such as a claims adjuster makes payments to an employee for workers' compensation, the payments are non-taxable. If the adjuster makes the payments directly to the district, instead of to the employee, the payments are also non-taxable. The employee should have their taxable wages decreased by the amount of the workers' compensation payment to the district. All applicable taxes such as federal income tax, state income tax, FICA, Medicare and SDI should be refunded to the employee. Employers should make sure that their employees receive correct W-2 information at year end. The employee’s salary account should be abated by the amount of the workers' compensation payment from the insurance carrier.

ILLNESS INJURY LEAVES

Workers Compensation Benefit Worksheet

Employee Name: Mary Johns **Date:** 6/8/2018

Date of Injury: 2/1/2017

Workers Comp. Paid Periods	Amount of Check	No. of Days
02/01/2018 - 02/14/2018	$490.00	10
TOTAL	**(1) $490.00**	**(2) 10**

SICK LEAVE ADJUSTMENT CALCULATION

W/C Daily Rate
W/C Benefits **(1) $490.00 / Days (2) 10 = W/C Daily Rate $49.00**

Employee Daily Rate - W/C Daily Rate = Adjusted Value of Sick Leave (S/L)
120.00 Less $49.00 = $71.00

Adjusted Value S/L 71.00 divided by **Employee Daily Rate** $120.00 = 59%

As of 2/1/2018 **Unused Sick Leave Days** 16 divided by 59% = 27 **Days**
Other Leaves: **Days** divided by = **Days**

FISCAL YEAR DATES	DUTY DAYS	DAYS WORKED	HOLIDAY/ LEAVES	VACATION	60 DAY W/C	S/L @ FULL PAY	S/L @ 1/2 PAY
2/01-2/28	20				20		
MARCH	23				23		
APRIL	20				17	3	
MAY	22					22	
JUNE	6					2	4
TOTALS	91	0	0	0	60	27	4

Section 8
RETIREMENT ISSUES

RETIREMENT ISSUES

Retirement Reporting for School and Community College Employees

California school district and community college employees may be mandated to belong and pay contributions into a state retirement plan. The state retirement plan an employee originally qualifies for membership in depends on their employee type and/or position.

The retirement system and membership status must be determined at the time the individual is hired. It may be necessary to re-determine the status each time an employee changes positions (i.e., classified to certificated) or experiences a change in employment conditions such as an increase in hours.

The state retirement systems are known as “defined benefit plan” systems. A defined benefit plan provides retirement benefits based on a formula using the employee’s age, compensation level, and length of service. Contributions into the plan are paid by both the employee and employer. Contribution amounts are actuarially determined by the state plans. Employers may through collective bargaining pick up the employee contributions.

CalSTRS- the California State Teachers Retirement System provides retirement coverage for eligible certificated employees. CalSTRS regulations can be found in the California Education Code Sections 22000-28101.

CalPERS- the California Public Employees’ Retirement System provides retirement coverage to eligible classified employees. CalPERS regulations can be found in California Government Code Sections 20000-22970.

RETIREMENT ISSUES

Public Employees' Retirement System (Cal-PERS)

As of January 1, 2013 under the Public Employees' Pension Reform Act of 2013 (**PEPRA**) employees who were members of CalPERS or a reciprocal system prior to 1/1/2013 are considered Classic Members and employees who become members of CalPERS for the first time after 1/1/2023 are considered New Members.

Cal-PERS Membership Qualifications-GC 20281

- Permanent Full-Time (40 hours per week)
- Part-Time averaging at least 20 hours per week, for at least one year
- Full-time for a temporary appointment in excess of 6 months
- Currently a member of a Cal-PERS – including membership established with another Cal-PERS agency (GC 20305 (a)(1))

If Funds are on deposit with Cal-PERS from previous employment – compulsory membership regardless if the type of employment less than half time **(GC 20281).**

New hires coming from a reciprocal agency need to fill out CalPERS Member Reciprocal Self-Certification Form (PERS-CASD-801). This form is used to identify if a new employee is a classic member due to reciprocity. See Circular Letter 200-063-12.

Temporary, Seasonal, on call, Emergency, Substitute, or Irregular basis (GC20305) (a) (3) (B)

- Qualifies when worked 1000 Hours or 125 days in a Fiscal Year
- Overtime Hours are included for qualifying purposes

Cal-PERS Membership Exclusions-GC 20300

- Independent Contractors
- Elected or appointed officers (effective July 1, 1994)
- Students employed by a school district they attend in a position established for only students
- Community colleges use the IRS guidelines, where student's status is based on attending 12 units in their district covered colleges

Retirement Contributions for 2017-2018

- Classic Member Contributions – 7%
- PEPRA New Member Contributions – 6.5%
- District Contributions – 15.531%
- Survivor Benefits - $2.00 per Pay period (For Non Social Security Districts)

RETIREMENT ISSUES

- PERS Employer's rate changes every fiscal year based on Actuarial Assessment. The Cal-PERS rate is an employer pool rate

Cal-PERS Compensation

- Pay Rate – A member's normal monthly rate of pay or base pay
- Report as earned according to the job classification
- Must be reflected in a publicly available pay schedule or bargaining unit agreement
- PERS members can be paid
  - Monthly Basis
  - Hourly Basis
  - Daily Basis

Special Compensation – Additional pay that an employee receives for special skills or knowledge. California Code of Regulations Section (CCR's) 571(a) & (b)

- Special Compensation items must meet definitions listed in 571(a) as well as the criteria outlines in 571(b) to be reported to Cal-PERS
- Limited to what is indicated by a labor policy or agreement to similarly situated members of a group or class of employment
- Reported in addition to and separately from pay rate
- See CalPERS Circular Letter, 200-062-12, dated December 27, 2012, Public Employees' Pension Reform Act of 2013-Pensionable Compensation and Benefit Enhancements

Commonly used special compensations items by schools:

- Incentive pay – includes bonus pay and longevity
- Educational pay – includes professional growth and/or educational incentive pay but not cost of tuition, books or registrations
- Bilingual Pay
- Premium/Temporary Upgrade pay – includes working out of class
- Shift Differential
- Holiday pay – When employees are required to work during scheduled holidays and paid over and above the normal salary
- Uniform Allowances (only applies to Classic Members) – Compensation paid or reimbursed for the monetary value of purchasing, renting and maintaining required clothing
  - Clothing must be a substitute for personal attire clothing (per IRS definition)
  - Excludes items considered safety equipment such as protective vests, pistols, bullets, and steel-toed boots

RETIREMENT ISSUES

Non-Reportable Compensation

- Automobile/Mileage Allowance
- Overtime over full month
- Cafeteria Plans
- Cash In lieu of health benefits
- Health Benefits/Fringe Benefits
- API Awards
- Lump sum vacation to clear books
- Severance pay

Cal-PERS Service Credit

- A member in full-time employment will be credited one year of service credit
- 10 months of work
- 215 days of work
- 1,720 hours of work in a fiscal year

How is service credit earned?

- Fiscal Year Basis: July 1 – June 30
- Earned by tenths: 10 Months = 1 Year
- Pro-rated for part-time employees based on 1720 Hours = 1 Year
- Service Credit = earnings ÷ full time pay rate for each service period

Qualifying Elections (EC 22508)

- Cal-STRS member hired for classified PERS position
- 60 days to elect to stay in Cal-STRS
- Use Form ES-372
- Cal-PERS member hired for a certificated STRS Position
- 60 days to elect to stay in Cal-PERS
- Use Form ES-372

Compensation Cap for CalPERS New Members-Employee portion only

For New Members who participate in Social Security, compensation is capped at the Social Security Wage Base. For 2018 calendar year the compensation cap is $121,388

For New Members who do not participate in Social Security, compensation is capped at 120% of the Social Security Wage Base. For 2018 calendar year the compensation cap is $145,666.

RETIREMENT ISSUES

Hiring a Cal-PERS Retiree (GC 21220)

- Can be hired for temporary assignment during emergency or the retiree has special skills
- Retirees can work up to 960 hours in a fiscal year
- An individual who retirees after January 1, 2013 must wait 180 days before returning to CalPERS covered employment unless they qualify for the 180 day exception. The employer must submit a copy of the certification-resolution along with a copy of the retiree's employment agreement to CalPERS before the first day of employment. None of the exceptions apply if the retiree receives a Golden Handshake or any other retirement incentive (G.C. 7552.56(f)).
- Retirees under "normal retirement age" must have a 60 calendar day separation in service prior to returning to employment as "retired annuitant" even if an exception to the 180-day wait period applies.
- A retiree can be appointed once as an interim employee to a vacant position during the recruitment for a permanent replacement. The recruitment must be "opened" and in place before the retiree is appointed. All other retired annuitant requirements also apply to interim appointments. (G.C. section 7522.56 and 21221(h)).
- The pay rate the retiree receives must be within the pay rate range to other employees performing comparable duties as listed on the employer's publically available pay schedule.
- The retiree cannot receive any benefit, incentive, compensation in lieu of benefits, or other form of compensation in addition to the hourly pay rate.
- If a retiree is hired through a third party employer or temporary employment agency and the position is one in which an active CalPERS member would earn service credit, the employment is subject to the retired annuitant requirements, you must obtain the pay rate and hours from the third party employer and report the retiree's payroll the same as for your directly employed retired annuitants.
- All retirees hired as retired annuitants must be enrolled and their payroll reported to CalPERS.

Cal-PERS Retiree/Unemployment

- District cannot hire a retired annuitant that received unemployment insurance payments for prior retired annuitant employment with any public employer within the previous 12 months. (G.C. section 7522.56(e) and 21224).

Hiring a Cal-PERS Disability Retiree

- Retirees can work for 960 hours – No approval required

- Employment in a permanent position with Cal-PERS Employer:

  - Employment must be in a different position
  - Cal-PERS approval required before accepting employment
  - Earnings limitation applies

RETIREMENT ISSUES

State Teachers' Retirement System (Cal-STRS)

As of January 1, 2013 under the Public Employees' Pension Reform Act of 2013 (**PEPRA**) employees who became a member of CalSTRS prior to 1/1/2013 are considered 2% at 60 and employees who become members of CalSTRS after 1/1/2013 are considered 2% at 62.

Cal-STRS Membership Qualifications- Ed Code 22502

- Full-Time (100% FTE) contract qualifies immediately at start of contract
- Part-time (50% - 99.9% FTE) qualifies 2nd pay period from hire

Less than 50% of Contract/daily/Hourly-Ed Code 225604

- Qualifies after 60 Hours/10 days
- Qualifies With a single district
- Qualifies first of following pay period

Substitute-Long Term/Daily/Hourly-Ed Code 22503

- Qualifies after 600 Hours/100 Days
- Qualifies with a single district
- Qualifies first of following pay period

Permissive Election (EC 22515)-SB352 changes effective 1/1/2017

- Provide NEW Form ES-350 "Permissive Election" to the employee within 30 days of the hire date
- Permissive election Form ES-350 is irrevocable
- No earlier than 30 days after the form is signed
- Form must be sent to CalSTRS no later than 30 days after it is signed

Qualifying Elections (EC 22508)-SB352 changes effective 1/1/2017

- Cal-STRS member hired for classified PERS position
- 60 days to elect to stay in Cal-STRS
- Use NEW Form ES-372
- Cal-PERS member hired for a certificated STRS Position *New Rules*
- 60 days to elect to stay in Cal-PERS
- Use NEW Form ES-372
- Form must be sent to CalSTRS no later than 30 days after it is signed

RETIREMENT ISSUES

Non Creditable Compensation if:

- The position is not eligible for state apportionment and
- Position does not require credential, certificate or permit
- See attached CalSTRS Employer Information Circular, Volume 28, Issue 1 dated August 29, 2012

Special Compensation

See CalSTRS Employer Directive 2012-07, California Public Employees Retirement Act of 2013 for special compensation reporting requirements.

Cal-STRS Service Credit

Cal-STRS service credit is calculated by dividing Earnings by the Full Annual Salary basis

Retirement Contributions for 2017-2018

- Member Contributions – 10.25% 2%@60
  9.205% 2%@62
- District Contributions – 14.43%
- Reduced Workload - 14.43% for 2017-2018

Compensation Cap for CalSTRS 2% at 62-Employee portion only

Chapter 296 added section 7522.10 to the Government Code, which establishes a limit on compensation used to calculate benefits for CalSTRS 2% at 62, including compensation credited to the DBS Program. For CalSTRS 2% at 62, the cap on compensation is equal to 120 percent of the 2013 Social Security contribution and benefit base, adjusted annually based on changes to the Consumer Price Index for All Urban Consumers. Beginning July 1, 2017 through June 30, 2018, the compensation cap for CalSTRS 2% at 62 is $143,082.

Employment of a Cal-STRS Retiree

- Cal-STRS retiree can work in certificated position with earnings limitation.
- Cal-STRS earnings limitations for 2017-2018 is $43,755.00.
- Cal-STRS retiree can work in a classified position as Instructional aide only (EC 45134)
- Pursuant to Section 24214.5 retired CalSTRS members who are under age 60 and have been retired for less than 6 months and returns to work during that time CalSTRS will reduce their retirement benefit dollar for dollar by an amount equal to their earnings.
- Under PEPRA a CalSTRS member who retires after January 1, 2013 cannot return to creditable service for 180 days after retirement.

RETIREMENT ISSUES

Unused Sick Leave & Excess Sick leave (EC 44978, 87781)

- Members with unused sick leave days receive additional service credit at retirement
- Basic Sick Leave – One day's paid leave of absence per pay period
- Excess Sick Leave – Number of days in excess of basic sick leave
- Formula for sick leave service credit: (Basic days + Excess days)/Contract Base Days
- *Last employer pays present value for excess sick leave service credit at retirement*
- Employers are required to report basic & Excess separately at retirement(EC 22724)

Retirement Qualification Rules

AUTOMATIC MEMBERSHIP AT APPOINTMENT:

CalPERS	CalSTRS	Membership Effective
Permanent Full-Time (100% FTE) (40 Hours Per Week) Full- Time for a Temporary Appointment in Excess of 6 Months Part-Time Averaging at Least 20 Hours per Week, for at Least One Year	Full Time Contract (100% FTE) (EC 22501)	First Working Day
	Part-Time (50%-99.9% FTE) Contract (EC 22502)	2nd Pay Period from Hire
Currently a Member of CalPERS Including Membership Established with Another CalPERS Agency (GC 20305(a)(1) *If Funds Are On Deposit With CalPERS From Previous Employment, Compulsory Membership Regardless Of The Type Of Employment Less Than Half Time (GC 20281)	Currently a Member of CalSTRS from Previous Employment (EC 22500) *If Funds Are On Deposit With CalSTRS From Previous Employment, Compulsory Membership Regardless Of The Type Of Certificated Employment Less Than Half Time (EC 22500)	First Working Day

MONITOR FOR CALPERS/CALSTRS QUALIFICATION (EMPLOYEES HIRED FOR LESS THAN HALF TIME, SUBSTITUTE, SHORT-TERM, TEMPORARY)

CalPERS	CalSTRS	Membership Effective
Worked 1000 Hours or 125 Days in a Fiscal Year, Includes Service with Different Districts within the Same County	Worked 60 Hours/10 Days in a Single District in One Month in Same Fiscal Year (EC 22504)	**CalPERS & CalSTRS**: First Day of the Month Following Qualification in the same fiscal year. *Does Not Apply for CalSTRS If Qualification in the Month of June
Full-Time Temporary Position for Less Than 6 Months (GC 20305(a)(3)(B))	Works 100 Days in a Single District in a Fiscal Year (EC 22503)	**PERS**: First Day of the Seventh Month of Employment **STRS**: First Day of the Pay Period in Which 100 days are Completed
	Permissive Election Any Time (EC 22515)	30 days after the ES 350 Form is Signed

Establishing Membership in CalSTRS and CalPERS

Recent CalSTRS audits have found that many districts have not implemented the correct recordkeeping procedures to assure that employees have been given the opportunity, when applicable, to become a member of CalSTRS under "Permissive Membership Election". Employee written acknowledgment should also be available to prove that employees who qualify for a "Right of Election" into CalPERS or CalSTRS have been informed of their right and given the proper election form.

CalSTRS Form ES 350 "Permissive Membership Election," should always be given to employees being hired into certificated positions who are not members of CalSTRS and whose position does not qualify for immediate CalSTRS membership. The ES 350 form must be completed and returned by the employee, to the district, indicating their acceptance or declination for permissive membership into CalSTRS. Once membership with CalSTRS is established, it is irrevocable and will result in all future CalSTRS Creditable positions being reported to CalSTRS until termination of membership in the system and a refund of the member's CalSTRS contributions.

Form ES 372 "Right to Election," should be given to employees who are members of CalSTRS and have accepted a position that meets membership qualifications with CalPERS. The form should also be given to CalPERS members who are either vested or are employed by a school employer, the Board of Governors of the California Community Colleges, or the State Department of Education within 120 days before the member's date of hire to perform service that requires member and have accepted a position that meets mandatory membership qualifications with CalSTRS. The employee has 60 days after the hire date to return the form to the employer, though it is not required to be returned unless the employee chooses to elect into the alternate retirement system. However, EC 22509 requires that within 10 working days of hire, an employer must provide the employee Form ES 372 and their right to make this election with the information regarding their election rights and must make available written information about the retirement systems to assist the employee in making an election. Districts are recommended to retain a written acknowledgement from employees that they have been advised and given Form ES 372 as to their retirement membership rights. The acknowledgment should be collected at the time the form is provided in the event the employee chooses not to return the election form.

Districts should check with their county office retirement department for instructions on where to send the completed Forms ES 350 and ES 372. Effective 1/1/2017 Forms ES 350 and ES 372 must be received by the appropriate retirement systems within 30 days of the date on which the employee signs and dates the form.

The following scenarios have been established to assist districts with making determinations and understanding required procedures for providing forms and setting an employee up in the appropriate retirement systems. These scenarios will not apply

to hiring a CalSTRS or CalPERS retiree who has retired from a K-12, Community College or County Office.

Certificated Retirement Scenarios

1) Positions: Certificated Full Time Contract (100% FTE) or
Certificated Part Time Contract (50% - 99% FTE)

Current Retirement Status: Non Member of CalPERS/CalSTRS

- 100% FTE Full Time Contract: Establish membership to CalSTRS upon hire
- 50% - 99% FTE Part Time Contract: Establish membership to CalSTRS on 2nd pay period.

2) Positions: Certificated Full Time Contract (100% FTE) or
Certificated Part Time Contract (50% - 99% FTE)

Current Retirement Status: CalPERS School Member

1.) A member of CalPERS who is employed by a school employer, Board of Governors of the California Community College Districts or State Department of Education within 120 days before the member's date of hire to perform service that requires membership in the Defined Benefit Program of the State Teachers' Retirement Plan **or** has at least five years of CalPERS credited service, as defined in Government Code Section 20309 will have that service credited with CalSTRS unless he/she files a written election (within 60 days of the date of hire in the new position) to have the service credited with CalPERS.) ***Effective January 1, 2018***

2.) If the employee meets the above listed criteria take the following steps:

- Provide Form ES 372 Right of Election & "Join CalSTRS? Join CalPERS?" to the employee within 10 working days of hire
- Employee has 60 days from date of hire to elect to have the new CalSTRS position reported to CalPERS
- If the employee fails to return the completed Form ES 372 within 60 days of hire date, establish the position to be covered by CalSTRS
- If the employee elects CalPERS on Form ES 372, establish the position to be covered by CalPERS
- If the employee elects CalSTRS on Form ES 372, establish the position to be reportable to CalSTRS

Important Note: No election is required if employee chooses to become a member of CalSTRS but you should still have the employee sign and date a statement that backs up the fact that they were given the option of election

RETIREMENT ISSUES

3) Positions: Certificated Full Time Contract (100% FTE) or
Certificated Part Time Contract (50% - 99% FTE)

Current Retirement Status: CalPERS **Non-School** Member
Example: Cal State systems, Universities & City Employment under CalPERS.

1) Check to see if the member is vested (5 years of service) into CalPERS retirement. CalPERS vesting can be verified on the My|CalPERS website. Or if the employee has an active appointment with CalPERS

- If the employee is not vested into Cal-PERS or has not employed by a school employer, Board of Governors or the State Dept. of Education within 120 days before the members date of hire to perform service that requires membership with CalPERS, (the employee does not have a choice to elect CalPERS), establish the employee in CalSTRS. For 100% FTE membership is upon hire. For Part Time 50% - 99% establish membership in 2nd pay period from hire.

2) If the employee is vested (5 years) into CalPERS or has an active appointment with CalPERS, take the following steps:

- Provide Form ES 372 Right of Election & "Join CalSTRS? Join CalPERS?" to employee within 10 working days of hire
- Employee has 60 days from date of hire to elect to have the new CalSTRS position reported to CalPERS
- If the employee fails to return the completed Form ES 372 within 60 days of hire date, establish the position to be covered by CalSTRS
- If the employee elects CalPERS on Form ES 372, establish the position to be reportable to CalPERS
- If the employee elects CalSTRS on Form ES 372 establish the position to be reported to CalSTRS

Important Note: No election is required if employee chooses to become a member of CalSTRS but you should still have the employee sign and date a statement that backs up the fact that they were given the option of election

RETIREMENT ISSUES

4) Positions: Certificated Part Time Hourly or Daily or
Certificated Substitutes

Current Retirement Status: Non Member of CalPERS/CalSTRS

➢Provide Form ES 350 Permissive Membership to the employee

1) If the employee declines CalSTRS membership on the Form ES 350 Permissive Membership, monitor time worked for mandatorily qualifying as a CalSTRS member

2) If the employee elects CalSTRS membership on the Form ES 350 Permissive Membership, establish the employee as a CalSTRS member 30 days after the date the employee signs the ES 350 form.

Note: Certificated non-members may elect CalSTRS membership at any time during their employment.

5) Positions: Certificated Part Time Hourly or Daily or
Certificated Substitutes

Current Retirement Status: CalPERS School or *Non*-School Member

➢Provide Form ES 350 Permissive Membership to the employee

1) If the employee elects CalSTRS membership, establish the employee as a CalSTRS member the first day of the pay period following the employee's election.

2) If the employee declines CalSTRS membership, monitor time worked for mandatorily qualifying as a CalSTRS member.

➢If less than 60 days from date of hire has passed prior to mandatorily qualifying for membership**, and** the employee is employed by a school employer, Board of Governors of Community College Districts or State Department of Education **or** has at least 5 years of CalPERS credited service, the employee is eligible for the Form ES 372 Right of Election
➢Provide Form ES 372 Right of Election & "Join CalSTRS? Join CalPERS?" too the employee within 10 working days of qualification
➢Employee has **only the remaining 60 days from date of hire** to elect to have the new CalSTRS position reported to CalPERS
➢If the employee fails to return the completed Form ES 372 within the timeframe, establish the position to be covered by CalSTRS effective the 1st day of the next pay period
➢If the employee elects CalPERS on Form ES 372, establish the position to be covered by CalPERS effective the 1st day of the next pay period

Note: Certificated non-members may elect CalSTRS membership at any time during their employment.

RETIREMENT ISSUES

6) Positions: Certificated Part Time Hourly or Daily or
Certificated Substitutes

Current Retirement Status: CalSTRS Member

Establish the position to be covered by Cal-STRS upon hire

7) Positions: Certificated Part Time Hourly or Daily or
Certificated Substitutes

Current Retirement Status: CalPERS School or *Non-School* Member and
CalSTRS Member

1) Any person who is a member of the Defined Benefit Program of the State Teachers' Retirement Plan employed by a community college district who subsequently is employed by the Board of Governors of the California Community Colleges to perform duties that are subject to membership in a different public retirement system may elect to have that service subject to coverage by the Defined Benefit Program of this plan and excluded from coverage by the other public retirement system.

2) If the employee meets the above listed criteria take the following steps:

- Provide Form ES 372 Right of Election & "Join CalSTRS? Join CalPERS?" to the employee within 10 working days of the hire
- Employee has 60 days from date of hire to elect to have the new CalSTRS position reported to CalPERS
- If the employee fails to return the completed Form ES 372 within 60 days of hire date, establish the position to be covered by CalSTRS
- If the employee elects CalPERS on Form ES 372, establish the position to be covered by CalPERS
- If the employee elects CalSTRS on Form ES 372, establish the position to be covered by CalSTRS

The form must be sent to CalSTRS and CalPERS within 30 days after the employee signed the form

Important Note: No election is required if employee chooses to have position reported to CalSTRS but you should still have the employee sign and date a statement that backs up the fact that they were given the option of election.

RETIREMENT ISSUES

Classified Retirement Scenarios

1) Positions: Classified Full Time or
Classified for 20 Hours or more/week

Current Retirement Status: Non-member of CalPERS/CalSTRS

Establish employee as a CalPERS member upon hire

2) Positions: Classified Full Time or
Classified for 20 Hours or more/week

Current Retirement Status: CalSTRS Member

- Provide Form ES 372 Right of Election & "Join CalSTRS? Join CalPERS?" to the employee within 10 working days of hire
- Employee has 60 days from date of hire to elect to have the new CalPERS position reported to CalSTRS
- If the employee fails to return the completed Form ES 372 within 60 days of hire date, establish the position to be covered by CalPERS
- If the employee elects CalPERS on Form ES 372, establish the position to be covered by CalPERS
- If the employee elects CalSTRS on Form ES 372, establish the position to be reportable to CalSTRS

Important Note: No election is required if employee chooses to have the position reported to CalPERS but you should still have the employee sign and date a statement that backs up the fact that they were given the option of election

3) Positions: Part time classified for less than 20 Hours/week or
Classified Substitutes, Professional Experts, Short Term Employees

Current Retirement Status: Non Member CalPERS/CalSTRS

Once the employee qualifies by working 1000 hours, set up as a CalPERS member effective the 1st of the following month

RETIREMENT ISSUES

4) Positions: Part time classified for less than 20 Hours/week
Classified Substitutes, Professional Experts, Short Term Employees

Current Retirement Status: CalPERS School/ *Non*-School Member

Establish position to be covered by Cal-PERS upon hire

5) Positions: Part time classified for less than 20 Hours/week
Classified Substitutes, Professional Experts, Short Term Employees

Current Retirement Status: CalSTRS Member

1. Monitor for qualifying into CalPERS

2. Once the employee qualifies by working 1000 hours, establish position to be covered by CalPERS effective the 1st of the following month

- Since more than 60 days from date of hire will pass prior to mandatory membership qualifications being satisfied, the employee is not eligible for the Form ES372 Right of Election.

California State Teachers'
Retirement System
Executive Office
PO Box 15275
Sacramento, CA 95851-0275
www.CalSTRS.com

December 27, 2012

TO: All County Superintendents of Schools
District Superintendents of Schools
County Offices of Education
Community College Districts
Charter School Administrators and
All Employing Agencies

FROM: Jack Ehnes
Chief Executive Officer

SUBJECT: Employer Directive 2012-07
California Public Employees' Pension Reform Act of 2013

PURPOSE

This directive notifies employers of changes to Education Code and Government Code sections contained in Chapter 296, Statutes of 2012 (AB 340—Furutani), known as the California Public Employees' Pension Reform Act of 2013, that becomes effective January 1, 2013.

SCOPE

This directive contains information for county superintendents of schools, school districts, charter schools, community college districts, and any agency that employs persons to perform creditable service under the CalSTRS Defined Benefit (DB) and Defined Benefit Supplement (DBS) programs.

DISCUSSION

Chapter 296 applies differently to employees depending on when they first became employed to perform activities creditable to CalSTRS.

CalSTRS 2% at 60: First *hired* to a position to perform activities subject to coverage by the DB Program on or before December 31, 2012. An existing member is also someone who may have refunded, reinstated, retired, started as a nonmember or elected to have their creditable service covered by another retirement plan, including Social Security.

CalSTRS 2% at 62: First *hired* to a position to perform activities subject to coverage by the DB Program on or after January 1, 2013.

ACTION

If you hire a person to perform service that is creditable to the DB Program before January 1, 2013, establish his or her account in the Secure Employer Web site before December 31, 2012. All members with accounts established prior to January 1, 2013 will be under CalSTRS 2% at 60.

Employers will be prohibited from backdating a status date for any CalSTRS 2% at 62 accounts established on or after January 1, 2013.

If a member is defaulted into CalSTRS 2% at 62 in error, please contact your CalSTRS Member Account Services Representative for further instruction.

Compensation Cap
Chapter 296 added section 7522.10 to the Government Code, which establishes a limit on compensation used to calculate benefits for CalSTRS 2% at 62, including compensation credited to the DBS Program. For CalSTRS 2% at 62, the cap on compensation is equal to 120 percent of the 2013 Social Security wage base and will be adjusted annually based on changes to the Consumer Price Index for All Urban Consumers.

Beginning January 1, 2013, the compensation cap for CalSTRS 2% at 62 is $136,440.

ACTION

CalSTRS 2% at 62:

- Report the full compensation earnable and actual compensation earned.
- Do not submit contributions on compensation over the compensation cap.

Edits implemented in the Secure Employer Web site will prevent employers from submitting contributions to the DB Program for CalSTRS 2% at 62 members whose earnings exceed the cap.

Employers may elect to offer a defined contribution plan for the contributions on salary above the cap to CalSTRS 2% at 62 members. However, the employer contribution rate cannot be greater than the 8.25 percent employer contribution rate for the DB Program.

For members under CalSTRS 2% at 62 who earn more than one year of service credit in a school year, contributions for that compensation will continue to be credited to the DBS Program provided that the compensation does not exceed the compensation cap.

Creditable Compensation
Chapter 296 added section 22119.3 to the Education Code and added section 7522.34 to the Government Code. These sections define and limit the types of compensation creditable to the DB and DBS programs for CalSTRS 2% at 62 as follows:

1) Creditable compensation is:

A. The normal monthly rate of pay or base pay of the member;

B. Paid pursuant to a publicly available pay schedule;

C. Paid in cash to all persons in the same class of employees on a full-time basis.

For compensation to be creditable, it must be included in the full-time equivalent or specifically identified on a salary schedule or other publically available document.

2) Creditable compensation paid to CalSTRS 2% at 62 members excludes:

A. An allowance;

B. A bonus;

C. Cash in-lieu of receiving a benefit;

D. Compensation that is payable for a specified number of times;

E. Compensation paid for the purposes of enhancing a benefit.

ACTION

For members under CalSTRS 2% at 62, employers cannot report special compensation creditable to the DBS Program only (account code 71) to CalSTRS. Edits implemented in the Secure Employer Web site will prevent employers from submitting special compensation to the DBS Program only for CalSTRS 2% at 62.

Employers may only report compensation paid to CalSTRS 2% at 62 members that meets the definition of creditable compensation under Education Code section 22119.3 and Government Code section 7522.34. Pay schedules may include individual employment contracts or agreements, traditional step and column salary schedules, or other publicly available documentation that delineates pay for a class of employees. Pay schedules must be publicly available, and employers must provide CalSTRS with copies upon request.

Certain payments, such as master's stipends, are considered creditable compensation as long as they are included in the full-time equivalent or specifically identified on a salary schedule or other publically available document. To report these types of compensation, use the existing contribution code 6 and a new assignment code 72.

Contribution Rates
Section 7522.30 was added to the Government Code by Chapter 296. This section establishes the contribution rate paid by members under CalSTRS 2% at 62 based on the normal cost of pension benefits. At its November meeting, the Teachers' Retirement Board adopted a normal cost of 15.9 percent for pension benefits under CalSTRS 2% at 62, based on analysis by the system's actuary. Based on this action, the contribution rate paid by a CalSTRS 2% at 62 members will be the same 8 percent rate currently set in statute for CalSTRS 2% at 60 members. There also is no change to the 8.25 percent employer contribution rate for compensation paid for any DB Program member.

Education Code section 22909 allows employers to pay all or a portion of the employee contributions, if that payment is made on behalf of all members in the same class of employees. However, Chapter 296 prohibits employers from paying employee contributions for CalSTRS 2% at 62 members, unless the prohibition would impair the obligations of an existing contract. Consequently, if such a contract currently exists, an employer may continue to pay all or a portion of employee contributions until the expiration of that contract, and upon expiration of that contract, may do so only if all members in the class of employees are CalSTRS 2% at 60 members. Employers may, however, continue to "pick-up" their employee's contributions, pursuant to Education Code section 22903, for the purposes of deferring income taxes, as authorized by Internal Revenue Code Section 414(h)(2) and Revenue and Taxation Code Section 17501.

ACTION

Contribution rates for all members, regardless of the benefit structure, and employers remain the same as set forth in Education Code sections 22901, 22950 and 22951. However, member contribution rates for CalSTRS 2% at 62 may change in the future.

Do not pay any portion of the employee contributions for CalSTRS 2% at 62 members unless an existing contract provides for such payment. Continue to pay all or a portion of the employee contributions for CalSTRS 2% at 60 members upon the expiration of that contract or a future contract only if all members in the same class of employees are CalSTRS 2% at 60 members.

Employer Election to Offer One-Year Final Compensation
Currently, Education Code section 22135 gives districts the ability to negotiate with employee organizations to provide one-year final compensation for all classroom teachers, as defined, who meet criteria specified in that section. Under Chapter 296, pursuant to added Government Code section 7522.32, CalSTRS 2% at 62 members' final compensation may only be averaged over at least three school years. Consequently, districts may still negotiate with employee organizations to provide one-year final compensation for CalSTRS 2% at 60 members who are classroom teachers only if all of their classroom teachers in the DB Program who meet the criteria specified in section 22135 are CalSTRS 2% at 60 members.

ACTION

Employers can continue to negotiate with employee organizations to provide one-year final compensation only if all of their classroom teachers in the DB Program who meet the criteria specified in section 22135 are CalSTRS 2% at 60 members.

Members Convicted of a Felony

Chapter 296 adds Government Code sections 7522.72 and 7522.74, which state if any member, regardless of their benefit structure, is convicted of committing a felony in the course of his or her official duties, any benefits that member accrued after committing the felony will be forfeited. Any benefits the member accrued prior to committing the felony will remain intact. Any contributions made by the member to CalSTRS after the date the felony was committed will be returned, without interest.

ACTION

A member convicted of a felony in the course of his or her official duties and the prosecuting agency are required to notify that member's employer within 60 days of the conviction.

The member and the employer are then required to notify CalSTRS within 90 days of the conviction. At a later date, we will provide more information regarding the process to notify CalSTRS of such felony convictions. In the meantime, if you become aware of such a conviction, please contact CalSTRS Legal Office by email at LegalServices@CalSTRS.com or by mail at the following address:

CalSTRS-Legal Services
PO Box 15275, MS #3
Sacramento, CA 95851

Postretirement Employment

Chapter 296 amends Education Code sections 24214 and 24214.5, which affect employers' ability to hire retired teachers and administrators to fill vacancies, depending on when a member retired.

Existing restrictions apply to retirees and members who retire on or before December 31, 2012. New restrictions apply to members who retire on or after January 1, 2013.

CalSTRS will publish a separate employer directive regarding postretirement work, exemptions and earnings limits.

Other Provisions Affecting Members

Nonqualified Service Credit
Chapter 296 adds Government Code section 7522.46, which prohibits any member from purchasing nonqualified service credit, also known as airtime, after December 31, 2012. In order for a member to purchase nonqualified service credit, he or she must be vested, and CalSTRS must receive the appropriate CalSTRS form by 5:00 p.m. on December 31, 2012.

Retirement Age and Career Factor
Chapter 296 adds Education Code sections 24202.6, 24202.7 and 24202.8, which make changes to the retirement age for CalSTRS 2% at 62. The normal retirement age for these members is 62 with a 2 percent age factor. The maximum age factor is 2.4 percent at 65 and the minimum age a CalSTRS 2% at 62 member can retire is age 55 with 5 years of service. Additionally, the career factor is eliminated for these members.

Replacement Benefits Program
Chapter 296 adds Government Code section 7522.43, which prohibits CalSTRS 2% at 62 members from receiving any benefits above the federal limit, known as the Replacement Benefits Program.

Retroactive Benefit Increases
Government Code section 7522.44 was added by Chapter 296, which stipulates future benefit enhancements for all members will only apply to service performed on or after the operative date of the improvement.

No employer action is needed for these other provisions affecting members.

If you have any questions, please contact your CalSTRS Member Account Services Representative.

CALSTRS
HOW WILL YOU SPEND YOUR FUTURE?

Public Employees' Pension Reform Act of 2013

Frequently Asked Questions

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Retirement Formula Designation

Q1 How do employers know which retirement formula applies to a member?

A1 An indicator is located in REAP that displays retirement formula information per member. In addition, a field on the Match File response file displays the retirement formula information per member.

Q2 If a non-member account was established prior to January 1, 2013 but the employee did not work prior to January 1, 2013, what is his or her retirement formula?

A2 Their retirement formula would be 2% at 60. Any individual with an account prior to January 1, 2013, regardless of membership status or service performed, will have the 2% at 60 retirement formula. Per AB 340, only employees hired to perform creditable service prior to January 1, 2013 are entitled to the 2% at 60 retirement formula.

Q3 If an account was established prior to January 1, 2013 but an employer did not report contribution lines until after January 1, 2013, what formula will the member default into?

A3 This account defaults into the 2% at 60 formula, as long as the transaction was performed prior to January 1, 2013. The retirement formula is set based on the transaction date (the date you perform the REAP or MR87 transaction) not the effective date you set for the account. Reporting contribution lines does not set or change the retirement formula.

Q4 Did employers need to submit reporting lines prior to January 1, 2013 to establish a member with a 2% at 60 retirement formula?

A4 No, if you established an account (member or nonmember) using REAP or the MR87 process prior to January 1, 2013, the account defaulted into the 2% at 60 formula. The retirement formula is set based on the transaction date (the date you perform the REAP or MR87 transaction) not the effective date you set for the account. This is because any employee first hired to perform creditable service on or after January 1, 2013 is subject to the 2% at 62 formula.

Q5 If an account was established on or after January 1, 2013 but the member worked prior to January 1, 2013, can the effective date on the account be backdated prior to January 1, 2013?

A5 Yes, but the effective date cannot be backdated prior to January 1, 2013 through REAP or the MR87 process. If an account is established on or after January 1, 2013 but the member worked prior to January 1, 2013 and this is preventing the employer from submitting their F496 report, the employer must contact their employer services representative to correct the retirement formula and change the effective date on the account.

Q6 If someone was offered employment in December 2012 but did not work until January 2013 which retirement formula will they default into?

A6 If they were first hired to perform creditable service prior to January 1, 2013 they are entitled to the 2% at 60 retirement formula per the Public Employees' Pension Reform Act of 2013.

Q7 If a person is a CalSTRS member prior to January 1, 2013, refunds and then takes a position on or after January 1, 2013, which retirement formula would apply?

A7 The 2% at 60 retirement formula applies in this case. Anyone hired to perform creditable service prior to January 1, 2013 is a CalSTRS 2% at 60 member, regardless of prior refunds.

Q8 If a person is hired to perform creditable service prior to January 1, 2013, elects CalPERS, terminates the position and is later hired to perform creditable service on or after January 1, 2013 and elects CalSTRS, which retirement formula would apply?

A8 They are entitled to the 2% at 60 retirement formula. Anyone hired to perform creditable service prior to January 1, 2013 is a CalSTRS 2% at 60 member, even if they chose to take that creditable service to CalPERS.

Q9 What documentation does a member need to provide to appeal their retirement formula designation?

A9 CalSTRS requires documentation that substantiates the hire date to perform creditable service in order to change the retirement formula.

Q10 How long does it take to resolve an appeal of a member's retirement formula?

A10 The retirement formula appeal process will quickly and efficiently resolve retirement formula discrepancies. For more information about the member's right to appeal, please refer to the CalSTRS Member Handbook.

Q11 Whose responsibility is it to prove the hire date if a member's retirement formula is incorrect?

A11 The member is ultimately responsible for providing verification of their hire date. Members can contact CalSTRS at 1-800-228-5453 to initiate an appeal of their retirement formula. In addition, during the first few months following January 1, 2013, CalSTRS anticipates that some members may have been established in error. In these cases, the employer can contact their employer services representative to correct the retirement formula and change the effective date on the account.

Equal Sharing of Pension Costs

Q1 Will changes to contribution rates affect all members (CalSTRS 2% at 60 and CalSTRS 2% at 62)?

A1 No, if contribution rates change under the Public Employees' Pension Reform Act of 2013, it will not affect all members; it will only affect CalSTRS 2% at 62 members. Under the Public Employees' Pension Reform Act of 2013, employees hired to perform creditable service on or after January 1, 2013 (CalSTRS 2% at 62 members) are required to pay 50% of the normal cost of pension benefits.

The member contribution rate remains 8 percent for the 2012-13 Fiscal Year for both CalSTRS 2% at 60 and CalSTRS 2% at 62 members. However, the member contribution rate for CalSTRS 2% at 62 members may change in the future if the normal cost of pension benefits increases or decreases by more than one percent. For CalSTRS 2% at 60 members, the contribution rate is set in statute and can only change by legislative action.

Creditable Compensation, Bonuses and Stipends

Q1 Can a separate pay schedule be created for CalSTRS 2% at 60 members and CalSTRS 2% at 62 members?

A1 No, the retirement formula change does not create a separate class of employees. The same salary schedule must apply to the entire class regardless of retirement formula used.

Q2 Are step increases considered normal monthly pay or base pay?

A2 Yes, step increases are considered normal monthly pay or base pay.

Q3 As of January 1, 2013, is all special compensation non-creditable for CalSTRS 2% at 62 members?

A3 No, not all special compensation is non-creditable for CalSTRS 2% at 62 members. Certain special compensation is still creditable for CalSTRS 2% at 62 members. In February 2013, CalSTRS will implement assignment code 72 to identify additional compensation for CalSTRS 2% at 62 members. If the compensation is not part of the base pay, this compensation must be reported using a contribution code 6 and assignment code 72. Refer to Employer Directive 2012-07 for more information regarding special compensation for CalSTRS 2% at 62 members.

Q4 If a stipend or other bonus is listed on the salary schedule is this reportable to CalSTRS?

A4 It depends. Compensation that is listed on a publicly available salary schedule that meets the definition of creditable can be reported to CalSTRS. Under the Public Employees' Pension Reform Act of 2013, however, bonuses are specifically not creditable. In February 2013, CalSTRS will implement assignment code 72 to identify additional compensation for CalSTRS 2% at 62 members. If the compensation is not part of the base pay, this compensation must be reported using a contribution code 6 and assignment code 72. Refer to Employer Directive 2012-07 for more information regarding special compensation for 2% at 62 members.

Q5 What special compensation can be reported with assignment code 72?

A5 Certain payments, such as master's stipends, are considered creditable compensation as long as they are included in the full-time equivalent or specifically identified on a salary schedule or other publically available document. Refer to Employer Directive 2012-07 for more information regarding special compensation for CalSTRS 2% at 62 members.

Q6 Are master's degree stipends reported using contribution code 6 for CalSTRS 2% at 62 members?

A6 Yes, as long as the contribution code 6 line is reported with assignment code 72. In February 2013, CalSTRS will implement assignment code 72 to identify additional compensation for CalSTRS 2% at 62 members. If the compensation is not part of the base pay, this compensation must be reported using a contribution code 6 and assignment code 72. Refer to Employer Directive 2012-07 for more information regarding special compensation for 2% at 62 members.

Q7 Is assignment code 72 valid for both Cash Balance and Defined Benefit?

A7 Yes, special compensation that can be reported for CalSTRS 2% at 62 members applies to both Cash Balance and Defined Benefit.

Q8 Are there edits in the Secure Employer Website that ensure correct assignment codes are used for CalSTRS 2% at 62 members?

A8 Yes, business rule B114 and B115 ensure assignment code 72 is reported for CalSTRS 2% at 62 members only.

Q9 When reporting special compensation for 2% at 62 members will there be an edit in the Secure Employer Website that monitors the total amount of compensation reported?

A9 Yes, an edit will be implemented that monitors the total amount of special compensation reported for CalSTRS 2% at 62 members. Since special compensation is limited for CalSTRS 2% at 62 members, the threshold will be set much lower than the current $15,000 limit set for CalSTRS 2% at 60 members.

Q10 Can employers add a bonus or stipend, that currently is not creditable to CalSTRS for the CalSTRS 2% at 62 members, to the salary schedule and make it part of the base pay?

A10 Yes, you can add a stipend or a bonus to a salary schedule to make it part of the base pay. The Public Employees' Pension Reform Act of 2013 states that the normal monthly pay or base pay is considered creditable to CalSTRS. If a bonus or stipend is added to the base pay it would be reportable to CalSTRS. However, a salary schedule change of this nature must apply to the entire class of employees. You cannot create a separate salary schedule for CalSTRS 2% at 62 members.

Cap on Compensation

Q1 If a member reaches the cap, is the employer required to pay contributions over the cap to Social Security and/or establish a separate Defined Benefit (DB) plan?

A1 No, CalSTRS members do not pay into Social Security, therefore, employers are not required to pay contributions over the cap to Social Security. Nor can employers establish a separate DB plan. However, the Public Employees' Pension Reform Act of 2013 does allow, but does not require, employers to contribute to a defined contribution plan for compensation above the cap. Beginning January 1, 2013, the cap on compensation for CalSTRS 2% at 62 members is $136,440.

If an agreement exists between an employer and its employees that a retirement supplement must be provided on compensation above a cap, CalSTRS is not aware of the details and cannot comment on how it should be implemented, except that per the Public Employees' Pension

Reform Act of 2013, any retirement supplement above the cap must be a defined contribution plan and the rate of employer contribution to such a plan cannot exceed 8.25 percent.

Q2 Is the cap on compensation based on a calendar year or fiscal year?

A2 Per the Public Employees' Pension Reform Act of 2013, the cap on compensation is based on a calendar year. However, CalSTRS is seeking legislative changes to base the cap on a fiscal year.

Q3 Does the compensation cap apply to Cash Balance participants?

A3 No, the Public Employees' Pension Reform Act of 2013 does not apply to Cash Balance. However, CalSTRS is pursuing legislation to apply the Public Employees' Pension Reform Act of 2013 requirements to the Cash Balance Benefit Program.

Q4 Does CalSTRS or the employer monitor the cap on compensation?

A4 Ideally, each employer should monitor the compensation reported to CalSTRS to prevent reporting problems. However, CalSTRS will be implementing a running balance, visible in REAP, of compensation reported to CalSTRS. This display can be used to monitor compensation reported to CalSTRS per member.

In addition, Defined Benefit business rules will evaluate the amount of contributions reported and prevent contributions from being submitted in excess of the compensation cap. The business rules allow for no contributions for members that meet the compensation cap.

Q5 If a member works for multiple districts and reaches the compensation cap, how will CalSTRS determine which district to accept contributions from?

A5 For members working in multiple districts, reporting will be accepted based on the transmittal date of the F496 report. Once CalSTRS accepts reporting from one district which causes the member to meet the compensation cap, contributions will not be accepted for any subsequent reporting regardless of district.

Q6 If an employee works for multiple districts in the same county and the compensation cap is met based on the cumulative total of two or more contribution lines on the same F496 file how will the system treat each individual line?

A6 CalSTRS is determining how the system will treat this scenario. This question will be updated when a solution is determined.

Q7 For subsequent year adjustment reporting for 2% at 62 members, will the compensation apply to the compensation cap for the fiscal year represented on the contribution lines or the fiscal year in which the contribution lines were received by CalSTRS?

A7 Compensation will apply to the fiscal year represented on the contribution lines. For example, if a contribution line is reported to CalSTRS in September 2014 (fiscal year 2014/2015) but the service period is for June 2014 (fiscal year 2013/2014), the compensation would apply to the cap for fiscal year 2013/2014.

Three-year Final Compensation

Q1 Does the three-year final compensation provision of the Public Employees' Pension Reform Act of 2013 affect CalSTRS 2% at 60 members?

A1 No, the three-year final compensation provision of the Public Employees' Pension Reform Act of 2013 does not affect CalSTRS 2% at 60 members. The three-year final compensation provisions only apply to members hired on or after January 1, 2013, CalSTRS 2% at 62 members. CalSTRS 2% at 60 members are still eligible for one-year and three-year final compensation.

Q2 Does the three-year final compensation provision affect CalSTRS 2% at 62 members that are entitled to employer paid one-year final comp per their employment agreement?

A2 Yes, the three-year final compensation provision supersedes any existing employment agreement. CalSTRS 2% at 62 members are subject to three-year final compensation regardless of their employment agreement.

Post Retirement Earnings Limitation

Q1 Does the 180-day post retirement earnings provision apply to members who retire before January 1, 2013?

A1 Yes, members who retire prior to January 1, 2013 are subject to the 180-day zero-dollar earnings limitation if they are under normal retirement age. Education Code section 24214.5 requires any retiree who retires prior to January 1, 2013, and who is under normal retirement age (age 60), to wait 180-days from the date of their retirement, or turn age 60, before returning to perform creditable service in order to avoid a reduction in his or her benefit. If a retiree who

retires prior to January 1, 2013 is at or above age 60, he or she is not subject to the 180-day break from service.

Q2 What exemptions to the 180-day zero dollar earnings limitation apply to 2% at 60 members versus 2% at 62 members?

A2 For all members who retire after January 1, 2013 and who are at or above normal retirement age (age 60 for CalSTRS 2% at 60 members, and age 62 for CalSTRS 2% at 62 members), an exemption can be requested if all of the following conditions are met:

- The appointment is necessary to fill a critically needed position
- The governing body of the employer approves the appointment through a resolution adopted at a public meeting.
- The retired member did not receive any financial inducement to retire.
- The retired member's termination of service was not the cause of the need to acquire the services of the member.
- The exemption request and documentation required are received by CalSTRS prior to any service being performed.

If approved, this exemption only applies to the zero-dollar earnings limit.

Q3 What exemptions to the annual postretirement earnings limitation apply to 2% at 60 members versus 2% at 62 members?

A3 For the 2012-13 and 2013-14 school years only, there is an exemption for all retired members who are at or above normal retirement age (age 60 for CalSTRS 2% at 60 members, and age 62 for CalSTRS 2% at 62 members) and who are appointed by a county superintendent of schools, the California Community Colleges Board of Governors, the State Board of Education or the State Superintendent of Public Instruction to specified positions to assist schools that are experiencing specific academic or fiscal distress. CalSTRS must receive the exemption request and required documentation substantiating a member's eligibility before the member begins working. The member is not eligible for this exemption if he or she has received a retirement incentive in the previous six months.

If approved, this exemption only applies to the annual postretirement earnings limit.

CalSTRS System Changes

Q1 When will CalSTRS implement the Match File changes (the indicator for CalSTRS 2% at 60 and CalSTRS 2% at 62)?

A1 The indicator on the Match file was added on January 1, 2013. The response field length still remains 30 characters long.

Q2 Can employers submit contribution lines with service periods prior to the effective date on a CalSTRS account?

A2 No, member contribution lines cannot precede the effective date on the CalSTRS account. These lines will receive a correction required error in SEW. Nonmember contribution lines also cannot precede the effective date on the CalSTRS account

Q3 What other items in the Public Employees' Pension Reform Act of 2013 is CalSTRS seeking clarification on?

A3 CalSTRS is pursuing numerous points of legislation to clarify and conform the Teachers' Retirement Law to Pension Reform. CalSTRS is pursuing legislation on:

- Allowing for CalSTRS members who were members of a concurrent retirement system prior to January 1, 2013, to be designated as CalSTRS 2% at 60 members if they performed service under that retirement system in the six months prior to performing CalSTRS creditable service;
- Changing the compensation cap to be based on a fiscal year instead of calendar year;
- Applying the Public Employees' Pension Reform Act of 2013 requirements to the Cash Balance Benefit Program;
- Allowing for bargained for employer-paid member contributions for 2% at 60 members;
- Allowing for bargained for one-year final compensation for 2% at 60 members;
- Clarifying the limits on types of creditable compensation.

CalSTRS will notify employers when updates occur that impact employer reporting. Regularly check the announcements on the SEW home page for updates.

Q4 Will there be a new assignment code to differentiate between 2% at 60 and 2% at 62 members?

A4 No, not at this time. CalSTRS is researching this requirement and may consider this for a future release. CalSTRS will update this FAQ question if this answer changes.

CALSTRS
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Employer Information Circular

Volume 28; Issue 1 **August 29, 2012**

Positions Not Eligible for Creditable Service

The purpose of this circular is to provide guidance for employers regarding the types of positions that are not eligible for CalSTRS.

Creditable service for CalSTRS is defined in section 22119.5 of the Teachers' Retirement Law. It states in part:

> "Creditable service" means any of the following activities performed for an employer in a position requiring a credential, certificate, or permit pursuant to this code or under the appropriate minimum standards adopted by the Board of Governors of the California Community Colleges or under the provisions of an approved charter for the operation of a charter school for which the employer is eligible to receive state apportionment or pursuant to a contract between a community college district and the United States Department of Defense to provide vocational.

In order for a position to be creditable to CalSTRS the position must be an academic position performing duties involved in the instruction, curriculum or material development, school health professionals, counselors, librarians or superintendents. A position that is responsible for supervising such positions is deemed to be an academic position therefore creditable to CalSTRS. **The specific title given the employee, whether it is, for example, director, dean, or chief, does not determine whether the service is creditable to CalSTRS. Rather, it is the nature of the duties performed by the employee that will determine whether the service is creditable to CalSTRS.**

Positions that are not deemed as academic are considered classified and subject to coverage by a different public retirement plan.

Examples of positions that are not reportable to CalSTRS are:

- Chief of Police
- Director of Buildings, Grounds, and Maintenance
- Director of Human Resources
- Chief Information Technology Officer
- Director of Payroll Services
- Chief Financial Officer

(Continued on next page . . .)

These positions are deemed non-academic and are not subject to coverage by CalSTRS. However in some situations, if the employee is also a CalSTRS member based upon previous employment, the employee may be eligible to elect CalSTRS coverage. For more information, see “Employer Information Circular, Volume 25, Issue 11”.

If you have any questions regarding this circular, please contact your CalSTRS Member Account Services analyst.

CALSTRS
HOW WILL YOU SPEND YOUR FUTURE?

Employer Information Circular

Volume 30; Issue 5 **December 10, 2014**

Creditable Compensation Regulations Effective January 1, 2015

The purpose of this circular is to alert employers that on January 1, 2015, CalSTRS Creditable Compensation Regulations, Sections 27200 through 27602 of Chapter 2, Division 3, Title 5 of the California Code of Regulations become effective. The regulations clarify Education Code sections 22112.5, 22119.2 and 22905 and apply to CalSTRS 2% at 60 members.

Class of Employees

Education Code section 22112.5 defines class of employees. It states, in part, that a "class of employees" means a number of employees considered as a group because they are employed to perform similar duties, are employed in the same type of program, or share other similarities related to the nature of the work being performed.

Section 27300 of the regulations clarifies similar duties and type of program. Job duties grouped within each paragraph outlined in Education Code section 22119.5(a)(1)-(9) and (b) are similar. A program is any educational program established under state or federal law.

CalSTRS did not clarify other similarities related to the nature of the work in the regulations. The regulations do not affect CalSTRS' ability to override an employer's determination of a class of employees.

In addition, Education Code section 22112.5 states a class of employees may be comprised of one person if no other person employed by the employer performs similar duties, is employed in the same type of program, or shares other similarities related to the nature of the work being performed and that same class is in common use among other employers. Section 27300 of the regulations clarifies common use means the same class is in use by at least two other employers throughout the state.

Section 27301 of the regulations prohibits the establishment of a class of employees based on any of the following:

- Retirement benefit formula or retirement program;
- Minimum or maximum threshold for age or service credit;
- Characterization or structure of compensation;
- Option or requirement to work a longer or shorter day, or more or fewer days per year, performing similar job duties, except as provided in the Education Code section 22138.5 for community college instructors; or
- Performing only outgrowth activities.

Creditable Compensation

Education Code section 22119.2 defines creditable compensation. The law states remuneration paid in cash by an employer to all persons in the same class of employees for performing creditable service in that position is creditable compensation. The law also states that both of the following are creditable:

- Salary paid in accordance with a publicly available written contractual agreement; and
- Remuneration paid in addition to salary provided that it is paid to everyone in the same class of employees and in the same amount or percentage.

Section 27400 of the regulations clarifies what compensation is considered salary. To be considered salary, the compensation must be all of the following:

- Paid in cash for the performance of creditable service;
- Explicitly characterized as salary on a contract, salary schedule or employment agreement;
- Used as the basis for future pay increases; and
- Paid without a requirement for proof of expenditure.

If compensation is paid for any outgrowth activities identified in Education Code section 22119.5(a)(6), it does not have to be the basis for future pay increases to still be considered salary.

Additionally, since salary is compensation for the performance of creditable service, the employer must establish a compensation earnable for all assignments for which an employee will earn salary.

If any compensation is restructured as salary, and it meets all four characteristics of salary outlined above, CalSTRS considers that compensation to be salary on the effective date of the restructure regardless of how the compensation was previously paid or characterized.

Section 27401 of the regulations clarifies compensation that is considered remuneration in addition to salary. The compensation must be paid in cash in accordance with a publicly available written contractual agreement, and the compensation is not associated with the performance of additional service. Remuneration in addition to salary is compensation that either meets a qualification or requirement on the list below *or* is paid contingent upon the availability of funds.

- Possession or an attainment of a certificate, license, special credential or advanced degree;
- Career or service longevity;
- Hiring, transfer or retirement;
- Employment in a position that is hazardous or difficult to staff;
- Employment in an assignment in which the number of students enrolled exceeds the contractual amount; or
- Achievement of a performance benchmark.

Compensation that meets the definition of remuneration in addition to salary is creditable to CalSTRS and reportable as special compensation.

Compensation Paid a Limited Number of Times

Education Code section 22905 requires contributions on certain types of compensation be credited to the Defined Benefit Supplement Program. Section 27602 of the regulations clarifies contributions on compensation that is not ongoing and is contingent upon either the availability of funds or meeting specified qualifications or requirements are creditable to the Defined Benefit Supplement Program only.

Noncreditable Compensation

Education Code section 22119.2(c) defines compensation that is not creditable. Sections 27501 and 27502 of the regulations define fringe benefit and an expense paid or reimbursed by an employer. Below are types of compensation that are noncreditable compensation:

- Automobile allowances;
- Cash in lieu of benefits; and
- Housing allowances.

Additionally, Section 27500 of the regulations states that compensation that is contingent on the purchase of any items listed in Education Code section 22119.2(a)(5) is deemed to be covered by the employer, and therefore, it is noncreditable compensation. If an employer offers compensation for the purchase of a Tax Sheltered Annuity, it would be deemed covered by the employer and considered noncreditable compensation.

Appropriate Crediting of Contributions

Education Code section 22119.2(f) provides CalSTRS with the authority to determine whether compensation is consistent throughout a member's career, consistent amongst an entire class of employees or consistent for a position. If CalSTRS determines compensation is inconsistent, it will determine which portion of the compensation is creditable to the Defined Benefit Program and the Defined Benefit Supplement Program.

Section 27600 states that seven years, ending with the last day used to calculate final compensation, is generally the period of time that CalSTRS will review to determine if an increase in compensation is consistent. For a member with three-year consecutive or one-year final compensation, this means that CalSTRS will review his or her compensation for the year he or she retired and the immediately preceding six years.

When CalSTRS determines an increase in compensation is inconsistent, the employer or member may rebut the determination by providing substantiating documentation that the increase was attributable to one or more of the specific circumstances listed in Section 27600 of the regulations:

- A restructure of compensation that is a permanent change.
- A salary deferral due to a reduction in school funds.
- A commensurate percentage increase in compensation earnable for the majority of members employed by the same employer.
- A change in duties required of the employee that is incorporated in the first contract for the immediate successor to the position.
- An increase in responsibility of the employee that is incorporated in the first contract for the immediate successor to the position.
- Attainment of an educational or performance benchmark.
- An increase that establishes pay parity.
- A commensurate compensation earnable for the immediate successor or predecessor.
- More education or experience than the immediate predecessor.
- An increase in compensation that is required to recruit for a position which is directly responding to a specific time-bound financial crisis, as defined in the regulations.

For example, if CalSTRS inquires about an unusual increase in pay prior to an individual's retirement and the employer can demonstrate that the job responsibilities for that position were expanded because of a permanent change in the employer's business practice that was continued for the next person to hold that position, that would be viewed by CalSTRS as a consistent pay increase.

In another example, if the employer provides documentation demonstrating that an individual was promoted to a new position and that the predecessor to that position earned a similar amount, that would generally be viewed as consistent, unless the employer shows a pattern of promoting individuals into this position just prior to retirement. If CalSTRS determines that there is a pattern of assignment of duties or responsibilities by an employer to employees during the final compensation period, the additional compensation for those duties is presumed to be inconsistent.

The contributions on compensation increases presumed to be inconsistent will be allocated to the Defined Benefit Supplement Program. Compensation that does not exceed150 percent of the median increase in compensation earnable earned by a broader population, as defined in the regulations, will be creditable to the Defined Benefit Program. Any compensation in excess of that amount will be allocated to the Defined Benefit Supplement Program.

Additionally, a restructure of compensation that does not meet the criteria of being permanent is presumed to be inconsistent, and the contributions on the restructured compensation will be credited to the Defined Benefit Supplement Program, even if the increase in compensation is less than 150 percent of the median increase of the applicable population.

CalSTRS will presume a restructure of compensation to be inconsistent if it is:

- Negotiated after January 1, 2016, and is outside of the employer's standard bargaining or employment contract timeframes; or
- Implemented for a class of one and is not negotiated in the first contract for the immediate successor in that position.

For complete information, please refer to the Creditable Compensation Regulations at calstrs.com/general-information/creditable-compensation.

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February 25, 2016

TO: All County Superintendents of Schools
District Superintendents of Schools
County Offices of Education and
Charter School Administrators

FROM: Jack Ehnes
Chief Executive Officer

SUBJECT: Employer Directive 2016-04
Supersedes Employer Information Circular Volume 28, Issue 1 (EIC12-1)
Reorganization and Clarification of Definition of "Creditable Service," Education Code Sections 22119.5 and 26113.

PURPOSE

This directive notifies employers of changes to Education Code sections 22119.5 and 26113, the definition of "creditable service," made by Chapter 782, Statutes of 2015 (Assembly Bill 963), that became effective January 1, 2016.

SCOPE

This directive contains information for county superintendents of schools, school districts, charter schools, community college districts and any agency that employs persons to perform creditable service under the CalSTRS Defined Benefit (DB), Defined Benefit Supplement (DBS) and Cash Balance (CB) Benefit programs.

DISCUSSION

Chapter 782, Statutes of 2015, reorganizes Education Code sections 22119.5 and 26113, the definitions of "creditable service" for the DB and CB Benefit programs respectively. The amendments clarify the certification qualifications and minimum standards requirements that need to be met, as well as activities that are considered creditable service.

Credentialing Requirements

Chapter 782 makes more specific the certification qualifications and minimum standards requirements that must be met in order for the activities performed to be creditable to CalSTRS.

Education Code sections 22119.5(a) and 26113(a) now specify that in order for service to be creditable to CalSTRS, members and participants must perform creditable activities for one of the following employers as specified:

1. A prekindergarten through grade 12 employer, including the state, when the service is performed in a position requiring certification qualifications as designated in regulations adopted by the Commission on Teacher Credentialing (CTC) pursuant to Education Code section 44001.

2. A community college employer when the service is performed by a faculty member (defined in Education Code section 87003) in an academic position (defined in Education Code section 87001(b)), or when it is performed by an educational administrator (defined in Education Code section 87002(b)), subject to the appropriate minimum standards adopted by the Board of Governors of the California Community Colleges, or pursuant to a contract between a community college district and the US Department of Defense to provide vocational training.

3. A charter school employer under the provisions of an approved charter for the operation of a charter school which is eligible to receive state apportionment.

Creditable Activities

Chapter 782 also updates and clarifies the types of activities that are considered creditable. The notable amendments to the activities that are creditable if performed by an individual who meets the requirements outlined in Education Code sections 22119.5(a) and 26113(a) include (amendments are *italicized*):

- The work of *employees* who plan courses of study to be used in California public schools, or research connected with the evaluation or efficiency of the instructional program.

- The selection, collection, preparation, classification, demonstration, or evaluation of instructional material of any course of study for use in the development of the instructional program in California public schools, or other services related to *California public* school curriculum.

- The examination, selection, in-service training, *mentoring*, or assignment of teachers, principals, or other similar personnel involved in the instructional program.

- The work of nurses, physicians, speech therapists, psychologists, audiometrists, audiologists, and other *California public* school health professionals.

- Services as a *California public* school librarian.

- *Activities connected with the enforcement of the laws relating to compulsory education, coordination of child welfare activities involving the school and the home, and the school adjustment of pupils.*

Creditable service also includes the activities listed in Education Codes sections 22119.5(b) and 26113(b) when they are performed for an employer by (amendments are *italicized*):

- Superintendents of California public schools, *and presidents and chancellors of community college employers.*

- *Consulting teachers employed by an employer to participate in the California Peer Assistance and Review Program for Teachers pursuant to Article 4.5 (commencing with Section 44500) of Chapter 3 of Part 25 of Division 3 or Title 2.*

Outgrowth Activities

Chapter 782 also amends Education Code sections 22119.5 and 26113 to require that outgrowth activities are only creditable when they are performed for the same employer for which the member is performing any of the other creditable activities.

ACTION

Report service to CalSTRS that meets the definition of "creditable service" as described in Education Code section 22119.5 or 26113. The title of the position has no bearing on the creditability of the service, but the duties of the position should be in accordance with Education Code section 22119.5 or 26113.

If you are unsure to which retirement system you should report the service of some of your employees, please contact the Member Account Services Training and Teachers' Retirement Law team using the information below, and we will work with you to determine how the service should be reported.

This employer directive does not take precedence over the law. To view Chapter 782, Statutes of 2015 (Assembly Bill 963), in its entirety, please go to http://leginfo.legislature.ca.gov.

If you have any questions regarding this employer directive, please contact the CalSTRS Member Account Services Training and Teachers' Retirement Law team by emailing MASTrainingandTRL@calstrs.com or calling toll free 844-679-7833.

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October 12, 2017

TO: All County Superintendents of Schools
District Superintendents of Schools
Community College Districts
Charter Schools and
Other Employing Agencies

FROM: Jack Ehnes
EXECUTIVE OFFICE

SUBJECT: Employer Directive 2017-05
October 1, 2017, Amendments to the Creditable Compensation Regulations

PURPOSE:

This directive provides information regarding the October 1, 2017, amendments to the Creditable Compensation Regulations (Chapter 2 of Division 3, Title 5 of the California Code of Regulations).

SCOPE:

This directive contains information for county superintendents of schools, school districts, charter schools, community college districts and any agency that employs persons to perform creditable service under the CalSTRS Defined Benefit (DB), Defined Benefit Supplement (DBS) and Cash Balance (CB) Benefit programs.

DISCUSSION:

Effective January 1, 2015, the Creditable Compensation Regulations clarify and make specific provisions related to class of employees, creditable compensation and the appropriate crediting of contributions for CalSTRS 2% at 60 members. The regulations were amended on October 1, 2017, to provide additional clarification. Refer to Employer Information Circular Volume 30, Issue 5, for more comprehensive information regarding the regulations in their entirety.

Programs Established Pursuant to a Local Control and Accountability Plan as a Basis for Establishing a Class of Employees

Chapter 47, Statutes of 2013 (AB 97–Committee on Budget), revised the public financing of educational programs by establishing the Local Control Funding Formula. Most of the categorical education programs previously established in state law were eliminated; instead, local educational agencies are now authorized under state law to create individually tailored plans to

expend the funds previously allocated for those categorical education programs. The vehicle for establishing a local program is a Local Control and Accountability Plan (LCAP). Although LCAPs are established pursuant to state law, the specific programs established in an LCAP are local, not state, programs.

Section 27300 of the Creditable Compensation Regulations clarifies the basis upon which an employer can create a class of employees. Education Code section 22112.5 defines a "class of employees" as a number of employees considered as a group because they are employed to perform similar duties, are employed in the same type of program or share other similarities related to the nature of the work being performed. The term "same type of program" is not defined in the statute, but it is specified through regulations in Section 27300 to include a state or federal program established in law.

Section 27300 was amended to clarify that programs established in an LCAP meet the criteria upon which an employer can establish a class of employees.

Compensation Paid for Mentoring and Similar Duties as Salary
Section 27400 of the Creditable Compensation Regulations clarifies the use of the term "salary" as it relates to creditable compensation. In order for compensation to be considered salary, it must be paid in cash by an employer, paid for the performance of creditable service, explicitly characterized as salary in a written agreement, and used for the basis of future pay increases. However, compensation paid to execute duties that are "related to, and an outgrowth of, the instructional and guidance program of the school" need not be the basis of future pay increases because these types of assignments are often not paid according to a salary schedule and do not always reflect year-over-year increases or decreases that mirror the salary schedule.

Section 27400 was amended to clarify that compensation paid "to perform creditable service activities that are related to the examination, selection, in-service training, mentoring, or assignment of teachers, principals, or other similar personnel involved in the instructional program" is another type of pay that is reportable as salary, but that does not need to be explicitly described as salary on the written agreement nor be the basis of future pay increases. As with any compensation deemed salary, the employer must establish a compensation earnable for these activities.

Class Size Overload as Creditable Compensation
Section 27401 of the Creditable Compensation Regulations defines "remuneration that is paid in addition to salary" as it relates to creditable compensation. "Remuneration that is paid in addition to salary" is defined, in part, as compensation that is not associated with the performance of additional service. Section 27401 includes a short list of the types of pay that may be creditable as remuneration in addition to salary, which includes "employment in an assignment in which the number of students enrolled exceeds the contractual amount." The language was amended to reference the "contractual class size maximum" for improved readability.

It is common, particularly among community college districts, for a written agreement to define "full time" in terms of a workload-based unit of measurement that is representative of full-time

hours worked. A full-time employee must achieve a given load factor to meet the full-time requirement. Based on this type of agreement, an instructor might earn double or triple the load credit by teaching a very large class. Generally, this additional load credit could be used to offset the number of courses that instructor teaches in a semester, or if the instructor is teaching in excess of a full load, it might be taken as additional pay above the full-time requirement during that semester or banked to offset a future semester, as permitted by the Education Code and according to the terms of the agreement.

Section 27401 was amended to clarify that when the contractual full-time is based on load credits or a similar non-time based measure, additional service includes any service that is associated with earning those credits. In other words, the compensation associated with accumulating load credits is associated with the performance of additional service and, therefore, is not reportable as remuneration in addition to salary. If the overload credit is banked for future use to cover a period when the employee works less than a full load, the compensation overload credit should be reported as salary when the banked time is used. If the overload credit is not banked for future use, the compensation should be reported as salary for an additional assignment.

In addition, compensation for large class sizes and other types of remuneration that is paid in addition to salary must be paid in the same manner to all members of a class of employees. If compensation is offered in an alternative form (for example, a teacher with extra students in the classroom can choose between a teachers' aide and cash compensation), the compensation is not creditable. This is true even if cash is one of the alternatives and it is the option selected. Section 27401 was amended to clarify this provision.

Additional Amendments with No Impact to the Reporting of Creditable Compensation
The aforementioned sections along with Section 27301 of the Creditable Compensation Regulations also include amendments to improve readability. In addition, Sections 27600 through 27602 were amended to clarify the manner in which CalSTRS assesses compensation for consistency and credits contributions appropriately. None of these amendments have a bearing on the manner in which employers report creditable compensation to CalSTRS.

ACTION

Refer to the updated Creditable Compensation Regulations to ensure compensation paid to CalSTRS 2% at 60 members for service performed on or after January 1, 2015, is accurately reported to CalSTRS.

The updated regulations will be included in the 2018 edition of the Teachers' Retirement Law book available on CalSTRS.com. In the meantime, you can access the updated regulations on the Secure Employer Website under Reference Items.

This Employer Directive does not take precedence over the law. If you have any questions regarding this Employer Directive, please email EmployerHelp@CalSTRS.com or call 877-277-5778.

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Reference No.:
Circular Letter No.: 200-055-12
Distribution: IV, V, VI, X, XII, XVI
Special:

Circular Letter

December 3, 2012

TO: **ALL CALPERS EMPLOYERS**

SUBJECT: **IMPLEMENTATION OF PUBLIC EMPLOYEES' PENSION REFORM ACT OF 2013**

The purpose of this Circular Letter is to confirm CalPERS current interpretation of the Public Employees' Pension Reform Act of 2013 (PEPRA) and related Public Employees' Retirement Law (PERL) amendments in Assembly Bill (AB) 340, passed by the California Legislature on August 31, 2012, and signed by the Governor on September 12, 2012.

Recent news about the enactment of pension reform has generated increased attention and questions from our employers, members, and stakeholders. We created this Circular Letter to provide a summary of the provisions outlined in the bill as they apply to CalPERS retirement and health benefits. We also include information on my|CalPERS system modifications and explain what actions employers need to take to comply with the new provisions that change how they do business with CalPERS.

This Circular Letter is not intended to provide a comprehensive summary of PEPRA and related law changes. The current interpretations discussed below address the key areas of the bill that may directly affect CalPERS interactions with our members and employers. Our pension reform team continues to analyze PEPRA provisions and the resulting impacts. As CalPERS moves ahead with implementing PEPRA and related amendments to the PERL, our interpretations may be revised. CalPERS strongly recommends that all employers review AB 340 in its entirety to understand how the changes in law will affect their organization and employees.

MEMBERSHIP AND BENEFIT FORMULAS

Definition of a New Member

A new member is defined in PEPRA as any of the following:

- A new hire who is brought into CalPERS membership for the first time on or after January 1, 2013, and who has no prior membership in any California public retirement system.
- A new hire who is brought into CalPERS membership for the first time on or after January 1, 2013, and who is not eligible for reciprocity with another California public retirement system.

- A member who first established CalPERS membership prior to January 1, 2013, and who is rehired by a different CalPERS employer after a break in service of greater than six months.

Effective January 1, 2013, every new enrollment will be tested against this definition of "new member", regardless of whether the enrollment is for a first-time CalPERS member or an existing CalPERS member.

It is important to note that if a member has a break in service of more than six months but returns to service with the same employer, the member would not be considered a new member under PEPRA. All State agencies, including CSU, are treated as a single employer under PEPRA, as are all school employers.

CalPERS refers to all members that do not fit within the definition of a new member as "classic members". All existing CalPERS members as of December 31, 2012, will retain the existing benefit levels for future service with the same employer. Because the new member determination is made on an appointment-by-appointment basis, classic members will be tested against the "new member" definition upon each new appointment and, in some cases, may become "new members" for services under a new appointment. PEPRA does not require retroactive reductions to benefits earned for prior service, even where a member separates from service and is later re-hired as a new member by a new employer and becomes subject to the applicable PEPRA formula. In these cases, the member's "classic member" service will be calculated separately from his or her service as a "new member".

CalPERS will develop a form for employers to use when a member hired by a CalPERS agency is considered a classic member as a result of membership with a previous reciprocal retirement system. Employers must complete the form and retain it in the individual's employment records for auditability purposes.

my|CalPERS will be updated to include fields on the enrollment page where employers will identify if the new hire is coming from a reciprocal agency and prompt the employer for the necessary data elements which subject them to reciprocity. It will be extremely important for employers to properly identify the status of members at the time of hire.

Based on the information provided by the employer, my|CalPERS will automatically determine the proper benefit group for each member. In addition, CalPERS will create for each employer a report identifying their recent enrollments and the correct corresponding formula based on the information provided at enrollment. If an employer believes the enrollment is incorrect, they may contact CalPERS to review and correct the data as necessary. Employers must store, in their own databases, the participant details necessary to categorize individuals as new members or classic members.

Important! These system enhancements are not yet available. All member enrollments with an effective date of January 1, 2013, or later should be held until employers receive notification that the transaction may be processed.

Throughout the upcoming months, CalPERS will create and/or update forms and publications to assist employers with enrollment transactions for new members. A Circular Letter will be sent to employers as those resources become available.

Benefit Formulas

The reduced benefit formulas and increased retirement age provisions under PEPRA create new defined benefit formulas for all new miscellaneous (non-safety) and safety members.

For new safety members, the law provides for three possible retirement formulas and requires that new safety members be provided with the new formula that is closest to the formula offered to classic members of the same classification and that provides a lower benefit at 55 years of age than the formula offered to classic members. The three new defined benefit formulas for new safety members include a normal retirement age of 50 and a maximum benefit at age 57.

For all new miscellaneous members, with the exception of State Tier II, the new defined benefit formula is 2% at age 62, with an early retirement age of 52 and a maximum benefit factor of 2.5% at age 67. For State Tier II members, the new formula is 1.25% at age 67.

Please refer to the tables below to see how the reduced benefit formulas compare to current formulas.

Current Miscellaneous Formula	New Miscellaneous Formula
1.5%@65	1.5%@65 (retain existing formula)
1.25%@65	1.25%@67
All others	2%@62

Current Safety Formula	New Safety Formula
3%@50, 3%@55, 2%@50	2.7%@57
2.5%@55	2.5%@57
2%@55, 2.5%@60, ½@55	2%@57

The new formulas will be implemented in my|CalPERS to take effect on January 1, 2013. The legislatively mandated formulas and provisions will be merged with the employer's existing optional provisions, with some exceptions, effective on December 31, 2012, to create the new benefit groups.

No formal contract amendments are necessary to implement the new mandated benefit groups. CalPERS will work with employers to update the employer's contract(s) either at the time of a future amendment or as soon as practicable. CalPERS estimates that it will take approximately two years to complete this update process for all employers.

EMPLOYER AND MEMBER CONTRIBUTIONS

Normal Cost Contributions

For public agencies, school employers, CSU, and the judicial branch, a new member's initial contribution rate will be at least 50% of the total normal cost rate for their defined benefit plan or "the current contribution rate of similarly situated employees, whichever is greater", except where it would cause an existing Memorandum of Understanding (MOU) to be impaired. If an employer determines that an existing MOU is impaired, and communicates that decision to CalPERS using the required certification form, then any otherwise impaired contribution rate agreement will apply to new members through the duration of the MOU. Once the impaired MOU is amended, extended, renewed, or expires, the new requirements will apply.

CalPERS interprets "similarly situated members" to mean those employees that are in the same benefit group (meaning those employees with the same benefit formula). The member contribution rate is not required to change for classic members of a public agency or school district.

State employees, including both classic and new members (excluding new CSU members and new judicial branch members), will pay the statutory rates determined through bargaining and provided for by statute. See Proposed Changes in Member Contribution Rates for State Employees for changes that PEPRA imposes on State member contributions available on CalPERS On-Line.

CalPERS will be sending a letter to each employer this month outlining the benefit formula applicable to new members, as well as the employer and member contribution rates that will be effective January 1, 2013, for new members. For classic members, employers should refer to the June 30, 2011 actuarial valuation report that was mailed in November 2012 to determine what amount reflects 50% of the total normal cost for classic members. In addition, a new report will be added in my|CalPERS that will identify member and corresponding member rates by group and plan. The *Appointment Details and Events* page in my|CalPERS will also display the appropriate contribution rates for members.

Beginning January 1, 2018, public agencies that have collectively bargained in good faith and completed impasse procedures (including mediation and fact-finding) will be able to unilaterally require classic members to pay up to 50% of the total normal cost of their pension benefit. It is important to note that the employee contribution may only be increased up to an 8% contribution rate for miscellaneous members, a 12% contribution rate for local police officers, local firefighters, and county peace officers, or an 11% contribution rate for all other local safety members.

Cost Sharing of Employer Contributions

Some public agencies have amended their CalPERS contract to have their members pay a portion of the employer's contribution. These contributions are paid in addition to the member contribution rate. Under existing law, such employer cost sharing contract amendments were required to be tied to a benefit improvement. This requirement will be eliminated as of January 1, 2013, when the new amendments to the PERL go into

effect. In addition, under the new law, cost sharing agreements may differ by bargaining unit or for classifications of employees subject to different benefit levels as agreed to in an MOU. The new law also permits cost sharing of the employer costs for non-represented employees as approved in a resolution passed by the public agency.

Employer Paid Member Contributions (EPMC)
PEPRA prohibits EPMC for new members, employed by public agencies, school employers, the judicial branch, or CSU, unless an employer's existing MOU would be impaired by this restriction. It is up to each employer to determine if an MOU would be impaired by this restriction on EPMC for new members. The impaired MOU must have an effective date of January 1, 2013, or earlier.

If the employer determines that an existing MOU is impaired, then any stated EPMC agreements will apply to new members through the duration of the MOU. CalPERS must receive the full required member contributions, regardless of the amounts paid by the member or the employer. Once the impaired MOU is amended, extended, renewed, or expires, EPMC will no longer be permitted for new members. CalPERS will implement a manual validation procedure to ensure EPMC is not being reported on payroll for new members.

Employers must notify CalPERS in writing if they determine that their MOU is impaired and provide a certification to CalPERS, signed by the agency's presiding officer, confirming that application of Section 7522.30(c) of PEPRA would cause an existing MOU to be impaired. CalPERS will provide a form to employers for this certification. More information on the certification and the form will be sent to employers in a future Circular Letter.

EPMC may continue to be reported for classic members pursuant to existing PERL provisions. Employers who wish to eliminate or reduce EPMC for classic members are able to do so under existing law through collective bargaining and contract amendments. Existing PERL statutes allow employers to periodically increase, reduce or eliminate employer paid member contributions.

Pension Holiday
The combined employer and member contributions required, in any fiscal year, cannot be lower than the total year's normal cost.

Some employers currently have a surplus in their plan and presently pay less than the total normal cost. CalPERS will review each employer in this category and determine whether this provision must be implemented at the start of the next fiscal year. A letter will be sent to affected employers notifying them of their required contribution amounts.

PENSIONABLE COMPENSATION

Compensation Caps
This provision caps the annual pensionable compensation that can be used to calculate final compensation for new members.

Presently, there is a compensation cap in place for first-time members hired after January 1, 1996. The compensation cap is set by the Internal Revenue Service and is referred to as the 401(a)(17) limit. CalPERS will continue to cap contributions for affected classic members at the 401(a)(17) limit.

New member contribution caps are effective January 1, 2013. The new member cap for 2013 will be $113,700 (100% of the 2013 Social Security contribution and benefit base) for members that participate in Social Security or $136,440 (120% of the 2013 contribution and benefit base) for those employees that do not participate in Social Security. Adjustments to the caps are permitted annually based on changes to the Consumer Price Index for All Urban Consumers.

Employers will report full pay rate and actual earnings for all members in my|CalPERS and the system will flag and notify the employer when the contribution limit has been reached for that calendar year. Member contributions must stop when the member's actual earnings reach the contribution limits outlined above.

Note that this does not necessitate a change to your file formatting structure; rather it is related to how employers track and report payroll. Reporting up to the compensation cap for new members will occur in the same manner it does currently for classic members subject to the 401(a)(17) limit.

Currently, CalPERS does not cap employer contributions at the 401(a)(17) limit and we do not intend to cap employer contributions at the PEPRA limits for at least the next two years. We are conducting further analysis to determine if employer contributions will be capped beginning with the 2015/2016 fiscal year. We will share the new information with you in a future Circular Letter once a final decision has been made.

Three-Year Final Compensation

PEPRA requires that a three-year final compensation period be used to calculate the average final compensation for a retirement calculation for all new members. Some employers, including the State, already provide for a three-year final compensation period.

Public employers are also prohibited from adopting a final compensation period of less than three years for classic members who are currently subject to three-year final compensation.

Pensionable Compensation

PEPRA introduces a new term "pensionable compensation" for the purposes of determining reportable compensation for new members. PEPRA broadly defines pensionable compensation, and while it specifically excludes some forms of compensation, it does not clearly identify which forms of pay fall within the scope of pensionable compensation. CalPERS is evaluating what forms of compensation are considered as pensionable compensation and how they should be reported. We will update employers on this issue in a future Circular Letter that we anticipate will be sent later this month.

Excessive Compensation
This new PERL provision requires the CalPERS Board to "define a significant increase in actuarial liability due to increased compensation paid to a non-represented employee". The Board is further directed to implement program changes to ensure that a public agency that creates a significant increase in actuarial liability bears the increased cost associated with that liability.

CalPERS will develop the program changes necessary to assess the cost of excessive compensation to the employer that paid the excessive compensation. This provision will apply to any significant increase in actuarial liability that is determined after January 1, 2013, regardless of when excessive compensation was paid.

CalPERS is working to develop the program changes and definitions necessary to administer these provisions and anticipates promulgating regulations to address these new requirements. Updates on this issue will be provided to employers in a future Circular Letter.

WORKING AFTER RETIREMENT

PEPRA includes two provisions applicable to working after retirement. These provisions include restrictions, including, but not limited to:

- All employees who retire from public service will be prohibited from working more than 960 hours per calendar or fiscal year for any public employer in the same public retirement system that the individual is retired from without reinstating from retirement.
- A 180-day waiting period is required for all employees who retire from a public employer before a retiree can return to work without reinstating from retirement, except under certain specified circumstances. The 180-day waiting period starts from the date of retirement.
- Any public retiree appointed to a full-time position on a State board or commission will be required to suspend their retirement allowance and become an active member of CalPERS, unless the appointment is non-salaried.

As currently required, employers must continue to report in my|CalPERS all the hours worked by any CalPERS retired annuitant in order to monitor the 960-hour cap per fiscal year. CalPERS retirees who are hired as independent contractors or consultants with a direct relationship, for purposes of this section, are considered retired annuitants and must also be reported and tracked in my|CalPERS.

The 180-day waiting period provision applies without exception to retirees who receive either a golden handshake or some other employer incentive to retire. Retired annuitants who started working before January 1, 2013, are not impacted by the 180-day waiting period.

my|CalPERS plans to validate the 180-day waiting period for all new enrollments and will flag any potential violations of this waiting period for additional review. Potential violations will not prohibit the online my|CalPERS enrollment; however, when enrolling a retiree under the certification-resolution exception to the 180-day waiting period, the

employer must submit a copy of the certification-resolution to CalPERS. The rest of the enrollment process will remain the same as today.

PENSION AND HEALTH BENEFIT CHANGES

Industrial Disability Retirement (IDR) Benefits

In addition to the current calculation options of the IDR benefit for a member, this provision adds a calculation for a safety member who qualifies for an IDR that may result in a higher benefit than 50% of salary. An actuarial reduced retirement formula, as determined by the actuary for each quarter year of service age less than 50, will be used to determine if the IDR benefit is greater for the safety member who qualifies for IDR. These provisions remain in effect only until January 1, 2018. After that date, the new IDR provisions will not apply unless the date is extended by statute.

Retroactive Pension Benefit Enhancements

Public employers will be prohibited from granting retroactive pension benefit enhancements that would apply to service performed prior to the operative date of the enhancement. An increase to a retiree's annual cost-of-living adjustment within existing statutory limits is not considered to be an enhancement to a retirement benefit.

CalPERS will develop a list of those existing optional benefits that are considered to be retirement benefit enhancements and therefore subject to this restriction. CalPERS also plans to promulgate a regulation interpreting and clarifying this provision. Additional information will be sent to employers in a future Circular Letter.

Replacement Benefit Plans

PEPRA prohibits public employers from providing new employees a plan of replacement benefits to supplement retirement benefits that are limited by Internal Revenue Code Section 415(b). This provision also prohibits public employers from offering a replacement benefit plan to any employee group that was not provided this benefit prior to January 1, 2013.

CalPERS will continue to offer replacement benefit plans for classic members not impacted by this provision.

Health Benefit Vesting Schedule

This provision generally prohibits employers from providing a more advantageous health benefit vesting schedule to certain individuals (namely a public employee who is elected or appointed, a trustee, excluded from collective bargaining, exempt from civil service, or a manager) than it does for other public employees, including represented employees, of the same public employer who are in related retirement membership classifications. In the event that bargaining groups under one employer have established different vesting schedules, the non-represented employees must align with the least advantageous of the groups in related membership classifications, such as State miscellaneous.

If an employer has established tiered vesting schedules based upon date of hire, then all non-represented employees must be subject to the same tiered vesting schedules as represented employees of the same membership classifications.

Additional Retirement Service Credit (ARSC)
The ability to purchase non-qualified service, or "airtime", will be eliminated on January 1, 2013. An official application must be submitted and stamped as received by CalPERS on or before December 31, 2012. Only applications from individuals who qualify to purchase ARSC on or before December 31, 2012, will be accepted. CalPERS is reviewing whether other types of nonqualified service credit may be impacted by this prohibition.

The prohibition on future "airtime" service credit purchases does not prohibit purchases of qualified service credit. For example, service credit purchases for qualified military service will still be allowed.

Felony Forfeiture of Pension Benefits
Any current or future public official or employee convicted of a felony while carrying out his or her official duties, in seeking an elected office or appointment, and/or in connection with obtaining salary or pension benefits, will be required to forfeit any pension or related benefit earned from the date of the commission of the felony.

OTHER RETIREMENT PROGRAMS

Alternate Retirement Program (ARP)
ARP, a retirement savings program that certain State employees are automatically enrolled in for two years from their initial hire date, will be eliminated. The bill provides that all new members hired on or after July 1, 2013, will no longer be enrolled in the program. An urgency legislative amendment was introduced to change the ARP elimination date from July 1, 2013 to January 1, 2013. CalPERS will continue to monitor the bill and work with the State Controller's Office and the California Department of Human Resources to determine how to enroll new State miscellaneous and industrial members beginning January 1, 2013. Once a process has been identified, we will notify State employers.

Members currently enrolled in ARP will continue to participate in ARP pursuant to existing statutory requirements.

CalPERS does not administer ARP. For program details on the ARP savings plan, contact the California Department of Human Resources at www.calhr.ca.gov.

Legislative Retirement System (LRS)
These provisions prohibit new members, including constitutional, statutory elected officers and the Insurance Commissioner, who assume office for the first time on or after January 1, 2013, from enrolling in LRS. Members already enrolled in LRS prior to January 1, 2013, will continue to participate in the plan until they separate or retire.

my|CalPERS will be modified to remove LRS enrollment as an option for new members. The current process that allows new members to elect optional membership into CalPERS will not change.

ADDITIONAL INFORMATION

CalPERS On-Line

For more information on PEPRA and how it impacts current and future CalPERS members, visit the Pension Reform Impacts page on CalPERS On-Line at www.calpers.ca.gov. This page features the latest updates regarding PEPRA including a question and answer section and links to additional resources. In addition, the video "Pension Reform: A Discussion with CalPERS Experts" highlights how pension reform impacts employers.

Teleconferences

CalPERS will conduct a series of teleconferences to address questions you may have relating to the information in this Circular Letter. Please register online via the Pension Reform Impacts page.

Date	Time	Agency Type
Dec 10	9:30 to 11:30 am	Public Agency
Dec 10	1:30 to 3:30 pm	School
Dec 11	9:30 to 11:30 am	State
Dec 12	9:30 to 11:30 am	Public Agency
Dec 13	9:30 to 11:30 am	School
Dec 14	9:30 to 11:30 am	State

my|CalPERS Changes

CalPERS will provide more detailed information regarding my|CalPERS changes in the coming weeks.

Contact Us

Please share this information with your employees to help answer their questions and provide additional information on the changes. If you have any questions, please call the CalPERS Customer Contact Center at **888 CalPERS** (or **888**-225-7377).

KAREN DeFRANK, Chief
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Reference No.:
Circular Letter No.: 200-062-12
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Special:

Circular Letter

December 27, 2012

TO: **PUBLIC AGENCIES, AGRICULTURAL DISTRICTS, COUNTY SUPERINTENDENT OF SCHOOLS AND INDIVIDUAL SCHOOL DISTRICTS**

SUBJECT: **PUBLIC EMPLOYEES' PENSION REFORM ACT OF 2013 – PENSIONABLE COMPENSATION AND BENEFIT ENHANCEMENTS**

The purpose of this Circular Letter is to provide further information regarding CalPERS current interpretation of "pensionable compensation" and "benefit enhancements" subject to the provisions of the Public Employees' Pension Reform Act of 2013 (PEPRA) and related Public Employees' Retirement Law (PERL) amendments in Assembly Bill (AB) 340.

PENSIONABLE COMPENSATION

For new members, as defined by Government Code (G.C.) Section 7522.04(f), "pensionable compensation" must meet the following four criteria as provided in G.C. Section 7522.34(a):

- Pay is part of the normal monthly rate of pay or base pay.
- Pay is paid in cash to similarly situated members of the same group or class of employment.
- Pay is for services rendered during normal working hours.
- Pay is paid pursuant to publicly available pay schedules.

G.C. Section 7522.34(c) also provides what cannot be included in "pensionable compensation" for new members. For example, "pensionable compensation" does not include monies paid to new members for bonuses, uniform allowance, overtime allowance or reimbursement for housing and vehicles, or any ad hoc or one-time payments. Please refer to G.C. Section 7522.34(c) for additional forms of compensation that are not considered "pensionable compensation" under PEPRA; the items listed above are only some of the most commonly reported items by employers.

CalPERS interpretation of the types of compensation that may be reported as "pensionable compensation" for CalPERS contracting agencies, provided those items meet the four criteria above, are attached to this letter. This list of "pensionable compensation" will be implemented on January 1, 2013, for new PEPRA public agency and school members. As discussed below, CalPERS intends to propose implementing

regulations to, among other things, include this list of items that may be reported as "pensionable compensation" for contracting agencies.

For classic members, please refer to California Code of Regulations (CCR) Section 571 for a list of special compensation items that may be reported. Employers should continue to report both pay rate and all reportable special compensation under CCR 571 as PEPRA does not impact reportable compensation for classic members.

BENEFIT ENHANCEMENTS

G.C. Section 7522.44(a) specifies that "any enhancement to a public employee's retirement formula or retirement benefit adopted on or after January 1, 2013, shall apply only to service performed on or after the operative date of the enhancement and shall not be applied to any service performed prior to the operation date of the enhancement."

Circular Letter #200-055-12, stated CalPERS would develop a list of those existing optional benefits that CalPERS considers to be retirement "benefit enhancements" and therefore subject to the restrictions of PEPRA. The proposed list of existing optional benefit provisions is as follows:

- G.C. Section 21427 – Improved Nonindustrial Disability Allowance
- G.C. Section 21547.7 – Alternate Death Benefit for Local Fire Members Credited with 20 or More Years of Service
- G.C. Section 21548 – Pre-Retirement Option 2W Death Benefit
- G.C. Sections 21624, 21626, 21628 – Post-Retirement Survivor Allowance
- G.C. Section 21151 – Industrial Disability Retirement for Local Miscellaneous Members
- Miscellaneous Member Classifications Optionally Reclassified to Safety by Amendment to the Contract

See the document Optional Benefits Listing on CalPERS On-Line for details on the benefit provisions listed above.

Please note that pursuant to G.C. Section 7522.44(d) "an increase to a retiree's annual cost-of-living adjustment within existing statutory limits shall not be considered to be an enhancement to a retirement benefit."

2013 REGULATORY PROCESS

In 2013, CalPERS will propose implementing regulations to clarify its interpretation of "publicly available pay schedules" and "benefit enhancements" as the terms apply to new members, and to provide a list of items that may be reported as "pensionable compensation" for contracting agencies to the extent those items meet the four criteria above. It is important to note that as the proposed regulations proceed through the regulatory process, some changes, including the items contained in the attached list, may be required. CalPERS will provide information on the proposed regulations as it becomes available.

CalPERS will continue to develop the program changes and interpretations for terms necessary to administer the provisions required by PEPRA. We recommend that you continue to refer to the Pension Reform Impacts page on CalPERS On-Line at www.calpers.ca.gov for the latest PEPRA updates.

In addition, a new online training class is available for employers. *my|CalPERS Changes Due to the Public Employee's Pension Reform Act of 2013 (PEPRA)* reviews important changes to the my|CalPERS system based on PEPRA provisions. To enroll in online training, log in to in my|CalPERS and select the **Education** tab.

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

KAREN DeFRANK, Chief
Customer Account Services Division

Enclosure
Pensionable Compensation Items – New PEPRA Public Agency and School Members (PDF, 31 KB)

"Pensionable Compensation" Items – New PEPRA Public Agency and School Members

CalPERS interpretation of the types of compensation that may be reported as "pensionable compensation" for CalPERS contracting agencies, provided those items meet the criteria contained in Government Code Section 7522.34(a), are listed below. CalPERS will initiate the regulatory process in 2013 to provide this list of items that may be reported as "pensionable compensation" for contracting agencies. More information on the proposed regulations will be provided to you as it becomes available.

In the meantime, the proposed list of "pensionable compensation" items below will be implemented, and can be reported on January 1, 2013, for new PEPRA public agency and school members. It is important to note that as the proposed regulations proceed through the regulatory process, some changes, including the items contained in this list, may be required.

Type	Reportable Special Compensation Items
Incentive Pay	• Dictation/Shorthand/Typing Premium • Longevity Pay • Marksmanship Pay • Master Police Officer • Physical Fitness Program
Educational Pay	• Applicator's Differential • Certified Public Accountant Incentive • Educational Incentive • Emergency Medical Technician Pay • Engineering Registration Premium • Government Agency Required Licenses • International Conference of Building Officials (ICBO) Certificate • Mechanical Premium (Brake Adjustment License, SMOG Inspector License) • National Institute of Automotive Service Excellence (NIASE) Certificate • Notary Pay • Paramedic Pay • Peace Officer Standard Training (POST) Certificate Pay

Continued on next page

"Pensionable Compensation" Items – New PEPRA Public Agency and School Members, Continued

Type	Reportable Special Compensation Items
Educational Pay, Continued	• Reading Specialist • Recertification Certificate • Special Class Driver's License Pay • Undergraduate/Graduate/Doctoral Credit
Special Assignment Pay	• Accountant Premium • Administrative Secretary Premium • Aircraft/Helicopter Pilot Premium • Asphalt Work Premium • Audio Visual Premium • Auditorium Preparation Premium • Bilingual Premium • Branch Assignment Premium • Canine Officer/Animal Premium • Cement Finisher Premium • Circulation Librarian Premium • Computer Operations Premium • Confidential Premium • Contract Administrator Coordinator Premium • Crime Scene Investigator Premium • Critical Care Differential Premium • D.A.R.E. Premium • Detective Division Premium • Detention Services Premium • DUI Traffic Officer Premium • Extradition Officer Premium • Fire Inspector Premium • Fire Investigator Premium • Fire Prevention Assignment Premium • Fire Staff Premium • Flight Time Premium • Float Differential Premium • Front Desk Assignment (Jail) • Fugitive Officer Premium • Gang Detail Assignment Premium • Grading Assignment Premium

Continued on next page

"Pensionable Compensation" Items – New PEPRA Public Agency and School Members, Continued

Type	Reportable Special Compensation Items
Special Assignment Pay, Continued	• Hazard Premium • Heavy/Special Equipment Operator • Height Premium • Housing Specialist Premium • Juvenile Officer Premium • Lead Worker/Supervisor Premium • Library Reference Desk Premium • Gas Maintenance Premium • Plumber Irrigation System Premium • Refuse Collector Premium • Street Lamp Replacement Premium • MCO Instructor Premium • Motorcycle Patrol Premium • Mounted Patrol Premium • Narcotic Division Premium • Paramedic Coordinator Premium • Park Construction Premium • Park Maintenance/Equipment Manager Premium • Parking Citation Premium • Patrol Premium • Police Administrative Officer • Police Investigator Premium • Police Liaison Premium • Police Polygraph Officer • Police Records Assignment Premium • Rangemaster Premium • Refugee Arrival Cleanup Premium • Safety Officer Training/Coordinator Premium • Sandblasting Premium • School Yard Premium • Search Pay Premium • Severely Disabled Premium • Sewer Crew Premium • Shift Differential

Continued on next page

"Pensionable Compensation" Items – New PEPRA Public Agency and School Members, Continued

Type	Reportable Special Compensation Items
Special Assignment Pay, Continued	• Solo Patrol Premium • Sprinkler and Backflow Premium • Tiller Premium • Tire Technician Premium • Traffic Detail Premium • Training Premium • Tree Crew Premium • Utility Meter Premium • Utilities Systems Operation Premium • Water Certification Premium
Statutory Items	• Fair Labor Standards Act (FLSA) • Holiday Pay

California Public Employees' Retirement System
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www.calpers.ca.gov

Reference No.:
Circular Letter No.: 200-063-12
Distribution: IV, V, VI, X, XII, XVI
Special:

Circular Letter

December 31, 2012

TO: **ALL CALPERS EMPLOYERS**

SUBJECT: **PUBLIC EMPLOYEES' PENSION REFORM ACT OF 2013 – NEW ENROLLMENTS, NEW AND REVISED FORMS AND PUBLICATIONS**

The purpose of this Circular Letter is to provide information regarding new enrollments and CalPERS forms and publications that were created or revised due to the Public Employees' Pension Reform Act of 2013 (PEPRA) and related Public Employees' Retirement Law (PERL) amendments in Assembly Bill (AB) 340.

NEW ENROLLMENTS

All new enrollments with an effective date of January 1, 2013, or later should be held until Monday, January 7, 2013. The necessary my|CalPERS system enhancements will then be available and you should resume processing transactions at that time. If an enrollment is required to be entered prior to that time due to other constraints, please call the CalPERS Customer Contact Center at **888 CalPERS** (or **888**-225-7377) for assistance.

Please note that enrollments with an effective date of December 31, 2012, or earlier may be processed as normal in my|CalPERS.

NEW FORMS

The new forms listed below will be available online after January 1, 2013. To access the online versions, please visit the Forms & Publications Center on CalPERS On-Line. Printed copies of the new forms are attached to this letter.

Member Reciprocal Self-Certification Form (PERS-CASD-801)
This form is for employers to use to identify if new employees are classic members due to reciprocity. It is extremely important for employers to properly identify the status of members at the time of hire.

While processing an enrollment in my|CalPERS, employers will identify if the new hire is coming from a reciprocal agency and be prompted to enter the necessary data elements which subject them to reciprocity. This form identifies those necessary data elements the employer is required to enter.

Based on the enrollment information entered by the employer, my|CalPERS will automatically determine the proper benefit group for the new employee. Employers must retain a copy of this form in the individual's employment records for auditability purposes.

Certification of MOU Impairment (PERS-CASD-800)
This form can be used by employers to notify CalPERS in writing if they certify that the terms of their Memorandum of Understanding (MOU), in effect on or before January 1, 2013, will be impaired by their compliance with the requirements of one or more provisions of Government Code Section 7522.30. See the form for more information.

Please review Circular Letter #200-055-12 for additional information on reciprocity and MOU impairment as it relates to PEPRA.

UPDATED PUBLICATIONS

The revised versions of the following publications will be available online in the Forms & Publications Center on CalPERS On-Line by January 1, 2013. Printed editions will be available in approximately 6-8 weeks:

- School Member Benefit Publication (PUB 2)
- State Safety Member Benefit Publication (PUB 7)
- Local Miscellaneous Member Benefit Publication (PUB 8)
- Local Safety Member Benefit Publication (PUB 9)
- Alternate Retirement Program (PUB 10)
- A Guide to Your CalPERS Service Credit Purchase Options (PUB 12)
- When You Change Retirement Systems (PUB 16)
- Employment After Retirement (PUB 33)
- A Guide to Completing Your CalPERS Disability Retirement Election (PUB 35)
- Reinstatement From Retirement (PUB 37)
- A Guide to CalPERS Community Property (PUB 38A)

The revised versions of the following publications are anticipated to be available online by January 15, 2013:

- Planning Your Service Retirement (PUB 1)
- State Miscellaneous & Industrial Member Benefit Publication (PUB 6)
- National Guard Member Benefit Publication (PUB 11)
- State Second Tier Election Application (PUB 52)

Please note that the dates of availability for the revised versions of the publications listed in this letter are subject to change.

We encourage you to visit the Pension Reform Impacts page on CalPERS On-Line at www.calpers.ca.gov for the latest PEPRA information and updates.

In addition, a new online training class, ***my|CalPERS Changes Due to the Public Employee's Pension Reform Act of 2013 (PEPRA)***, is now available for employers. This class reviews important changes to the my|CalPERS system based on PEPRA provisions.To enroll in online training, log in to in my|CalPERS and select the **Education** tab.

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

KAREN DeFRANK, Chief
Customer Account Services Division

Enclosures
Member Reciprocal Self Certification Form (PERS-CASD-801)
Certification of Memorandum of Understanding (MOU) Impairment (PERS-CASD-800)

California Public Employees' Retirement System
Customer Account Services Division
Retirement Account Services Section
P.O. Box 942709
Sacramento, CA 94229-2709
TTY: (877) 249-7442
888 CalPERS (or **888**-225-7377) phone • (916) 795-3005 fax
www.calpers.ca.gov

Certification of Memorandum of Understanding (MOU) Impairment

Agency Name: _____ CalPERS ID: _____

The undersigned is the duly elected or appointed _____ of _____ (the "Public Agency") and is authorized to execute this Certification of MOU Impairment (the "Certification") on behalf of the Public Agency.

The undersigned, as the Public Agency's authorized signatory, hereby certifies that the terms of that certain Memorandum of Understanding, dated _____ (the "MOU"), would be impaired by Public Agency's compliance with the requirements of one or more provisions of section 7522.30 of the Government Code. Therefore, pursuant to section 7522.30(f) of the Government Code, Public Agency is notifying CalPERS that it will not comply with those provisions of section 7522.30 that would impair the MOU until such time as the MOU expires under its terms, or is terminated, amended, renewed, or extended. Notwithstanding an MOU impairment, Public Agency acknowledges and agrees that the sum total of all member and employer contributions must be paid when due (whether paid by the employer or the member), and an MOU impairment shall not result in a reduction of such sum total. Public Agency further acknowledges and agrees that for purposes of crediting member contributions, CalPERS will treat the member contribution rate for new members as being the rate described in Government Code section 7522.30(c). The undersigned agrees that the Public Agency shall immediately notify CalPERS upon the expiration, renewal, termination, amendment or extension of the MOU, and at such time will fully comply with section 7522.30 of the Government Code.

The undersigned further certifies that, to the best of his or her knowledge, the information provided below is true, complete and correct in all material respects.

Membership Group Impacted	Type of Impairment (EPMC and/or Cost Sharing)	MOU Expiration Date

Name: _____ Signature: _____

Title: _____ Date: _____

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P.O. Box 942709 Sacramento, CA 94229-2709
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TTY: (877) 249-7442 | Fax: (916) 795-4166
www.calpers.ca.gov

Employer Account Management Division

Dear Member,

You are being provided with the background, explanation, and instructions for the **Reciprocal Self-Certification Form (PERS-EAMD 801)**. Reciprocity among qualified Public Retirement Systems is to allow members to separate from one qualified Public Retirement System and enter into employment under another within a specific time period without losing valuable retirement and related benefit rights.

With the implementation of the Public Employees' Pension Reform Act of 2013 (PEPRA), Government Code section 7522, on January 1, 2013, the California Public Employees' Retirement System (CalPERS) requires that employers provide you with this package to complete the Reciprocal Self-Certification form. The Reciprocal Self-Certification form allows you to provide essential information to your employer and will be used by your employer to enroll you into CalPERS membership and every new appointment under CalPERS. This information will assist CalPERS in identifying the correct retirement benefit level to enroll you into CalPERS. For more information regarding PEPRA, please see our website at **www.calpers.ca.gov**.

Within 10 business days of membership or new appointment you must complete, sign, date, and submit to your employer the Reciprocal Self-Certification form. When completing the form, reference the attached list of qualifying Public Retirement Systems in California. Complete the form by indicating that you are not a current or past member of a qualifying Public Retirement System; **OR** indicate that you have prior membership in a qualifying Public Retirement System and complete the box listing your previous membership dates, permanent separation dates, and retirement or refund dates, if applicable.

It is important to ensure you are providing accurate information so your retirement enrollment level can be properly determined. It is your responsibility to ensure the accuracy of the data provided on the Reciprocal Self-Certification Form. Inaccurate information may cause your account to reflect an incorrect retirement enrollment level which can have many impacts to your account including ineligible retirement benefit formulas, adverse effects on how your retirement benefit is calculated, and delays in CalPERS processing timeframes. Providing inaccurate information may lead to future retroactive adjustments to your member and employer contributions, and you and your employer will be responsible for any debts that may occur.

Information to remember when completing the form:

- Please ensure you are providing complete and accurate dates. You must provide a month, date, and year. If you are unsure of the dates, please contact the qualifying Public Retirement System to verify prior to completing the form.
- For each prior Reciprocal System reported, you must provide the name of the qualifying Public Retirement System and membership date. If you have separated, retired, or refunded from that Reciprocal System, please indicate that by providing dates in the appropriate sections. If you have not separated, retired, or refunded from that Reciprocal System, you may leave these sections blank or indicate that by entering N/A (not applicable).

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Employer Account Management Division

- It is not necessary to include data related to employment covered by CalPERS when completing this form as this information is already withheld in the CalPERS system.
- Only include information related to a Defined Benefit Plan of a qualifying Public Retirement System. Defined contribution plans are not eligible for reciprocity.

The completion of this form provides data to be used to enroll you into the correct retirement enrollment formula**.** The completion of the Reciprocal Self-Certification Form does not establish reciprocity, nor is it a request to establish reciprocity. In order to request that reciprocity be established, visit the CalPERS website, **www.calpers.ca.gov** and download the publication ***When You Change Retirement Systems***. It is the responsibility of the employee to complete and send the form, ***Confirmation of Intent to Establish Reciprocity When Changing Retirement Systems,*** to CalPERS.

Sincerely,

Membership Services

Enclosures: List of Qualifying Public Retirement Systems in
California Reciprocal Self-Certification Form (PERS-EAMD-801)

List of Qualifying Public Retirement Systems in California

Name of County/Agency/System:	Qualification(s):
Alameda County^	
City and County of San Francisco*	
City of Concord*	
City of Costa Mesa*	Safety Employees only
City of Fresno	Miscellaneous and Safety Retirement systems
City of Los Angeles	Non-Safety only
City of Oakland	Non-Safety only
City of Pasadena	Fire and Police Only
City of Sacramento*	
City of San Clemente*	Non-Safety only
City of San Diego	
City of San Jose	
Contra Costa County^	
Contra Costa Water District	
County of San Luis Obispo	
East Bay Municipal Utility District	
East Bay Regional Park District	Safety Employees only
Fresno County^	
Imperial County^	
Judges' Retirement System	
Kern County^	
Legislators' Retirement System	
Los Angeles County Metropolitan Transportation Authority	Non-Contract Employees' Retirement Income Plan, formerly Southern California Rapid Transit District
Los Angeles County^	
Marin County^	
Mendocino County^	
Merced County^	
Orange County^	
Sacramento County^	
San Bernardino County^	
San Diego County^	
San Joaquin County^	
San Mateo County^	
Santa Barbara County^	
Sonoma County^	
Stanislaus County^	
State Teachers' Retirement System	
Tulare County^	
University of California Retirement System	
Ventura County^	

*=Also CalPERS-covered agency ^=1937 Act Counties

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RECIPROCAL SELF-CERTIFICATION FORM

Complete the following information and return this form to your Personnel Office ***within 10 business days***

Employee Name	(Last)	(First)	(Middle)
Date of Birth:		CalPERS ID:	

Check the applicable statement:

☐ I have not been a member of a qualifying Public Retirement System in California.

☐ I have prior membership under another Public Retirement System in California. *(Complete the box below with verified dates including month, date, and year.* ***If you are unsure of the dates, please contact the Public Retirement System to confirm information prior to completing form****.)*

Name of Most Recent Reciprocal System:	Membership Date:	Separation Date*:	☐ Retired* ☐ Refunded* Date:
Name of Prior Reciprocal System:	Membership Date:	Separation Date*:	☐ Retired* ☐ Refunded* Date:
Name of Prior Reciprocal System:	Membership Date:	Separation Date*:	☐ Retired* ☐ Refunded* Date:

**Please provide dates, if applicable. Not all sections may be applicable for each Reciprocal System.*

I understand that by accepting employment in a qualified retirement system, I am subject to the applicable laws and regulations of that system. I also understand that completing this form does not constitute a request to establish reciprocity.

I hereby certify that the foregoing information has been verified as true and correct and any information found to be incorrect may require corrections to my account in the California Public Employees' Retirement System including, but not limited to, my retirement enrollment level. CalPERS may make any necessary corrections to my account to ensure I am properly enrolled and eligible to receive the correct retirement benefits.

_____ _____

Employee Signature Date

TO BE COMPLETED BY EMPLOYER ONLY:

Name of CalPERS Agency:	CalPERS Business Partner ID:	Employee's CalPERS Original Hire Date:
Designee of Employer: (Print Name) (Title)		Employee's CalPERS Membership Eligibility Date:
Designee's Signature:		(Date)

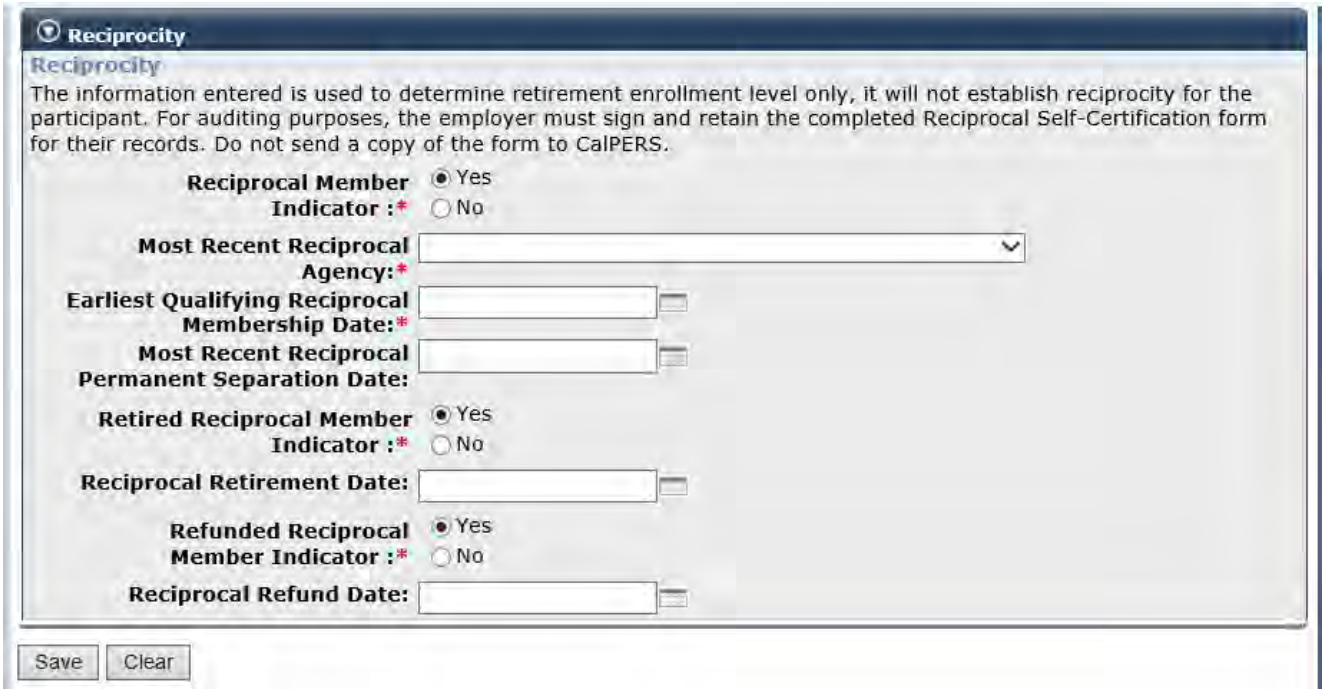
The employer must retain this form in the employee's file for auditing purposes.

RECIPROCAL SELF-CERTIFICATION FORM INSTRUCTIONS (EMPLOYER)

1. Employers must provide the Reciprocal Self-Certification Form to all employees upon membership.

2. Employers must sign and date the Reciprocal Self-Certification Form once received back from employee.

3. The employer must enroll the employee into my|CalPERS utilizing the information provided on the Reciprocal Self-Certification Form. If the employee indicates they are a prior member of a qualifying Public Retirement System in California, be sure to complete the data fields in the Reciprocity panel in my|CalPERS. Please enter the permanent separation date, retirement date, or refund date, if applicable, as provided by the member. No CalPERS data should be entered on the reciprocity panel as all CalPERS data is already stored in my|CalPERS.



4. The proper retirement benefit formula will be automatically determined by my|CalPERS. If you believe the retirement benefit formula is incorrect, you may contact CalPERS at **(888) 225-7377**.

5. It is the responsibility of the employer to retain the completed Reciprocal Self-Certification Form in the employee's employment records for auditing purposes. **Do not send a copy of the form to CalPERS.**

Privacy Notice

The privacy of personal information is of the utmost importance to CalPERS. The following information is provided to you in compliance with the Information Practices Act of 1977 and the Federal Privacy Act of 1974.

Information Purpose

The information requested is collected pursuant to the Government Code (sections 20000 et seq.) and will be used for administration of Board duties under the Retirement Law, the Social Security Act, and the Public Employees' Medical and Hospital Care Act, as the case may be. Submission of the requested information is mandatory. Failure to comply may result in CalPERS being unable to perform its functions regarding your status.

Please do not include information that is not requested.

Social Security Numbers

Social Security numbers are collected on a mandatory and voluntary basis. If this is CalPERS' first request for disclosure of your Social Security number, then disclosure is mandatory. If your Social Security number has already been provided, disclosure is voluntary. Due to the use of Social Security numbers by other agencies for identification purposes, we may be unable to verify eligibility for benefits without the number.

Social Security numbers are used for the following purposes:

1. Enrollee identification
2. Payroll deduction/state contributions
3. Billing of contracting agencies for employee/employer contributions
4. Reports to CalPERS and other state agencies
5. Coordination of benefits among carriers
6. Resolving member appeals, complaints, or grievances with health plan carriers

Information Disclosure

Portions of this information may be transferred to other state agencies (such as your employer), physicians, and insurance carriers, but only in strict accordance with current statutes regarding confidentiality.

Your Rights

You have the right to review your membership files maintained by the System. For questions about this notice, our Privacy Policy, or your rights, please write to the CalPERS Privacy Officer at 400 Q Street, Sacramento, CA 95811 or call us at 888 CalPERS (or 888-225-7377).

CALSTRS
HOW WILL YOU SPEND YOUR FUTURE?

Employer Information Circular

Volume 33; Issue 2 **February 22, 2017**

PENSION PLAN LIMITS FOR TAX YEAR 2017

The purpose of this circular is to alert employers that the Internal Revenue Service has announced the pension plan limits for tax year 2017 and to inform employers of the creditable compensation limit under the Teachers' Retirement Law for California State Teachers' Retirement System (CalSTRS) members and participants who are subject to the California Public Employees' Pension Reform Act of 2013 (PEPRA). The following limits apply to benefits paid and compensation creditable to the Defined Benefit (DB), the Defined Benefit Supplement (DBS) and the Cash Balance (CB) Benefit programs. CalSTRS is not authorized to give tax advice; accordingly, if you have any questions about these or any other Internal Revenue Code (IRC) sections, please contact your tax advisor or the Internal Revenue Service.

Internal Revenue Code Section 401(a)(17) Compensation Limit

IRC section 401(a)(17) limits creditable compensation that may be counted toward a CalSTRS retirement benefit for all persons who became a CalSTRS DB member or CB participant on or after July 1, 1996.

The compensation limit in effect from July 1, 2016, through June 30, 2017, is $265,000. The compensation limit for July 1, 2017, through June 30, 2018, is $270,000.

If you have an employee who will earn compensation in excess of this limit *and* the employee became a CalSTRS member or participant on or after July 1, 1996, please contact your CalSTRS Member Account Services representative for reporting instructions. Employer and member contributions to the DB, DBS and CB Benefit programs should not be taken on the excess amount.

Creditable Compensation Limit for CalSTRS 2% at 62 Members and CB Participants Subject to the California Public Employees' Pension Reform Act of 2013

The California Public Employees' Pension Reform Act of 2013 (PEPRA) limits creditable compensation that may be counted toward a CalSTRS retirement benefit for all CalSTRS members and CB participants subject to PEPRA. All persons first hired on or after January 1, 2013, are subject to PEPRA and are known as CalSTRS 2% at 62 members and CB participants subject to PEPRA.

The creditable compensation limit is applicable to compensation creditable to the DB, DBS and CB Benefit programs combined and is based on 120 percent of the 2013 Social Security contribution and benefit base, adjusted annually for changes to the Consumer Price Index for All Urban Consumers: U.S. City Average.

The creditable compensation limit for CalSTRS 2% at 62 members and CB participants subject to PEPRA for July 1, 2016, through June 30, 2017, is $139,320.

If you have an employee who will earn creditable compensation in excess of this limit, please contact your CalSTRS Member Account Services representative for reporting instructions. Employer and member contributions to the DB, DBS and CB Benefit programs should not be taken on the excess amount.

CalSTRS will publish a separate employer information circular to inform employers of the compensation limits for CalSTRS 2% at 62 members and CB participants subject to PEPRA that will be effective July 1, 2017.

Internal Revenue Code Section 415(b) Retirement Benefit Limit

IRC section 415(b) is a federal statutory provision that limits the amount of annual retirement benefit that may be received from a tax-qualified pension plan and applies to all DB members and CB participants. The annual retirement benefits payable from CalSTRS retirement plans are subject to the dollar limits imposed by IRC section 415(b).

The limitation on the annual benefit for CalSTRS 2% at 60 members or participants, age 65, who participate in the DB or CB Benefit programs is $183,781 for the 2017 calendar year.

The limit is actuarially adjusted for retirement before and after age 65. For example, the 2017 limit for CalSTRS 2% at 60 members age 55 with less than 30 years of service is $109,041; the 2017 limit for CalSTRS 2% at 60 members at age 55 with more than 30 years of service is $109,776; and the 2017 limit for CalSTRS 2% at 60 members age 70 is $187,826.

Any benefits due to members and participants in excess of this limit are payable from the Replacement Benefits Program administered by CalSTRS. No action is required by employers to initiate payment of benefits under the Replacement Benefits Program. However, under federal law, if members or participants were paying the Medicare Part A payroll tax when employed, payments from the Replacement Benefits Program will also be subject to the payroll tax deduction. CalSTRS will work with the member regarding any tax deductions under this part.

CalSTRS 2% at 62 members and CB participants subject to PEPRA are not eligible for the Replacement Benefits Program.

If you have any questions regarding this circular, please contact your CalSTRS Member Account Services representative.

California Public Employees' Retirement System
P.O. Box 942715 | Sacramento, CA 94229-2715
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Payroll

Circular Letter

January 16, 2018
Circular Letter: 200-001-18
Distribution: IV, V, VI, X, XII, XVI

To: **All CalPERS Employers**
Subject: **2018 Compensation Limits for Classic and New Members**

Purpose

The purpose of this Circular Letter is to update your agency on the 2018 compensation limits for Classic and Public Employees' Pension Reform Act (PEPRA) members. These guidelines provide information 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 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 PEPRA members who are subject to the compensation limit requirements.

Compensation Limit

The compensation limit for classic members for the 2018 calendar year is $275,000.
Employees with membership dates prior to July 1, 1996, are not impacted by these limits.

The compensation limits for classic members during 2014-17 are:

2017	2016	2015	2014
$270,000	$265,000	$265,000	$260,000

The compensation limit for new members for the 2018 calendar year is:

Year	Social Security Participants	Non-Social Security Participants
2018	$121,388	$145,666

The compensation limits for new members during 2014-17 are:

Year	Social Security Participants	Non-Social Security Participants
2017	$118,775	$142,530
2016	$117,020	$140,424
2015	$117,020	$140,424
2014	$115,064	$138,077

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

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Date: May 3, 2004
Reference No.:
Circular Letter No.: 200-154-04
Distribution: **I, VI, XII, XVI**
Special:

Circular Letter

TO: ALL PUBLIC AGENCIES

SUBJECT: METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA v. SUPERIOR COURT OF LOS ANGELES ["CARGILL" (2004) 32 Cal. 4th 491]

This Circular Letter further addresses the above court case discussed in our earlier Circular Letters of 200-064 dated July 24, 2000, and 200-043 dated March 19, 2001.

The Supreme Court of California has now issued its decision in this case. With respect to California Public Employees' Retirement System (CalPERS), the Court reached the following conclusions:

- "We conclude, as did the lower courts, that the PERL incorporates common law principles into its definition of a contracting agency employee and that **the PERL requires contracting public agencies to enroll in CalPERS all common law employees** except those excluded under a specific statutory or contractual provision." (Emphasis added; "PERL" is the Public Employees' Retirement Law, Government Code Section 20000 et seq.)

- "…the PERL contains no broad exclusion for long-term, full-time workers hired through private labor suppliers."

- "Nor, of course, has the Legislature provided in the PERL for any coemployment exception to a contracting agency's duty to enroll employees in CalPERS."

The court also found that the definition of "employee" in Government Code Section 20028 does **not** require that the funds used to pay employees of a contracting agency be directly controlled by the contracting agency. Common law employees of a contracting agency must be enrolled in CalPERS regardless of the source of the funds used to pay them. Thus, unless otherwise excluded by law or by contract with CalPERS, a person deemed a common law employee of a contracting agency must be enrolled in CalPERS.

Government Code Section 20125 provides that the CalPERS' Board of Administration "shall determine who are employees and is the sole judge of the conditions under which persons may be admitted to and continue to receive benefits under this system." The

common law rules used by CalPERS for determining employee status can be found at the following URLs:

http://www.irs.gov/pub/irs-pdf/p15a.pdf (starting from page 3)

http://www.irs.gov/pub/irs-pdf/p963.pdf (starting from page 21)

The common law rules for determining whether a worker is an employee may also be used to distinguish "independent contractors" from "employees." In that regard, the CalPERS' Procedures Manual defines an "independent contractor" as follows:

> "An independent contractor is someone who contracts to do a piece of work according to his/her own methods, and is subject to his/her employer's control only as to the **end product or final result** of work, and not as to the means and manner in which the work is performed." (Page 2.6)

Factual questions may ultimately exist as to whether a person is an employee under the established common law rules. To facilitate this determination, employers should maintain documentation substantiating whether a person meets the definition of a common law employee.

QUESTIONS

Will the provisions of Government Code Section 20283 be applied to employers?

Government Code Section 20283 states: "Any employer that fails to enroll an employee into membership when he or she becomes eligible, or within 90 days thereof, when the employer knows or can reasonably be expected to have known of that eligibility shall be required to pay all arrears costs for member contributions and administrative costs of five hundred dollars ($500) per member as a reimbursement to this system's current year budget."

The provisions of Government Code Section 20283 will be applied to contracting agencies on a case-by-case basis, depending on the individual circumstances relevant to each contracting agency.

Is the ruling to be applied retroactively?

CalPERS has concluded that a common law employee of a contracting agency not otherwise excluded from CalPERS enrollment by law or contract must be enrolled into membership retroactive to the original date of qualification. In cases where a person is deemed a common law employee and is no longer employed with a contracting agency, the employer must nevertheless submit a Member Action Request (AESD-1) form for the employee. This form should indicate:

- Box 10 (Effective Date of Action) – The date the employee should have qualified for CalPERS membership. (If unknown, enter the date this person was hired.)
- Box 8 (Remarks) – Enter the date the person separated from your employment.

CalPERS will determine whether any retroactive retirement contributions for the employee are necessary and will notify subsequently affected employers as necessary.

Can agencies request a contract exclusion of "leased" workers, or workers with a genuine "co-employment" relationship?

Requests for exclusions of leased or "co-employed" employees will be reviewed for compliance with the standards for contract exclusions that were approved in 1997 by the CalPERS' Board of Administration. A copy of these standards is attached to this Circular Letter for your reference.

Kenneth W. Marzion, Chief
Actuarial and Employer Services Division

Attachment

STATE OF CALIFORNIA
BOARD OF ADMINISTRATION
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

RESOLUTION

Subject: **Procedure and Guidelines for Determining Future Public Agency Contract Exclusions** No. MSD-97-01

WHEREAS, 1. The purpose of the Public Employees' Retirement Law, Government Code section 20000 et seq., as stated in section 20001, is to provide a retirement system for public service employees.

2. For purposes of the Public Employees' Retirement Law, the term "employee" is defined in Government Code section 20028(b) to include any person in the employ of any contracting agency.

3. The California Constitution, article XVI, section 17 provides that the CaIPERS Board has plenary authority and fiduciary responsibility for administration of the CaIPERS system.

4. The California Constitution, article XVI, section 17, and Government Code section 20151 provide that the CaIPERS Board must exercise its authority and duties subject to its fiduciary obligations to its participants and beneficiaries, and that the Board's duty to its participants and beneficiaries takes precedence over any other duty.

5. Government Code section 20120 provides that management and control of the CaIPERS system is vested in the CaIPERS Board.

6. Government Code section 20121 provides that the CaIPERS Board may make such rules as it deems proper.

7. Government Code section 20460 provides that public agencies may contract with the CaIPERS Board to participate in CaIPERS and make all or part of their employees members of the system.

8. Under the statutory scheme set forth in the Public Employees' Retirement Law, specifically Government Code sections 20300 et seq. and 20502, all employees of a contracting agency are mandated into CaIPERS membership unless they are excluded either by statute or by a contractual provision.

9. Government Code section 20502 provides that contractual exclusions of public agency employees shall be based on groups of employees such as departments or duties, and not on individual employees, and further that the CaIPERS Board may disapprove the exclusion of any group, if in its opinion the exclusion adversely affects the interest of the system.

10. Government Code section 20305 sets forth the specific situations in which employees serving on less than a full-time basis are excluded from CaIPERS, and further provides that except as provided in section 20502, no contract or contract amendment entered into after January 1, 1981, shall contain any provision excluding persons on an irregular employment basis.

11. Government Code section 20460 et seq. provides for a specific process for the execution of and amendments to contracts between CaIPERS and public agencies.

12. Government Code section 20460 et seq. anticipates generally the involvement of employees and recognized employee representatives in situations relating to the adoption and amendment of public agency contracts with CaIPERS.

THEREFORE, BE IT RESOLVED THAT,

A. In determining whether to approve future public agency contract exclusions pursuant to Government Code section 20502, either in a new contract or through amendment to an existing contract, the CaIPERS Board shall follow the Procedures and Guidelines set forth in Attachment A to this Resolution.

B. The CaIPERS Board delegates to the Chief Executive Officer the authority to implement this Resolution.

C. This Resolution shall be effective immediately.

** *** * * * *

I hereby certify that on the 16th day of April, 1997, the Board of Administration of the Public Employees' Retirement System made and adopted the foregoing Resolution.

/S/

_____

WILLIAM DALE CRIST, PRESIDENT
BOARD OF ADMINISTRATION
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

I understand and accept this delegation.

/S/

4/22/97 .
Date

_____

JAMES E. BURTON
CHIEF EXECUTIVE OFFICER
PUBLIC EMPLOYEES' RETIREMENT SYSTEM

ATTACHMENT A

PROCEDURE AND GUIDELINES FOR DETERMINING FUTURE CONTRACT EXCLUSIONS

APPLICABILITY

These procedures and guidelines apply to requests by public agencies (as defined in Government Code section 20025) that are either: seeking to contract with CaIPERS for coverage for their employees and wish to exclude part of their employees from membership; or, are seeking to amend their existing contract for CaIPERS coverage to exclude certain future employees.

PROCEDURE

The public agency shall submit to the CaIPERS Member Services Division a written request specifying the group of employees it wishes to exclude. The request must include:

- A detailed explanation of the group of employees the agency wishes to exclude, including a description of the type of employees who normally would fall within the group and an explanation, with supporting documentation (including job descriptions and class specifications), of why the employees are considered non-career employees. (See Guidelines.)

- A statement that the public agency has, in compliance with California law, notified the pertinent recognized employee organizations of its request to exclude certain groups of employees, or in the case where there is no pertinent recognized employee organization, has posted (in a conspicuous location frequented by its employees) a notice of its intent to exclude certain groups of employees.

CaIPERS will review the public agency's request based on the guidelines set forth below. When appropriate, CaIPERS will request additional information from the public agency. The employee organizations may also submit information. After receiving all necessary information and reviewing the request in light of the guidelines, CaIPERS will, as quickly as is administratively possible, issue a written determination letter to the public agency and the responding employee organizations that approves or disapproves the contract exclusion.

In the case of either a new public agency contract or an amendment to an existing contract, the public agency must complete the statutory process set forth in Government Code section 20460 et seq. to implement the contract or amendment. An employer or employee organization representing the affected employees who is dissatisfied with the Member Services Division determination, may seek further review by, within 30 days of the date of the determination letter, submitting a written request to the CaIPERS Chief Executive Officer. Upon receipt of such a request, the Chief Executive Officer will convene a three-person panel, consisting of the

Chief Actuary, the Assistant Executive Officer - Member and Benefit Services, and the General Counsel. This panel will consider the original request, the Member Services Division's determination, any additional written arguments submitted, and oral presentations if requested by the parties or desired by the panel. An employer who is dissatisfied with the review panel's determination may seek further review by, within 30 days of the review panel's determination letter, submitting a written request to the Chief Executive Officer. The Chief Executive Officer will place the matter on the agenda for the next administratively-feasible meeting of the Benefits and Program Administration Committee. The Benefits and Program Administration Committee will review the issue based upon written materials submitted and will make a recommendation to the Board. The Board's decision will be final.

GUIDELINES FOR REVIEWING PROPOSED CONTRACT EXCLUSIONS

In reviewing public agency requests for contract exclusions, CalPERS will apply the guidelines set forth below on a case-by-case basis. Based on its review of the request in light of these guidelines, CalPERS will determine whether to approve the contract exclusion.

No single factor is necessarily dispositive. **In making its determination, CalPERS shall consider all the factors and circumstances as a whole.**

1. The exclusion must be based on a "group" of employees.
(Note, the definition of "group or class of employment" located in Government Code section 20023(e) is not controlling for this purpose.)

- The group of employees to be excluded must be clearly defined. Specifically, CalPERS must be able to ascertain which employees are in the group. Further, the group must be clearly defined so that it is not possible for the employer arbitrarily to move employees in and out of the group.

- The employees in the group must share some common characteristic. These characteristics may include, for example, department, duties, or job classification.

- Consistent with Government Code section 20305, the defining characteristic of a group may not be irregular employment status. For example, the exclusion may not be for "temporary" or "seasonal" employees.

- As provided in Government Code section 20502, exclusions must be based on groups of employees such as departments or duties, and not on individual employees.

2. The exclusion must not adversely affect the interests of the system.

CaIPERS will review the proposed exclusion to determine whether it adversely affects the interests of the system. This review will include an exploration of the possible impacts of the exclusion on the system's various administrative and operational interests, as well as an analysis of whether the exclusion is consistent with CaIPERS' purpose to provide a retirement system for employees who become superannuated or otherwise incapacitated.

In considering the impact of the proposed exclusion on CaIPERS' administrative and operational interests, CaIPERS will consider factors including the following:

- Whether any unreasonable administrative burden or cost would be required for CaIPERS to implement the exclusion.
- Whether the exclusion is sufficiently defined so as to enable CaIPERS, through its normal audit process, to monitor the agency for contract compliance.
- Whether the exclusion might lead to disqualification of the plan for failure to satisfy Internal Revenue Code qualification requirements.
- Whether the exclusion would violate any applicable federal or state provisions.
- Whether, from an administrative or operational perspective, the proposed exclusion has other adverse effects on the system.

CaIPERS will also consider the proposed exclusion in light of the purpose of the Public Employees' Retirement Law, as set forth in Government Code section 20001, specifically to provide a retirement system for employees who become superannuated or otherwise incapacitated. As a general guideline, the exclusion of groups of employees who are career employees, or could reasonably be anticipated to become career employees, is not consistent with the purpose of the Public Employees' Retirement Law. To determine whether the group under consideration for exclusion consists of non-career employees, CaIPERS will consider factors including the following.

- The types of employees who generally fall within the group. For example, does the group consist of employees in a position generally held by retirees or students? (For example, Crossing Guard positions are often held by retirees; bookstore positions are often held by students.)
- Whether the group consists of employees in a training position, at the end of which it is anticipated that they will seek employment elsewhere. (These types of positions are often established in connection with a program affiliated with a facility of higher education.)

- Whether the group consists of employees in an intern position which is part of an approved study plan or a graduation requirement (e.g., a medical internship).

- Whether the group consists of employees in a department or classification for which there is no established career path or promotional ladder leading to classifications where employees are CaIPERS members.

- The manner in which funding is provided for the positions that fall within the group. For example, is funding established on a short-term basis or are the affected positions permanently budgeted?

- For employers that operate under a civil service system, whether the group consists of employees who are in non-civil service positions.

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CLASSIC VS. PEPRA NEW MEMBER SCHOOL SCENARIOS

CalPERS Membership Scenarios			
SCENARIO	**CLASSIC**	**PEPRA**	**NOTES**
CalPERS School Member prior to 1/1/13, becomes employed with ANY School/County Office of Education (COE) either WITHIN or AFTER 6 months	X		Regains Classic due to same employer rule
CalPERS School Member prior to 1/1/13, becomes employed with a State or Public Agency (PA) WITHIN 6 months	X		Regains Classic due to movement within 6 months
CalPERS School Member only prior to 1/1/13 becomes employed with a State or PA AFTER 6 months		X	No prior membership at new employer
CalPERS School member prior to 1/1/13, refunds contributions terminating membership, returns to membership with CalPERS WITHIN or AFTER 6 months with ANY School/COE	X		Only prior membership with a school is required even if refunded
CalPERS School member prior to 1/1/13, refunds contributions terminating membership, returns to membership with CalPERS WITHIN 6 months with a State or PA	X		Regains Classic due to movement within 6 months
CalPERS School member only prior to 1/1/13, refunds contributions terminating membership, returns to membership with CalPERS AFTER 6 months with a State or PA		X	No prior membership at new employer

Rev. 09/16/2016

CLASSIC VS. PEPRA NEW MEMBER SCHOOL SCENARIOS

CalPERS Membership Scenarios			
SCENARIO	**CLASSIC**	**PEPRA**	**NOTES**
CalPERS State or PA member prior to 1/1/13, becomes employed with a School/COE WITHIN 6 months	X		Regains Classic due to movement within 6 months
CalPERS State or PA member prior to 1/1/13, becomes employed with a School/COE AFTER 6 months		X	More than a 6 month break to a different employer; no prior membership with any School/COE employer

CalPERS Retired Membership Scenarios			
SCENARIO	**CLASSIC**	**PEPRA**	**NOTES**
CalPERS School member only prior to 1/1/13, retires and reinstates back to ANY School/COE WITHIN and AFTER 6 months	X		Regains Classic due to same employer rule
CalPERS School member ONLY prior to 1/1/13, retires and reinstates back to a State or PA WITHIN 6 months	X		Regains Classic due to movement within 6 months
CalPERS School member only prior to 1/1/13, retires and reinstates back to a State or PA AFTER 6 months		X	More than a 6 month break to a different employer; no prior membership at new employer

CLASSIC VS. PEPRA NEW MEMBER SCHOOL SCENARIOS

CalPERS Non-Membership Scenarios			
SCENARIO	**CLASSIC**	**PEPRA**	**NOTES**
Part-time School employee prior to 1/1/13, becomes a CalPERS member with a School/COE on or after 1/1/13		X	Is only an employee prior to 1/1/13, no membership ever established in CalPERS until after 1/1/13
Part-time State or PA employee prior to 1/1/13, becomes a CalPERS member through with a School/COE on or after 1/1/13		X	Is only an employee prior to 1/1/13, no membership ever established in CalPERS until after 1/1/13
Part-time School, State or PA employee prior to 1/1/13 with previously refunded CalPERS membership with a School/COE, becomes a CalPERS member with a School/COE on or after 1/1/13.	X		Due to previous Classic CalPERS membership with same employer, even if refunded.
Part-time School, State or PA employee prior to 1/1/13 with previously refunded CalPERS membership with a State or PA, becomes a CalPERS member with a School/COE on or after 1/1/13.		X	No prior membership at new employer

CLASSIC VS. PEPRA NEW MEMBER SCHOOL SCENARIOS

Reciprocal Scenarios			
SCENARIO	**CLASSIC**	**PEPRA**	**NOTES**
Other Reciprocal Public Retirement System[1] or CalSTRS member prior to 1/1/13, becomes employed in a position with a School/COE, State or PA reportable to CalPERS resulting in membership WITHIN 6 months	X		Regains Classic due to movement within 6 months
Other Reciprocal Public Retirement System or CalSTRS member prior to 1/1/13, becomes employed in a position with a School/COE, State or PA reportable to CalPERS resulting in membership AFTER 6 months		X	No prior CalPERS membership with same employer
CalSTRS member prior to 1/1/13, continues employment subject to coverage with CalSTRS, becomes employed in a different position with a School/COE, State or PA reportable to CalPERS resulting in membership in CalPERS; concurrent membership	X		Moved within 6 months. Concurrent membership is allowed with CalSTRS and CalPERS as long as they are different positions
Other Reciprocal Public Retirement System or CalSTRS member prior to 1/1/13, terminates membership and refunds contributions, becomes employed in a position with any School/COE, State or PA reportable to CalPERS resulting in membership WITHIN or AFTER 6 months		X	Due to termination of membership in Other Reciprocal Public Retirement System or CalSTRS, no longer "subject to reciprocity" [2]
Other Reciprocal Public Retirement System or CalSTRS member prior to 1/1/13, retires then becomes employed in a position with a School/COE, State or PA reportable to CalPERS resulting in membership WITHIN or AFTER 6 months		X	Due to retirement, no longer "subject to reciprocity".

[1] 1937 Act County, Public Agency Retirement Systems, and UCRP

[2] CalSTRS is a non-reciprocal public retirement system. However, for the purposes of PEPRA movement between systems must be within 6 months to be considered "subject to reciprocity".

Other Reciprocal Public Retirement System or CalSTRS member prior to 1/1/13, becomes employed in a part-time School/COE, State or PA position reportable to CalPERS, reaches 1000 hours attaining membership AFTER 6 months	X		The PERL allows for employment that leads to membership to be used to establish reciprocity as long as it begins within 6 months after separation from the last system.
Other Reciprocal Public Retirement System or CalSTRS member prior to 1/1/13, becomes employed in a position with a School/COE, State or PA reportable to CalPERS resulting in membership WITHIN 6 months. Then later retires from the other Public Retirement System or CalSTRS	X		As long as the member is "subject to reciprocity"[3] or the "applicable date"[4]

[3] California Code of Regulations 579.3
[4] California Code of Regulations 579.3 (b)

CLASSIC VS. PEPRA NEW MEMBER SCHOOL SCENARIOS

Complex Scenarios – Result in Multiple Member Enrollment Levels			
SCENARIO	**CLASSIC**	**PEPRA**	**NOTATIONS**
CalPERS School Member prior to 1/1/13;	X		Classic member employed prior to 1/1/13
Separates from employment at School/COE then AFTER 6 months separation is employed by a State of PA employer;		X	This employment is subject to PEPRA due to no prior employment at new agency
Subsequently, returns back to employment with ANY School/COE employer AFTER 6 months;	X		Regains Classic due to same employer rule
Then is employed with State or PA WITHIN 6 months	X		Moved within 6 months eligible to retain Classic membership from last employment
State Member retires 12/31/12;	X		Classic member employed prior to 1/1/13
Works one year as a Retired Annuitant (RA) for the State then reinstates into CalPERS membership through a School/COE WITHIN 6 months of leaving the RA employment		X	RAs are not enrolled into CalPERS membership. The reinstatement to the new employer is greater than 6 months from the date of initial retirement and with a different employer; no prior School/COE employment at new agency

State Member retires 12/31/12; Works one year as a Retired Annuitant (RA) for a School/COE, then reinstates into CalPERS membership through ANY School/COE WITHIN 6 months of leaving the RA employment	X	X	Classic member employed prior to 1/1/13 RAs are not enrolled into CalPERS membership. Although the reinstatement is with the same employer it is greater than 6 months from the date of initial retirement
CalPERS School member retires prior to 12/31/12; Works one year as a Retired Annuitant (RA) for a School/COE, then reinstates into CalPERS membership through ANY School/COE WITHIN 6 months of leaving the RA employment	X		Classic member employed prior to 1/1/13 RAs are not enrolled into CalPERS membership. However, the reinstatement is with the same employer even if it is greater than 6 months from the date of initial retirement enter Classic membership upon return same employer.
CalPERS School member prior to 1/1/13, after 1/1/13, becomes concurrently employed in another position eligible for membership	X		As long as movement between CalPERS employers is within 6 months even overlapping the member maintains previous membership status.

Publications

Federal-State Reference Guide

A Federal-State Cooperative Publication

- **Social Security Administration**
- **Internal Revenue Service**
- **National Conference of State Social Security Administrators**

Providing guidelines for social security and Medicare coverage and tax withholding requirements for state, local and Indian tribal government employees and public employers.

Publication 963 (Rev. 11-2014) Catalog Number 21843B Department of the Treasury I**nternal Revenue Service** www.irs.gov

Introduction

The *Federal-State Reference Guide* provides state and local government employers a comprehensive reference source on social security and Medicare coverage and federal tax withholding issues. The *Guide* was first published by the Internal Revenue Service (IRS) in July 1995 with special assistance from the State of Colorado, and is a cooperative effort of the Social Security Administration, the IRS, and the National Conference of State Social Security Administrators (NCSSSA). Topics addressed in this publication include determination of worker status, public retirement systems (FICA replacement plans), social security and Medicare coverage and benefits, Section 218 Agreements, employment tax laws, and other tax issues. The tax information is generally applicable to federal agencies, with some exceptions; for example, Section 218 Agreement information and section 530 relief are not applicable to federal agencies.

Since 2002, the IRS office of Federal, State and Local Governments (FSLG) has produced the *Federal-State Reference Guide* annually, primarily as a web-based document. FSLG was created as part of the reorganization of the IRS, to be an office devoted exclusively to the federal tax needs of governmental entities. The most recent version of Publication 963 can be downloaded at any time from the FSLG website. This website also contains information about other related tax topics, upcoming events, the FSLG Newsletter, and the IRS. All IRS forms and publications referred to in this publication can be ordered without charge from the IRS at (800) 829-3676, or can be downloaded from the IRS website. Governmental taxpayers may get assistance with general or account-related questions by calling Customer Account Services at (877) 829-5500, Monday through Friday.

This publication also includes information to assist Indian tribal governments. Federal tax law establishes the role of Indian tribal governments as employers. Tribal governments are required to follow substantially the same procedures as other employers; however, tribes are not eligible for Section 218 Agreements, and other special statutory provisions apply to these entities. If you have questions about Indian Tribal governments, please visit the office of Indian Tribal Governments (ITG) website or telephone your local IRS ITG office. This website also contains Publication 4268, *Employment Tax Desk Guide,* containing further information that specifically addresses employment tax issues for tribal governments.

Frequently asked questions appear at the end of each chapter. After each answer, the primary contact for the topic is indicated - "IRS," "SSA," or "STATE".

The *Federal-State Reference Guide* is for informational and reference purposes only. Under no circumstances should the content be used or cited as authority for assuming, or attempting to sustain, a technical position with respect to employment tax, social security benefits, or other legal issues. The Internal Revenue Code (IRC), Social Security Act (Act) and related regulations, rulings and case law are the only valid citations of authority for technical matters.

Contents

Chapter 1

Social Security and Government Employers

Federal tax requirements generally apply to public employers in the same way that they do to private employers. However, there are some differences arising from the unique history of laws governing social security and Medicare coverage for state and local government employees. Special provisions apply to the application of these taxes as well as certain withholding requirements.

Historical Overview

Social security taxes were first collected in 1937. The funding mechanism for the social security program was officially established in the Internal Revenue Code (IRC) as the Federal Insurance Contributions Act (FICA). Under the original Social Security Act of 1935, state and local government employees were excluded from social security coverage because of unresolved legal questions regarding the federal government's authority to impose taxes on state and local governments and their employees.

Beginning in 1951, states were allowed to enter into voluntary agreements with the federal government to provide social security coverage to public employees. These arrangements are called "Section 218 Agreements" because they are authorized by Section 218 of the Social Security Act. Originally, government entities filed with the SSA, but since 1987, the IRS has been responsible for collecting these taxes from governmental employers. All 50 states, Puerto Rico, the Virgin Islands, and approximately 60 interstate instrumentalities have Section 218 Agreements with SSA, providing varying degrees of coverage for employees in the state.

Social security coverage of government employees varies greatly from state to state. In 26 states, at least 90% of state and local government employees work in positions covered by social security. By contrast, in California, Colorado, Louisiana, Nevada, and Texas, less than half of state and local government employees are covered. As of 2008, 27.5%, of the state and local government workforce, or 6.6 million, state and local government employees, were not covered by social security.

The largest proportion of uncovered government employees work at the local level. The majority of uncovered local government public employees are police officers, firefighters and teachers. Approximately one-fourth of the nation's public employees are not covered for social security.

The following chart includes the major historical developments since state and local employees first became eligible for social security coverage in 1951.

Key Dates

January 1, 1951	Beginning this date, states could voluntarily elect social security coverage for public employees not covered under a public retirement system (FICA replacement plan) by entering into a Section 218 Agreement with SSA. Prior to this date, there was no mandatory social security coverage.
January 1, 1955	Beginning this date, states could extend social security coverage to employees (other than police officers and firefighters) covered under a public retirement system.
July 1, 1966	Beginning this date, employees covered for social security under a Section 218 Agreement are automatically covered for Medicare.
April 20, 1983	Beginning this date, coverage under a Section 218 Agreement cannot be terminated unless the governmental entity is legally dissolved.
April 1, 1986	State and local government employees hired on or after this date, not already covered, are mandatorily covered for Medicare, unless the position is specifically excluded by law. For state and local government employees hired before April 1, 1986, Medicare coverage may be elected under a Section 218 Agreement.
January 1, 1987	Beginning this date, State Social Security Administrators were no longer responsible for collecting social security contributions from public employers or for verifying and depositing the taxes owed by public employers. After 1986, public employers pay Federal Insurance Contributions Act (FICA) taxes directly to the Internal Revenue Service (IRS) in the same manner as do private employers.
July 2, 1991	Beginning this date, state and local government employees became subject to mandatory social security and Medicare coverage, unless they are (1) members of a qualifying public retirement system, or (2) covered under a Section 218 Agreement.
August 15, 1994	The Social Security Independence and Program Improvements Act of 1994 established the SSA as an independent agency, effective March 31, 1995. This Act also increased the FICA exclusion amount for election workers from $100 to any amount less than the threshold amount mandated by law in a calendar year. (To verify the current year amount, see the SSA website.) States were authorized to amend their Section 218 Agreements to increase the FICA exclusion amount for election workers to the statutorily mandated threshold. The Act also amended Section 218 of the Act to allow all states the option to extend social security and Medicare coverage to police officers and firefighters who participate in a public retirement system. (Under previous law, only 23 states were authorized to do so.)
October 21, 1998	Public Law 105-277 provided a 3-month period for states to modify their Section 218 Agreements to exclude from coverage services performed by students. This provision was effective July 1, 2000, for states that exercised the option to take this exclusion.
March 2, 2004	Public Law 108-203 enacted, requiring public employers to furnish Form SSA-1945 to public employees hired after December 31, 2004, informing them that they are earning retirement benefits not covered by social security; also closed the Government Pension Offset (GPO) loophole, effective April 1, 2004.

Key Public Employer Responsibilities

The following are the major responsibilities that apply to all public employers, regardless of their social security coverage and public retirement system:

- Properly classify workers as independent contractors or employees
- Solicit and collect valid taxpayer identification numbers from all employees and payees
- Determine which employees are exempt from social security and/or Medicare taxes
- Withhold, report and pay appropriate social security and Medicare taxes, or Medicare-only taxes, for each employee.
- Obtain clarifications of laws, regulations, and other appropriate information from State Social Security Administrators, IRS, and SSA.

Considerations for Social Security Coverage (Section 218 and Mandatory)

Social security coverage can vary widely within a state or even a local area. Do not make an assumption about Section 218 coverage for an entity and whether it is in compliance with all applicable laws merely because of the status of a similar entity, either in the same or a different state. For Section 218 coverage questions, contact your State Social Security Administrator (see www.ncsssa.org). For mandatory (non-section 218) coverage questions, contact an IRS FSLG Specialist (see www.irs.gov/govts for a directory). Related information can also be found at the SSA State and Local Government Employers website at http://www.ssa.gov/slge/sitemap.htm.

In general, to determine the correct coverage for a group of employees, a government employer must address the following questions:

If employees *are* covered by a Section 218 Agreement:

1. When did the state enter into a Section 218 Agreement to elect social security coverage for a particular political subdivision?
2. What optional exclusions and what coverage groups were listed in that Agreement or later modification?
3. Does the political subdivision have more than one modification?
4. Did the state or political subdivision terminate voluntary social security coverage, in its entirety or with respect to any coverage group(s), before April 20, 1983?
5. Has the state elected to provide Medicare-only for a particular entity?

If employees *are not* covered by a Section 218 Agreement:

1. Does the state or political subdivision have any employees who were hired prior to April 1, 1986, and who are exempt from mandatory Medicare?
2. Does the state or political subdivision have a public retirement system?* If so, employees who are qualified participants in the public retirement system are not subject to mandatory social security coverage that began July 2, 1991.

** Throughout this publication, the term "public retirement system"(or"FICA replacement plan") refers to a retirement system administered by a state, political subdivision, or instrumentality thereof that meets the requirements of section 3121(b)(7)(F) of the Internal Revenue Code. See Revenue Procedure 91-40 in the Appendix. For section 218 purposes, it is irrelevant whether the retirement system meets the minimum benefit standards for a qualified plan under the Employee Retirement Income Security Act (ERISA). See Chapter 6.*

***Note:** In some situations, legal challenges occur that are resolved in the federal courts. It is even possible that, while cases are pending, the application of the laws can vary and be applied by the IRS and SSA solely in one state (if a case has been heard and decided in a federal district court) or in states only in one federal circuit (if a case has been heard and decided at the federal circuit court level). It is important, therefore, in such situations to be aware of which federal district or circuit court has jurisdiction over federal laws that apply to each state. To locate a map and contact information for federal courts, go to: http://www.uscourts.gov/court_locator.aspx*

Steps To Determine Social Security and Medicare Coverage of State and Local Government Employees

State and local government employees may be covered for social security and Medicare under either a Section 218 Agreement, which applies to anyone holding the affected position; or under mandatory coverage, which is based on the situation of the individual employee.

If the position is covered under a Section 218 Agreement, any employee occupying that position is covered. This is the first coverage consideration for a governmental employer. If, however, the position is not covered under an Agreement, then the employer must determine whether mandatory FICA coverage applies. To do this, the employer must first determine whether the employee is deemed to be a member of a public retirement system (or "FICA replacement plan"). This is a critical consideration in determining whether and how Section 218 or mandatory FICA coverage applies to an employee.

The following steps outline how a public employer should determine whether social security and Medicare coverage or Medicare-only coverage applies to an employee.

Step 1: Determine whether the employee's position is covered by a Section 218 Agreement (Chapter 5, **Social Security and Medicare Coverage**.)* If the answer is "yes," the employee is covered for social security and Medicare under the Agreement, unless an exclusion applies for that position. If the answer is "no," proceed to the next step.

Step 2: If the employee's position is not covered under a Section 218 Agreement, determine whether the employee is a member of a public retirement system (Chapter 6, **Social Security and Public Retirement Systems**.) If "no," the employee is subject to mandatory social security and Medicare, unless an exclusion applies. If "yes" (the employee is a member of a public retirement system), the employee is exempt from mandatory social security. Medicare is mandatory for public employees hired or rehired after March 31, 1986, regardless of membership in a public retirement system. Proceed to the next step to determine Medicare coverage for any employee hired prior to April 1, 1986.

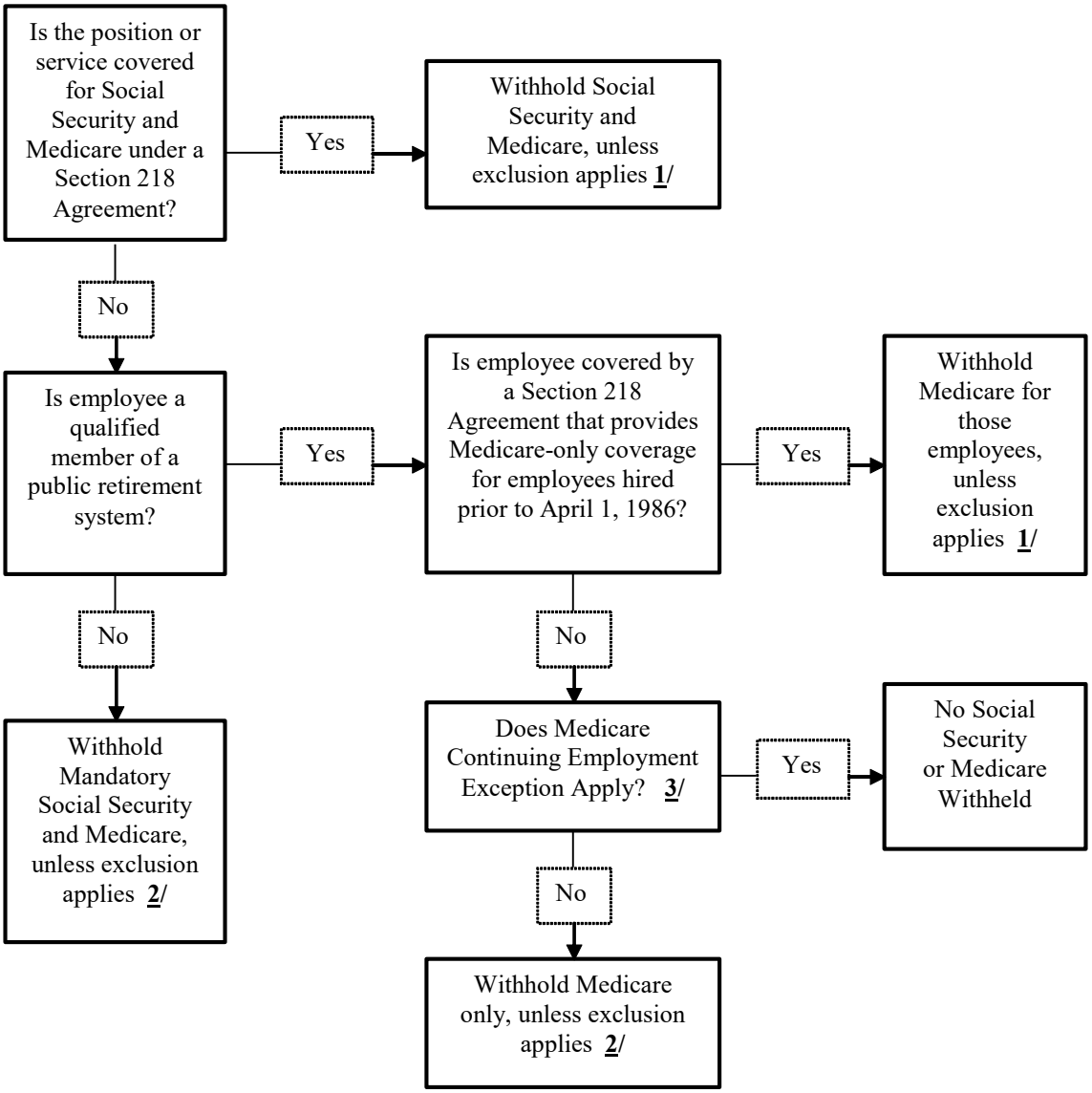
Step 3: Determine whether a Section 218 Agreement provides Medicare-only coverage for employees hired prior to April 1, 1986. If "yes," the employee is covered for Medicare only. If "no," proceed to the next step.

Step 4: Determine whether the Medicare continuing employment exception applies to the employee (Chapter 5). If "yes," the employee is exempt from mandatory Medicare. If "no," the employee is subject to mandatory Medicare, unless an exclusion applies.

* State enabling legislation can have an effect on positions and entities covered by the particular state's Section 218 Agreement. Consult the appropriate state's enabling legislation to determine which positions are eligible for coverage under that state's Section 218 Agreement. For a list of state enabling statutes, see the Appendix of this Guide.

The flowchart on the next page illustrates the above steps.

SOCIAL SECURITY AND MEDICARE COVERAGE OF STATE AND LOCAL GOVERNMENT EMPLOYEES



1/ Section 218 Mandatory and Optional Exclusions (see Chapter 5)
2/ Mandatory Exclusions from FICA (see Chapter 5)
3/ Medicare Continuing Employment Exception (see Chapter 5)

NOTE: This chart is meant as a guide only and is not a substitute for discussing complex Section 218 coverage situations with your State Social Security Administrator or FICA taxation issues with your IRS FSLG Specialist.

IRS, SSA, State Social Security Administrators and Public Employer Social Security and Medicare Tax Responsibilities

The **Social Security Administration** is responsible for administering the Social Security Act, including the interpretation of individual Section 218 Agreements. SSA also administers benefits and maintains individual earnings records. See Chapter 7, **Social Security Administration**.

The **Internal Revenue Service** is responsible for administering the Internal Revenue Code (IRC), advising employers of their responsibilities, collecting taxes, and working with SSA and State Social Security Administrators on social security coverage and related tax issues. See Chapter 8, **Internal Revenue Service**.

The **State Social Security Administrator** is the designated official legally appointed to act for the state in negotiations with the Social Security Administration. This official acts for the state with respect to the initial Section 218 Agreement and modifications, the performance of the state's responsibilities under the Agreement, and in all state dealings concerning the administration of the Agreement. Each state's Section 218 Agreement ("Agreement"), and Social Security Regulation 404.1204, provide a legal obligation for each state to designate such an official. In many states the actual day-to-day responsibilities are delegated to the staff of the designated state official. See Chapter 9, **State Social Security Administrators**.

Public employers are responsible for the following:

- Properly classify workers as independent contractors or employees
- Determine which employees are exempt from social security and/or Medicare taxes
- Withhold, report and pay appropriate social security and Medicare taxes, or Medicare-only taxes for each employee
- Obtain clarifications of laws, regulations and other appropriate information from State Social Security Administrators, IRS and SSA.

Where to Direct Questions

The IRS, SSA, and State Social Security Administrator have different responsibilities and areas of authority in dealing with issues related to social security coverage, taxation, and reporting. The following indicates the primary point of contact for many common questions.

Topics for the Internal Revenue Service:

- Federal income tax
- Worker classification (employee or independent contractor) for employees not covered by a Section 218 Agreement
- Collection of social security or Medicare tax
- Completion and filing of Form W-2 and W-3
- Employment tax returns (941, 943, 944)
- Definition of public retirement system (FICA replacement plan)
- Is an employee covered under mandatory social security?
- Are certain payments subject to social security or Medicare tax?

- Do I need a new employer identification number?

Topics for the Social Security Administration:

- Social security benefits
- Section 218 coverage determinations
- Individual earnings records and quarters of coverage
- Verification of Section 218 terms
- Form W-2 records
- Problems with social security number

Topics for the State Social Security Administrator:

- Existence or terms of a Section 218 Agreement
- Modifications to the Section 218 Agreement
- Treatment of a specific position under a Section 218 Agreement
- Other issues involving interpretation of state law

Frequently Asked Questions

1) **What is a Section 218 Agreement?** A Section 218 Agreement is a written voluntary agreement between one of the 50 states (or Puerto Rico, the Virgin Islands, or an interstate instrumentality) and the SSA pursuant to the provisions of Section 218 of the Social Security Act. This Agreement provides social security and Medicare, or Medicare-only, coverage for designated groups of state and local government employees. The term refers to the original agreement and all subsequent modifications. These agreements can cover services of employees who are covered by a public retirement system as well as those who are not. To determine whether your entity is covered under a Section 218 Agreement, or can execute one, contact your State Social Security Administrator. See list of State Administrators on-line at the NCSSSA website. [SSA/STATE]

2) **How may a Section 218 Agreement affect employees covered by a public retirement system?** An Agreement may provide social security and Medicare coverage for employees already covered by a public retirement system (or FICA replacement plan). This may include:

    a. Employees covered by a retirement system who elect coverage under a referendum. The social security and Medicare coverage applies in addition to retirement system coverage.

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    b. Employees performing services that are excluded from mandatory social security coverage provisions, but are only optionally excluded under Section 218 Agreements, such as student services, and services of election workers who earn less than the threshold amount.

    c. Election workers, by establishing a dollar threshold for social security coverage lower than that set by the statutory requirement.

d. Employees hired before April 1, 1986, who meet the continuing employment Medicare exception. [STATE]

3) **Why might a Section 218 Agreement be modified?** Modifications to Section 218 Agreements are necessary to include additional coverage groups, to cover additional services in a group already covered (services previously optionally excluded), to cover ineligibles, to cover employees changing to the "Yes" group in a divided retirement system, to cover previously terminated groups, or to identify political subdivisions joining a covered retirement system. See Chapter 5. [STATE]

4) **I was told by the State Social Security Administrator that my town is covered for social security under the state's Section 218 Agreement and cannot be terminated. Is this true?** Yes. By law, after April 20, 1983, coverage obtained under a Section 218 Agreement, cannot be terminated. Beginning July 2, 1991, any state and local government employees not covered for social security under a Section 218 Agreement who are not qualified participants in a public retirement system (FICA replacement plan), are covered under ***mandatory*** social security. [STATE/SSA]

5) **Are Indian tribal government employers eligible to enter into Section 218 Agreements?** No, Indian tribal governments are not considered states or subdivisions of states for this purpose. See Internal Revenue Code section 7871. [IRS]

6) **I have a question regarding social security and Medicare coverage requirements for employees of my city. Whom do I contact?** The State Social Security Administrator should always be an entity's first contact on any questions regarding coverage under social security or Medicare. If additional assistance on coverage is needed, the SSA should be consulted. Questions about whether specific services are subject to mandatory social security and Medicare taxes should be directed to the IRS. [STATE]

7) **What is the responsibility of State Social Security Administrators with respect to non-Section 218 entities?** Under Section 218 of the Act, the primary legal responsibility State Social Security Administrators have is for Section 218 entities. However, the responsibilities the Administrator has with respect to non-Section 218 entities vary from state to state. Some State Administrators may not interact with non-Section 218 entities, while in other states the State Administrator may perform monitoring, quasi-regulatory and enforcement functions for them. If a non-Section 218 entity needs information regarding coverage under an agreement, the State Social Security Administrator should be contacted. [STATE]

8) **If an entity has a Section 218 Agreement in effect, and joins the state's public employee retirement system, does Section 218 coverage continue?** After April 20, 1983, a Section 218 Agreement cannot be terminated for any reason as long as that entity exists. The addition of a retirement system does not affect employee coverage under the Section 218 Agreement. [SSA]

Chapter 2

Government Entities and Federal Taxes

The Bureau of the Census estimated that there were 89,004 units of local government in the United States in 2012. These units of government employ more than 20% of the American workforce.

This chapter discusses the legal basis for different types of government entities and the specific tax questions that arise in connection with them. Many tax laws apply differently to government entities than to other organizations and individuals.

The income of certain government entities, including states, political subdivisions of states, or integral parts of states or political subdivisions, is generally exempt from tax. The income of other government entities, such as instrumentalities, might be excludable from gross income under IRC §115 if that income is derived from the exercise of an essential governmental function and accrues to a state or political subdivision of a state.

Certain government entities, such as colleges or universities, that are agencies or instrumentalities of a state or political subdivision of a state, are subject to the tax on unrelated business income under IRC §511. For more information, see Publication 598, *Tax on Unrelated Business Income of Exempt Organizations*.

State Government

States are recognized as entities by the U.S. Constitution. However, different definitions of a "state" apply for different legal purposes. Federal employment taxes generally apply to all 50 states, the District of Columbia, and all U.S. Territories. For purposes of a Section 218 Agreement, a "state" may refer to any of the 50 states, Puerto Rico, the Virgin Islands, and interstate instrumentalities. For this purpose, the definition of a "state" does not include the District of Columbia, Guam, American Samoa, the Commonwealth of the Northern Mariana Islands or Indian tribal governments.

Authority

The states have primary responsibility for many aspects of government. The 10th Amendment to the U.S. Constitution reserves to the states or to the people all powers not delegated to the federal government nor prohibited by the Constitution. Some services for which the state has primary responsibility include:

- Protection of lives and property by maintenance of a police force
- Regulation and improvement of transportation and roads within the state
- Regulation of business within the state
- Education and maintenance of schools
- Condemnation of property through eminent domain

In many cases, the federal and state governments share responsibility, with the federal government providing most of the funding and the state distributing the services. Some common services involving shared responsibility include:

- Health care
- Public assistance for persons in need
- Protection of natural resources
- Improvement in living and working conditions

Local Government and Political Subdivisions

Local governments are generally political subdivisions of states. They differ from state and federal governments in that their authority is not based directly on a constitution. Each state constitution governs the procedure for the establishment of local governments. In most cases, the state legislature must approve the creation or incorporation of a local government. The local government then receives a charter defining its organization, authority and responsibilities, including the means for electing governing officials.

Local government units bear a variety of names, such as city, county, township, village, parish, borough, or district. The legal significance of these terms may vary from state to state.

Authority

The authority of local governments varies greatly among the states and individual jurisdictions. Generally, a local government has the authority to:

- Impose taxes
- Try people accused of breaking local laws or ordinances
- Administer local programs within its boundaries

In addition to funding provided by local taxes, fees, and other sources, local governments receive financial aid from state and federal governments in providing these services according to need. Some of the services that local governments take primary responsibility for providing include:

- Conducting and coordinating elections
- Public safety
- Building and repairing local roads and streets
- Providing police and fire protection
- Collecting garbage and recycling
- Ensuring the safety of drinking water
- Maintaining courts, courthouses and jails
- Collecting state and local government taxes
- Keeping official records, such as for marriage, birth and death

Instrumentalities

An instrumentality is an organization separate from, but affiliated with, a state or local government. It may or may not be created by or pursuant to state statute, but it is operated for public purposes. Generally, an instrumentality performs governmental functions, but does not have the full powers of a government, such as police authority, taxation, and eminent domain (sovereign powers). Questions concerning the legal status of an instrumentality, for federal tax or

social security and Medicare purposes, should be directed to the IRS. Questions concerning a specific Section 218 Agreement should be addressed to the State Administrator or the SSA (see Chapter 7).

A wholly-owned instrumentality of one or more states or political subdivisions is treated as a state or local government employer for purposes of the mandatory social security and Medicare provisions of IRC section 3121(b)(7)(F).

Interstate Instrumentalities

An interstate instrumentality is an independent legal entity organized by two or more states to carry on governmental functions. Examples include a regional planning authority, transportation system or water district. For purposes of Section 218, an interstate instrumentality is treated as a state.

For an interstate instrumentality to cover its employees with a retirement system, a referendum must be held prior to the execution of a Section 218 Agreement. All interstate instrumentalities are authorized to provide a retirement system either on a divided system basis or a majority vote referendum (see Chapter 5 for referendum procedures). Employees of an interstate instrumentality who are **not** covered for social security under a Section 218 Agreement, but who **are** qualified participants in a public retirement system, are not covered for social security even if the employer incorrectly continues to withhold and report such taxes.

Characteristics of Instrumentalities

In Revenue Ruling 57-128, the IRS addressed the question of whether an organization is wholly-owned by one or more states or political subdivisions. This revenue ruling established the following factors as relevant to a determination of whether the entity is a government:

- Whether it is used for a governmental purpose and performs a governmental function
- Whether performance of its function is on behalf of one or more states or political subdivisions
- Whether there are any private interests involved, or whether the states or political subdivisions involved have the powers and interests of an owner
- Whether control and supervision of the organizations is vested in public authority or authorities
- Whether express or implied statutory or other authority is necessary for its creation and/or use of the instrumentality, and whether such authority exists
- The degree of financial autonomy and the source of operating expenses

Schools, hospitals and libraries, as well as associations formed for public purposes, such as soil and water conservation districts, may be instrumentalities of government, depending on the facts and circumstances. State sponsorship of an organization, state regulation of its activities, the participation of its employees in a public retirement system, and operation with public funds are

among the factors to be considered in determining whether an organization is an instrumentality. If an organization is essentially under private ownership and control, it is not an instrumentality of government. See Revenue Ruling 69-453.

Associations formed for conservation, protection and promotion, although carrying out a public purpose, may not rise to the level of state instrumentalities. The following associations may or may not be state instrumentalities:

- Soil and water conservation districts
- Fire associations that protect forestland
- Associations that promote a state or municipality

To determine the status of an entity, it is essential to review the documents that establish statutory authority. The following cases elaborate on the principles established in IRS Revenue Ruling 57-128.

Soil and Water Conservation Districts - Entities whose revenues are principally generated from fees collected from land owners within the district may or may not be instrumentalities of government, depending upon application of the factors listed above, including whether the district is under public or private control.

> **Example:** A soil conservation district in Minnesota was established to carry out a state conservation program. The Soil Conservation Service of the U.S. Department of Agriculture furnished the district with technical and clerical personnel. The disbursements made by the district were made from fees collected from members (occupiers of the land within the district) for services rendered, from funds allocated by the U.S. Department of Agriculture, and from state appropriations. The soil conservation district was created by statute as a political subdivision of the state and was under the control of a board of supervisors elected or appointed in accordance with state law. The soil conservation district is a political subdivision of the state. [Revenue Ruling 57-120, 1957-1 C.B. 310]
>
> **Example:** A Connecticut soil and water conservation district was formed as a private nonstock corporation by private individuals. The state had authority to assist private individuals in forming conservation districts, but did not have the power to operate them. The private individuals had complete control over the corporate operations, revenue and expenditures. Therefore, the soil and water conservation district is not a wholly-owned instrumentality of the state. [Revenue Ruling 69-453, 1969-2 C.B. 182]

Fire associations - Fire associations may or may not be instrumentalities of government, depending on whether they are under public or private control.

> **Example:** A fire association was organized pursuant to an Oregon state law that required all forest land in the state to be adequately protected from the dangers of fire. While the fire association was organized as a result of an

Oregon law, it was organized and operated for the mutual benefit of its members, and was not an instrumentality of the state. Furthermore, except for the work it performed on a cost basis for the state and federal government, the association derived most of its support from assessments imposed on its members. [Revenue Ruling 70-483, 1970-2 C.B. 201]

Example: Under the laws of the state of Pennsylvania, townships have the authority to purchase fire engines and fire apparatus out of general township funds for use of the township and to appropriate money to fire companies located in the township in order to secure fire protection. These volunteer fire companies are instrumentalities under Pennsylvania state law, and the members of volunteer fire departments are employees of the political subdivision. [Revenue Ruling 70-484, 1970-2, C.B. 202]

Associations that Promote a State or Municipality - State sponsorship of promotional activities is not sufficient to raise an association to instrumentality status.

Example: A municipal league comprised of qualified officials of member cities or villages, but with no control and supervision vested in a public authority, is not a state instrumentality. The League's activities consisted of publishing a monthly magazine featuring articles on governmental matters, conducting conferences, and sponsoring and participating in municipal law institutes and seminars. The state had no statute for the incorporation of a league of this nature as an instrumentality. [Revenue Ruling 65-26, 1965-1, C.B. 444]

Note: *Some state statutes specifically create certain associations as instrumentalities. A review of the establishing legislation is required to make a status determination.*

Indian Tribal Governments

The legal relationship between the United States and Indian tribal governments is set forth in the Constitution, treaties, statutes, and court decisions. Congress may limit the authority of Indian tribal governments; but, within those limits, the tribal governments retain attributes of sovereignty over both their members and their territory. Generally, Indian tribal governments provide government services, such as transportation, education, and medical care to reservation Indians.

Authority

Tribal governmental power includes the authority to:

- Choose the form of tribal government
- Determine tribal membership
- Regulate tribal and individual property
- Levy taxes
- Establish courts

- Maintain law and order

Employment Taxes

Generally, Indian tribal governments should follow general rules that apply to nongovernmental entities for employment tax. Publication 15, *Employer's Tax Guide*, and Publication 15-A, *Employer's Supplemental Tax Guide*, provide the basic rules for employers. There are, however, some special employment tax rules that apply to Indian tribal governments:

- An exception applies to the definition of "employment" for FUTA purposes for services performed in the employ of an Indian tribe. See IRC section 3306(c)(7). An Indian tribe may elect to make contributions to the state unemployment fund as if services by its employees were employment under FUTA, or it may make payments in lieu of the contributions in amounts equal to the unemployment benefits attributable under the state law to the service. An Indian tribe may make separate elections for any subdivision, subsidiary, or business enterprise wholly owned by it. If an Indian tribe fails to make either form of payment within 90 days of receiving a notice of delinquency, or if it fails to post a required payment bond, then service for the tribe is not excepted from "employment" until the failure has been corrected. See IRC section 3309(d). For this purpose, the term "Indian tribe" has the meaning given in 25 USC Section 450b(e) (Section 4(e) of the Indian Self-Determination and Education Assistance Act), and includes any subdivision, subsidiary, or business enterprise wholly-owned by an Indian tribe. See IRC section 3306(u).

- Amounts paid to members of Indian tribal councils for services performed as council members are not wages for purposes of FICA and income tax withholding (although such amounts are includible in gross income). Revenue Ruling 59-354, 1959-2 C.B. 24.

- Certain income derived by Indians from the exercise of their recognized tribal fishing rights is exempt from federal income and employment taxes (IRC section 7873). Wages paid to a member of a tribe employed by another member of the same tribe, or by a qualified Indian entity for services performed in a fishing rights-related activity of the employee's tribe, are exempt not only from federal income tax, but also from both the employer's and the employee's share of the social security and Medicare tax (Notice 89-34, 1989-1 C.B. 674).

Extensive information specifically addressing Indian tribal governments and employment tax issues can be found in Publication 4268, *Employment Tax Desk Guide,* on the IRS Indian Tribal Governments (ITG) website.

Frequently Asked Questions

1) **How is the tax treatment of governments different from that of other entities?**
Under IRC §115, the income of certain government entities, including states, political

subdivisions of states, or integral parts of states or political subdivisions, is generally not taxable. The income of other government entities, such as instrumentalities, might be excludable from gross income if that income is derived from the exercise of an essential governmental function and accrues to a state or political subdivision of a state. Colleges and universities that are agencies or instrumentalities of any government, or any political subdivision of government, or that are owned or operated by a government or political subdivision of a government, are subject to tax on unrelated business income.[IRS]

2) **Can the IRS issue a letter indicating that our entity is a tax-exempt government?** In order for a government entity to receive an official determination of its status as a political subdivision, instrumentality of government, or whether its income is excludable from gross income, exempt under Internal Revenue Code (IRC) section 115, it must obtain a letter ruling by following the procedures specified in Revenue Procedure 2014-1 or its successor. There is a fee associated with obtaining a letter ruling. [IRS]

   As a service to government entities, IRS can issue a "governmental information letter" free of charge. This letter describes government entity exemption from federal income tax and cites applicable Internal Revenue Code sections pertaining to deductible contributions and income exclusion. Most organizations and individuals will accept the governmental information letter as the substantiation required for these purposes. Contact an FSLG Specialist or go to the FSLG Customer Services page for more information. [IRS]

Chapter 3

Wage Reporting and Employment Taxes

A government entity that has employees needs to be familiar with the basic responsibilities and requirements applicable to all employers, as well as some provisions that are unique to governments. This chapter briefly covers the main types of compensation that are included in employee wages and the requirements for tax withholding and payments. Tax requirements for employers are discussed in detail in Publication 15, *Employer's Tax Guide (Circular E)*. This chapter highlights some key requirements for employers generally, and matters of special interest to governmental employers.

All governmental entities that employ workers are subject to federal employment taxes on wages, except where the law provides specific exceptions. The Internal Revenue Code (IRC) defines wages subject to income tax withholding under section 3401, and defines wages for social security and Medicare purposes taxes under section 3121. As discussed in chapter 2, a broad exception exempts government employment from federal unemployment tax (FUTA).

Social security and Medicare taxes, also referred to as Federal Insurance Contributions Act (FICA) taxes, consist of Old-Age, Survivors and Disability Insurance (OASDI, or social security) and Medicare Hospital Insurance (Medicare) taxes. Internal Revenue Code (IRC) section 3101 imposes tax on the employee, and section 3111 imposes tax on the employer. State or local entities covered by social security and/or Medicare must withhold and pay over the employee share of the taxes and must pay the employer share. Under section 3402, employers are also generally required to withhold income tax from wages.

In general, all compensation provided to an employee is included in taxable wages unless an exception is provided by law. An exception may apply for FICA taxes, or federal income tax withholding, or both. The following discussion addresses the treatment of certain forms of compensation, focusing on some that are of particular interest to government employers.

Note: *Workers are subject to social security, Medicare, or income tax withholding only when performing services as employees of the organization. The process for determining whether workers are employees is the subject of Chapter 4.*

Social Security and Medicare Wages

IRC section 3121(a) provides that wages include all remuneration for employment, whether paid in cash or in some other form, unless specifically excluded by statute. Examples of wages for social security and Medicare purposes include salaries, fees, bonuses, prizes, awards and commissions. It is immaterial whether the payments are based on the hour, week, month, year, piecework, percentage of revenue, or other system.

An important exception is provided by IRC 3121(b)(7)(F), which excludes state and local government employees from the OASDI tax, except where these employees are not covered by a public retirement system (FICA replacement plan), or where a Section 218 Agreement exists. Chapter 5 discusses the application of the tax to governmental employees in detail.

The Social Security Administration establishes the maximum amount of wages subject to the social security tax per year. For 2015, this amount is $118,500. The amount is adjusted each year. (Since 1994, there has been no wage base limit for Medicare tax.)

Social Security, Medicare and Additional Medicare Tax Rates and Limits

Social Security and Medicare Tax				
Social Security (OASDI) Information	**2012**	**2013**	**2014**	**2015**
Employee Rate	4.20%	6.20%	6.20%	6.20%
Employer Rate	6.20%	6.20%	6.20%	6.20%
Maximum Wages Subject to Tax*	$110,100	$110,100	$117,000	$118,500
Medicare Tax Information				
Employee Rate	1.45%	1.45%	1.45%*	1.45%*
Employer Rate	1.45%	1.45%	1.45%	1.45%
Maximum Wages Subject to Tax	All Wages			
Additional Medicare Tax Information				
Employee Rate	----	0.9%	0.9%	0.9%
Employer Rate	----	N/A	N/A	N/A
Withholding Threshold	Wages that exceed $200,000 in a calendar year			

Additional Medicare Tax

Beginning in 2013, a 0.9% Additional Medicare Tax applies to Medicare wages, Railroad Retirement Tax Act compensation, and self-employment income over a threshold amount based on the taxpayer's filing status.

An employer must withhold Additional Medicare Tax from wages and RRTA compensation it pays to an employee in excess of $200,000 in a calendar year, without regard to the employee's filing status or wages paid by another employer. Any withheld Additional Medicare Tax will be credited against the total tax liability shown on the individual's income tax return (Form 1040).

Unlike OASDI and Medicare taxes, the Additional Medicare Tax is only paid by the employee. There is no employer match for Additional Medicare Tax.

An employer is required to begin withholding Additional Medicare Tax in the pay period in which it pays wages in excess of $200,000 to an employee and continue withholding it until the end of the calendar year.

All wages that are currently subject to Medicare tax are subject to Additional Medicare Tax if they are paid in excess of the applicable threshold for a taxpayer's filing status.

For more information on Additional Medicare Tax, see Questions and Answers for the Additional Medicare Tax on IRS.gov.

Statutory Exceptions to Social Security and Medicare Coverage

State and local government employment not covered by a public retirement system (see Chapter 6) is generally subject to social security and Medicare coverage under IRC 3121(b)(7)(F). However, the Internal Revenue Code provides some statutory exceptions that exclude certain services from the definition of employment for purposes of mandatory social security coverage. These exceptions include services performed by:

3121(b)(7)(F)(i*) – individual employed to be relieved from unemployment

3121(b)(7)(F)(ii) – inmate or hospital patient

3121(b)(7)(F)(iii) – individual serving on a temporary basis because of emergency

3121(b)(7)(F)(iv) – election official or worker, for amounts below an annually designated threshold

3121(b)(7)(F)(v) – public official compensated solely on a fee basis

In cases where social security coverage is provided by a Section 218 Agreement, the exclusions for some of these groups may apply differently. These are discussed in greater detail in Chapter 5.

Other Forms of Cash Compensation

In addition to stated salary or wages, employees may receive cash designated in various other ways. Below are some other common forms of cash compensation.

Sick Pay

Sick pay is an amount paid to an employee because of inability to work because of sickness or injury. Sick pay is generally subject to social security and Medicare taxes and

income tax withholding if paid by the employer. The employer withholds from sick pay based on the employee's Form W-4. Sick pay is sometimes paid by a third party, such as an insurance company or employee trust. The rules on third-party withholding, paying and reporting social security and Medicare taxes differ, depending upon whether the third party is acting as an agent of the employer or an independent insurer, and the terms of an agreement between the employer and agent or insurer.

If the third-party payer does not withhold income tax, the employee may request income tax withholding by completing and giving to the third party Form W-4S, *Request for Federal Income Tax Withholding from Sick Pay*.

See Publication 15-A, *Employer's Supplemental Tax Guide*, for more details on third-party sick pay.

The following types of sick pay or injury pay are **not** subject to social security and Medicare taxes:

1. Payments received under a workers' compensation act, or under a statute in the nature of a workers' compensation act.
2. Payments, or portions of payments, attributable to the employees' contributions to a sick pay plan.
3. Payments on account of sickness or injury made by, or on behalf of, an employer, more than six months after the last calendar month in which the employee worked for the employer.

Vacation Pay

Vacation pay is wages and is subject to social security and Medicare tax and income tax withholding. When vacation pay is made in addition to regular wages for the vacation period, withhold as if the vacation pay were a supplemental wage payment, discussed later.

Military Differential Pay

Military differential pay is any payment made by an employer to an individual during the period that the individual is called to active duty in the uniformed services for a period of more than 30 days, and represents part or all of the wages the individual would have received from the employer if the individual were performing service for the employer during that time.

The Heroes Earnings and Relief Tax Act of 2008 defines military differential pay as wages for income tax purposes, reportable on Form W-2, box 1.

After December 31, 2008, the following rules apply:

1. Differential wage payments made to an individual on active duty for more than 30 days are subject to income tax withholding, but not to social security and Medicare (FICA) or unemployment tax (FUTA).
2. Differential wage payments are supplemental wages. Employers may use either the aggregate or the separate method to calculate income tax withholding in these situations. For a discussion of these methods, see section 7, "Supplemental Wages", in Publication 15, *Employer's Tax Guide*.
3. The amount of differential wages must be reported on Form W-2.

Deceased Employee's Wages

If an employee dies during the year, the employer must report the accrued wages, vacation pay, and other compensation paid after the date of death. Also, report wages that were available to the employee while he or she was alive, regardless of whether the wages actually were in the possession of the employee, as well as any other regular wage payment, even if is necessary to reissue the payment in the name of the estate or beneficiary. How the payment is reported depends on the year in which payment is made.

Payment made in the year of death - If you made the payment after the employee's death but in the same year the employee died, you must withhold social security and Medicare taxes on the payment and report the payment on the employee's Form W-2 only as social security wages (box 3) and Medicare wages and tips (box 5) to ensure proper social security and Medicare taxes withheld in boxes 4 and 6. Do not show the payment in box 1.

Payment made after the year of death - If the payment was made after the year of death, it should not be reported on Form W-2 and social security and Medicare taxes should not be withheld.

Whether the payment is made in the year of death or after the year of death, report it in box 3 of Form 1099-MISC, *Miscellaneous Income*, as a payment to the estate or beneficiary. Use the name and taxpayer identification number (TIN) of the estate or beneficiary on Form 1099-MISC. See Revenue Ruling 86-109, 1986-2 C.B.196.

See the Instructions for Forms W-2 and W-3 and Publication 559, *Survivors, Executors, and Administrators*, for more information on the treatment of payments on behalf of a decedent.

Back Pay

Back pay is pay received in a tax year for actual or deemed employment in an earlier year. For social security coverage and benefit purposes, **all** back pay is wages, except amounts specifically and legitimately designated otherwise, such as interest, penalties, and legal fees. For tax purposes, back pay is treated as wages in the year received and is reported on Form W-2 for that year. Income, social security and Medicare tax withholding apply in the year of payment at the rates in effect for that period.

If the back pay is awarded ***under a statute*** (for example**,** under the Americans with Disabilities Act or Fair Labor Standards Act), the period for which back pay is credited as wages for social security purposes is different from the tax year it is reported. However, payments of back pay under a statute will remain posted to the employee's social security earnings record in the year reported on Form W-2 unless the employer or employee notifies the SSA in a special, separate report. If this is done, SSA can allocate the statutory back pay to the appropriate periods for purposes of retirement benefit calculations. See IRS Publication 957, *Reporting Back Pay and Special Wage Payments to the Social Security Administration*, for more information.

Workers' Compensation

Amounts received by police officers, firefighters, and other employees or their survivors for personal injuries or sickness incurred in the course of employment are excludable from income and social security and Medicare taxes if they are paid under a workers' compensation act or a statute in the nature of a workers' compensation act that provides compensation to employees for personal injuries or sickness incurred in the course of employment.

This exclusion does not apply to retirement plan benefits based on age, length of service, or prior contributions to the plan, even if the individual retired because of an occupational sickness or injury.

Workers' compensation benefits are fully excluded from gross income and are not subject to employment taxes, income tax withholding or reporting.

Noncash Payments

Generally, noncash payments are wages subject to social security and Medicare. The dollar value of wages paid in a medium other than cash should be computed based on the fair market value of the property at the time of the payment. The fair market value may be based on the prevailing value of the item in the locality or upon a reasonable value established for other purposes. Special rules may apply to noncash fringe benefits, discussed below.

Fringe Benefits

Fringe benefits, which generally include any compensation other than cash wages or salary, must be included in an employee's wages unless an exception is provided by law. Examples of employer-provided fringe benefits include:

- Vehicles for personal use
- Meals
- Health or life insurance
- Tickets to entertainment or sporting events
- Holiday gifts
- Personal use of employer facilities
- Transportation passes

The tax treatment of some of these benefits is determined by specific statutes; others fall under general rules for broader categories of fringe benefits. IRS Publication 15-B, *Employer's Tax Guide to Fringe Benefits*, updated annually, addresses fringe benefits applicable to all employers. In addition, the office of Federal, State and Local Governments (FSLG) produces Publication 5137, *Fringe Benefit Guide,* especially for government employers. For a more comprehensive discussion of fringe benefits, you can view or download this publication on the FSLG website. Some common tax-exempt benefits are discussed below.

Business Expense Reimbursements – Accountable Plan

Payments to employees for travel and other ordinary and necessary expenses of the employer's business generally are wages subject to social security and Medicare and income tax withholding unless they are made under an ***accountable plan***. There are three requirements for a reimbursement procedure to be treated as an accountable plan:

1. The expenses must qualify as deductible business expenses incurred while performing services for the employer;
2. The employee must adequately account for the expenses to the employer within a reasonable period of time; and
3. The employee must return any amounts received that exceed expenses within a reasonable period of time.

See IRC section 62(c), section 1.62-2 of the Income Tax Regulations, and Publication 15 for more information on accountable plans.

The use of per diem rates at or below the federal rate for travel expenses can reduce and simplify the recordkeeping requirements for accounting for these expenses. See Publication 463, *Travel, Entertainment, Gift, and Car Expenses*, or the FSLG's Publication 5137, *Fringe Benefit Guide,* for more information on per diem reimbursement systems.

Reimbursements Not Made Under Accountable Plan

If an employer provides reimbursements that do not comply with the accountable plan rules, these amounts are treated as wages and subject to all employment taxes. The employee may be able to deduct the expenses incurred on his or her individual income tax return.

Hourly or Tool Rate Reimbursement

The payment of an hourly rate to cover the cost of tools, equipment, etc., is not an accountable plan if the amount would be paid regardless of the amount of expenses incurred or whether expenses actually are incurred. Only if actual business expenses that are accounted for under the rules above are incurred can the amount be excluded from wages.

Working Condition Fringe Benefit

An employer may exclude from the wages of an employee the value of any property or services provided by the employer to the extent that, if the employee paid for the property or services, the payment would be allowable as a business expense deduction. This is called a working condition fringe benefit. See IRC section 132(a)(3). Working condition fringe benefits include property provided that is necessary for employees to accomplish work. Common examples include vehicles or special clothing provided by the employer.

Employer-Provided Vehicles

If an employer provides an employee with unrestricted use of a vehicle, the employee receives a noncash fringe benefit and the value of the use is required to be included in income. The entire value of the vehicle for the tax year is included in income unless the employee substantiates its business use. The portion of the value that is attributable to the employee's substantiated business use of the employer's vehicle is excludable from the employee's income as a working condition fringe. See IRC section 274(d) and Regulation section 1.274-5T.

There are three methods for determining the value of the personal use of a vehicle:

- Cents-per-mile rule
- Commuting rule
- Lease value rule

The requirements for each of these rules are discussed in IRS Publication 15-B, and in the FSLG's Publication 5137, *Fringe Benefit Guide*.

The value of a "qualified nonpersonal use vehicle" can be excluded from income as a working condition fringe benefit. A qualified nonpersonal use vehicle is one that, due to its nature, is not likely to be used more than a minimal amount for personal purposes. This includes, for example, a clearly marked police, fire, or public safety officer vehicle, a

flatbed truck, a school bus, or ambulance. An employee is not required to substantiate the business use of a qualified nonpersonal use vehicle in order to exclude its value from income. See IRC section 274(d)(i) and Publication 15-B.

Clothing Provided by Employer

The value of work clothing provided by the employer is not taxable to the employee if:

1) the employee must wear the clothing as a condition of employment, and
2) the clothing is not suitable for everyday wear.

It is not enough that the employee wear distinctive clothing; the employer must specifically require the clothing for work. The second test is not met solely because the employee does not, in fact, wear the work clothes away from work; the clothing must not be suitable for taking the place of regular clothing. The value and upkeep of work clothes provided to firefighters, health care workers, law enforcement officers or letter carriers is nontaxable to the employee. The value of provided items such as safety shoes or boots, safety glasses, hard hats and work gloves provided and maintained by the employer is not taxable if the employer requires the items for work and the items are not suitable for everyday use.

Health Benefits

Under IRC sections 105 and 106, contributions to or benefits provided from an employer-provided health care plan, including reimbursements and paid insurance premiums, are generally excluded from the wages of the employees and are not subject to social security, Medicare taxes or income tax withholding. A health reimbursement arrangement (HRA) may provide for the carryover of benefits from year to year, and may specify the types of medical benefits that are covered. An HRA can only be financed by employer contributions, and cannot involve an employee election to participate. For more information, see Publication 969, *Health Savings Accounts and Other Tax-Favored Health Plans*.

Note: *The Affordable Care Act made changes affecting the tax treatment of HRAs. See www.irs.gov for more information.*

Cafeteria (Section 125) Plans

Cafeteria plans, including flexible spending arrangements, are benefit plans under which employees can choose from among cash and certain qualified benefits. If the employee elects qualified benefits, employer contributions are generally excluded from the wages of the employees and are not subject to social security, Medicare taxes or income tax withholding. A cafeteria plan is a separate written plan maintained by an employer for employees that meets the specific requirements of section 125 of the Internal Revenue Code and associated regulations. It provides participants an opportunity to receive certain benefits on a pre-tax basis. Participants in a cafeteria plan must be permitted to choose

among at least one taxable benefit (such as cash) and one qualified benefit. If an employee elects to receive cash instead of any qualified cafeteria plan benefit, that amount is treated as wages subject to all employment taxes.

A qualified benefit is a benefit that does not defer compensation and is excludable from an employee's gross income under a specific provision of the Code, without being subject to the principles of constructive receipt. Qualified benefits include:

- Accident and health benefits (but not Archer medical savings accounts or long-term care insurance)
- Adoption assistance
- Dependent care assistance
- Group-term life insurance coverage (including costs that cannot be excluded from wages)
- Health savings accounts, including distributions to pay long-term care services

Generally, qualified benefits under a cafeteria plan (including health and accident insurance) are excluded from the wages of the employees. The cost of group-term life insurance of up to $50,000 provided by an employer is excludable from income and social security, and Medicare wages. However, the cost of group-term life insurance that exceeds $50,000 of coverage is included in wages (but is not subject to income tax withholding) and is subject to social security and Medicare taxes, even when provided as a qualified benefit in a cafeteria plan. The cost of group-term life insurance that is includible in income only because the insurance exceeds $50,000 of coverage is considered a qualified benefit. Adoption plans are also subject to social security and Medicare taxes. See IRS Publication 15-B for details.

Health benefits provided under a cafeteria plan may include insurance or a flexible spending arrangement (FSA) for qualifying medical expenses. An employer may have both a Health Reimbursement Arrangement (HRA) and a cafeteria plan, but the salary reductions cannot be used to directly or indirectly fund an HRA (see Revenue Ruling 2005-24).

Any amounts paid for health benefits pursuant to a salary reduction election are considered paid by the employer; therefore, the employee is not entitled to exclude from income any amounts paid as "reimbursements" to the employees for benefits under the plan. See Revenue Ruling 2005-24 for more information on the interaction between an HRA and various reimbursement arrangements.

Annual Limitation

For plan years beginning after December 31, 2012, a cafeteria plan may not allow an employee to request salary reduction contributions for a health FSA in excess of $2,500. This amount will be indexed for future years.

A cafeteria plan offering a health FSA must be amended to specify the $2,500 limit (or any lower limit set by the employer). While cafeteria plans generally must be amended on a prospective basis, an amendment that is adopted on or before December 31, 2014, may be made effective retroactively, provided that in operation the cafeteria plan meets the limit for plan years beginning after December 31, 2012. A plan that does not limit health FSA contributions to $2,500 is not a cafeteria plan and all benefits offered under the plan are includible in the employees' gross income. See Notice 2012-40.

In general, all amounts credited to an employee in the plan must be used up by the end of the calendar year or are forfeited. However, under a "grace period rule" an IRC 125 cafeteria plan may permit an employee to use amounts remaining from the previous year to pay expenses incurred for certain qualified benefits during the period of up to two months and 15 days immediately following the end of the plan year. See Notice 2005-42 .

A plan may be amended to provide that up to $500 of unused amounts remaining at the end of a plan year in a health FSA to be paid or reimbursed to plan participants for qualified medical expenses incurred during the following plan year. However, if this provision is adopted, the grace period discussed above does not apply. See Notice 2013-71.

Meals and Lodging Furnished by Employer

The value of meals is excludable **if** the meals are furnished on the business premises of the employer **and** are provided for the convenience of the employer.

The value of lodging is excludable if the lodging is furnished on the business premises, is furnished for the convenience of the employer, **and** if the employee is required to accept the lodging as a condition of employment. See Publication 15-B for more information.

Retirement Plans

Regardless of social security coverage, most public employees are covered by some form of retirement plan. The terms of these plans may vary greatly, but in general provide for tax-deferred income placed in trust for the benefit of employees. These plans may involve employee or employer contributions, or both. Under certain provisions of the IRC, contributions may be deferred from tax until they are withdrawn. The term "qualified" is widely used to describe private-sector plans under IRC 401 that meet specific provisions of the Employee Retirement Income Security Act (ERISA) that enable them to offer certain tax advantages to the participants. Many public employees, however, are covered by nonqualified plans, generally under IRC sections 403(b) or 457, discussed below.

Income Tax Withholding on Qualified Retirement Plans

For income tax withholding purposes, employer and employee contributions made under qualified plans (up to the maximum allowable for the year) are deferred from income tax. The employee will be subject to tax on distributions of these amounts when they are

withdrawn from the plan. In most cases, withdrawals that are not rolled over into another plan are subject to mandatory income tax withholding upon distribution.

Employer "Pick-Up" Contributions

IRC Section 414(h)(2) allows state and local government entities with governmental plans within the meaning of IRC 414(d) to treat contributions that have been designated as employee contributions, but which are "picked up" (paid) by the employer, to be treated as employer contributions, and therefore as excludable from income. These "picked up" contributions are also exempt from social security and Medicare tax as long as they are not made pursuant to a salary reduction agreement. For more information on the conditions required for employer pick-up. See IRC 414(h)(2). For more information, visit www.irs.gov and search for "Employer pick-up contributions."

Section 403(b) Plans

Plans under IRC section 403(b), also called tax sheltered annuities, are available to certain employees of public schools, employees of tax-exempt organizations, and certain ministers. These plans resemble qualified plans in many respects. Many public school employees are covered by 403(b) plans in addition to receiving social security coverage under a Section 218 Agreement.

Employer contributions to tax-sheltered annuities under section 403(b) for public school employees are exempt from social security and Medicare taxes, unless the contributions are made by reason of a salary reduction agreement. Eligible participants may defer amounts from income tax up to an annual limit ($18,000 in 2015). This amount may be increased for certain employees with more than 15 years of service. In addition, additional tax-deferred "catch-up" contributions may be made for employees age 50 or older.

Employee contributions, including those made by salary reduction arrangements, are subject to social security and Medicare tax. See IRC §3121(a)(5)(D).

For more information, see Publication 571, *Tax-Sheltered Annuity Plans (403(b) Plans)*, and the section 403(b) page on IRS.gov.

Section 457 (Nonqualified) Plans

Many public employees participate in nonqualified section 457, deferred compensation plans. These plans can be established by state and local governments or tax-exempt organizations. If they meet the requirements of IRC section 457(b), they are considered "eligible" plans; if not they are considered "ineligible" plans, and are governed by IRC section 457(f).

Section 457(b) – Eligible Plans
Governmental 457(b) plans must be funded, with assets held in trust for the benefit of employees. Plans eligible under 457(b) may defer amounts from income tax up to an annual limit ($18,000 in 2015). Governmental 457(b) plans may make "catch-up"

contributions to employees age 50 or older, in addition to the basic section 457(b) catch-up. Social security and Medicare taxes generally apply to all employer and employee contributions. For further information regarding social security and Medicare tax withholding and reporting on amounts deferred into eligible deferred compensation plans, see the section 457(b) page on IRS.gov.

Amounts deferred from wages into eligible section 457(b) plans are not subject to income tax withholding until they are distributed from the plan or made available to the participant or beneficiary. For further information regarding income tax reporting and withholding upon amounts deferred into and distributed from eligible governmental deferred compensation plans, see the section 457(b) page on IRS.gov, and Section VI of Notice 2003-20.

Section 457(f) – Ineligible Plans
Nonqualified state or local government plans that do not meet the requirements of section 457(b) are ineligible, or section 457(f), plans. There is no limit on the annual deferrals on these plans, but to defer taxation, all deferrals must be subject to substantial risk of forfeiture. Amounts deferred under a section 457(f) plan are generally subject to social security and Medicare taxes at the later of the time 1) when the services giving rise to the related compensation are performed, or 2) when there is no substantial risk of forfeiture of the rights to the amounts.

Employer Reporting Responsibilities

Basic federal tax requirements that generally apply to all employers are discussed below. For a more detailed explanation, see Publication 15.

Employer Identification Number

IRS identifies individual taxpayers by using taxpayer identification numbers (TINs). For individuals, the TIN is the social security number. State and local entities use employer identification numbers (EINs) assigned by IRS to identify their accounts and tax returns. The EIN should be used on all employment tax returns (e.g., Form 941), information returns (e.g., Form W-2) and correspondence with the IRS. Generally, each county, city, school district or other governmental unit will have a unique EIN. However, this is not always the case within state governments. Many state agencies use an EIN assigned to another agency; some larger state agencies may use a unique EIN.

When two entities are combined (for example, when one municipality annexes another, or when school districts are consolidated) the EIN of the annexed area or abolished district should no longer be used, as it is no longer a separate entity. A continuing entity that absorbs or annexes another can retain its EIN. However, if a new entity is created from the dissolution of two or more preexisting entities, a new EIN should be obtained. When an unincorporated area is incorporated, it becomes a separate entity and must obtain its own EIN.

To obtain a new EIN, complete Form SS-4, *Application for Employer Identification Number*. Once you have received an EIN, ensure that it is accurate and complete on each tax document submitted. When an incorrect EIN is used, credit for tax payments can be delayed or applied incorrectly.

Note: *For tax years prior to 1987, SSA assigned EINs beginning with the digits "69" for government employers to report earnings, but these are no longer used. Prior to 1987, these numbers were assigned for new modifications to Section 218 Agreements, and then used to process wage reports. Many states have a filing system based upon the 69 number and, therefore, continue to sequentially assign 69 numbers for internal recordkeeping purposes.*

Form SSA-1945

State and local government employers are required to notify employees hired on or after January 1 2005, in jobs not covered by social security, of the effects of the Windfall Elimination Provision and the Government Pension Offset. The law requires newly hired public employees to sign Form SSA-1945, indicating that they are aware of a possible reduction in their future social security benefit entitlement. For more detailed information about this law, see Chapter 7 or http://www.socialsecurity.gov/form1945.

Form W-2

An employer is responsible for furnishing Form W-2, *Wage and Tax Statement*, to each employee from whom income, social security or Medicare tax was withheld, or would have been withheld if the employee had claimed no more than one withholding allowance or had not claimed exemption from withholding on Form W-4. Statements to employees must be furnished by January 31 of the following year. The aggregate amounts are reported on Form W-3, *Transmittal of Wage and Tax Statements*. For more information, see the Instructions for Forms W-2 and W-3.

Employers who file 250 or more Forms W-2 must file them electronically. Statements may be furnished to employees electronically only if an affirmative consent has been received from the employee to do so. See Publication 1141 for more information.

An employer uses Form 941, *Employer's QUARTERLY Federal Tax Return* (or for certain employers, the annual Form 943 or 944) to report wages paid and taxes withheld. After the calendar year ends, employers prepare individual employee reports on Forms W-2, *Wage and Tax Statement*, with Form W-3, *Transmittal of Wage and Tax Statements*, showing the total wages paid and taxes withheld for each employee during the year. An employer reports wage information to SSA for crediting to the employees' earnings records. This is done either by sending SSA Copy A of the paper Form W-2 with a covering Form W-3, or by sending the Form W-2 information in the form of electronic reports.

If you need to talk directly to SSA about an electronic file or other wage reporting problem, you may contact an Employer Services Liaison Officer (ESLO) through the

ESLO page on the SSA website, or call 1-800-772-6270 for assistance from an earnings report technician. Specifications for electronic reporting of Form W-2 information can be found at the SSA employer page or by calling the ESLO for your state.

Form 941

Form 941, *Employer's Quarterly Federal Tax Return*, is used to report total wages, wages subject to social security and Medicare tax, and federal income tax. Agricultural employers file Form 943**,** *Employer's Annual Tax Return for Agricultural Employers*. Form 944, discussed below, is an annual version of the form, for employers with the smallest payrolls. Generally, annual Form 941 or Form 943 totals must match the aggregate wages shown on all Forms W-2 issued to employees for the same period.

To prepare Form 941, the total wages and compensation for the quarter must be determined. Wage payments are included in the quarter in which they are paid. For example, an employee works for the county in a pay period ending on March 20, but is not paid until April 5. In this situation, the employee's wage payment is included in the second quarter when the payment is made, not the first quarter when the work was done. Total wages and compensation entered on line 2 of Form 941 includes all payments to employees. Examples of these payments include:

1) Wages, salaries, commissions, fees, and bonuses
2) Vacation allowances
3) Dismissal pay and severance pay
4) Tip income
5) Noncash payments, including goods, lodging, food, clothing or services

Wages from which social security and Medicare tax must be withheld may differ from total wages. This may be because certain amounts are not included in wages for income tax purposes, but are subject to social security and Medicare tax (for example, deferred compensation in a nonqualified deferred compensation plan). Another common reason for a difference in the totals is that earnings exceeding the annual wage base are not subject to the OASDI portion of social security tax. The total income tax withheld (line 3) includes all federal income tax withheld from all employees for the calendar quarter covered by the return.

Form 941 must be filed with the IRS by the last day of the month following the calendar quarter. For example, the first quarter return covering January through March is due by April 30. If all taxes are deposited when due, the employer has 10 additional days after the due date to file the return. If the return is not filed by this date, the employer may be subject to penalties and interest in addition to the tax due on the return.

Form 944

Certain taxpayers with small payrolls may report their employment taxes on an annual rather than a quarterly basis. The IRS will notify these taxpayers that they are eligible to use Form 944. Instead of the quarterly Form 941, they file annual Form 944, *Employer's*

Annual Employment Tax Return. An employer may contact the IRS to request to file a Form 941 instead of a Form 944. See Revenue Procedure 2009-51. The deposit requirements, discussed below, are the same as for quarterly filers. For more information on eligibility, see Publication 15 or the Instructions for Form 944.

Except for the return due date, references to the requirements for quarterly Form 941 discussed in this chapter are also applicable to filers of annual Form 944.

Form 941-X

Employers correct errors to Form 941 or 944 by filing Form 941-X, *Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund*, or Form 944-X, *Adjusted Employer's ANNUAL Federal Tax Return or Claim for Refund*. Form 941-X is a stand-alone return that should be filed as soon as the error is discovered. The return for the period when the error is discovered is not affected. Additional requirements are discussed in the Instructions for Form 941 and in the Instructions for Form 941-X.

Special Reporting Situations for Government Employers

These are some circumstances commonly facing government employers that involve special reporting rules.

Multiple Employers and the Wage Base

Because each employer must withhold social security tax on wages up to the annual maximum, an employee who works for more than one employer in one calendar year may have excess social security taxes withheld. In order to get a refund of the excess social security tax withheld by the employers, the employee shows the overpayment on Form 1040. Employers are not responsible for making any adjustments based on wages paid by other employers and cannot claim a refund in this situation, because each employer is responsible for withholding and paying social security tax on wages paid to each employee up to the wage base.

For the purpose of determining responsibility for reporting wages, a state is considered to be one employer and each political subdivision is considered a separate employer. An employee who transfers from one state agency to another during a calendar year does not change employers. In this case, the state should withhold and pay social security tax only up to the wage base for that employee. However, an employee who transfers from a state agency to a political subdivision of the state, a city or county, has changed employers. Each employer must withhold and pay social security tax up to the wage base for that employee, regardless of other employment.

Medicare Qualified Government Employment (MQGE)

As explained in Chapter 2, all employees hired after March 31, 1986, are subject to Medicare tax. State and local employers that provide coverage under a public retirement

system may have employees who are not subject to social security but are subject to Medicare tax. This is referred to as Medicare Qualified Government Employment (MQGE). MQGE Forms W-2 are filed separately from those for employees covered by social security and Medicare, or from Forms W-2 having no social security or Medicare wages. Paper MQGE Forms W-2 must be transmitted with a covering Form W-3 with "Medicare Govt. Emp." checked in box b. See the Instructions for Forms W-2 and W-3 or contact your ESLO for more information. **Note:** Electronically transmitted records should be grouped to follow a "Code RE" record with an Employment Code of "Q". All other W-2 records should be grouped to follow a Code RE record with an Employment Code of "R". Do not group MQGE W-2 records and non-MQGE W-2 records together after a single Code RE record. See SSA Publication 42-007, *Specifications for Filing Forms W-2 Electronically* (EFW2).

Employees Covered for MQGE and FICA

If they are employed in more than one capacity, some state and local employees may be subject to both Medicare-only withholding and full social security and Medicare in the same reporting year. When an employee is in a continuous employment relationship with the same employer for the year, and the employer has both types of employees, the employer has two reporting options:

1. Prepare a single Form W-2 with the total annual wages in box 1, the total Medicare wages and taxes from BOTH positions in box 5 and box 6. Social security and Medicare wages and taxes are entered in box 3 and box 4 (SSA prefers that this method be used in order to reduce errors), or

2. Use a separate Form W-2 for wage data from the Medicare-only position and a second Form W-2 for FICA wage data from the positions with both social security and Medicare coverage.

Information Reporting for Election Workers

If the compensation of an election workers is less than a statutorily established amount ($1,600 for calendar year 2015), it is generally not subject to mandatory social security and Medicare tax. See IRC sections 3121(b)(7)(F)(iv) and 3121(u)(2)(B)(ii)(V). However, under a state's Section 218 Agreement an election workers' compensation may be subject to social security and Medicare taxes at a level below the statutory amount. In any case, compensation of election workers is not subject to income tax withholding.

If an election worker's wages are subject to withholding of social security and Medicare tax, Form W-2 reporting is required for all compensation, regardless of the amount. If an election worker's compensation is not subject to withholding of social security and Medicare tax, Form W-2 reporting is required for payments that aggregate $600 or more in a calendar year. See Revenue Ruling 2000-6 for a discussion of information reporting with respect to election workers.

Information Returns

Any entity, including a governmental organization, conducting a trade or business, is required to file with the IRS, and furnish to recipients, information returns for certain types of payments. In most cases, these payments are reported on Form 1099-MISC, *Miscellaneous Income*.

IRC 6041(a) states that all persons engaged in a trade or business and making payment in the course of the trade or business to another person of rent, salaries, wages, premiums, annuities, compensation, remuneration, emoluments, or other fixed and determinable gains, profits, and income (with certain exceptions) of $600 or more in any year must furnish an information return indicating the amount of such income and the name and address of the recipient of such payment. The return with respect to certain payments of compensation to an employee is made on Forms W-2 and W-3; never use Form 1099-MISC to report payments for services by an employee. The recipient of the payment is required to furnish to you the entity's name, address and identification number. You should obtain this information before payments are made. This identification number must be included on the information return. Payments for nonemployee compensation are discussed in the Instructions for Form 1099-MISC.

Governments must file Form 1099-G, *Certain Government Payments*, for certain payments, including tax refunds, unemployment compensation, and taxable grants. See the Instructions for Form 1099-G for more information. A variety of information returns are required to report various other types of payments.

Payers responsible for filing 250 or more information returns of one type (for example, Form 1099-MISC) are required to file these electronically. Regardless of whether the returns are filed electronically, a paper statement must be furnished to each recipient unless correct procedures are followed for establishing an electronic system for furnishing statements, including affirmative consent from each individual to receive the information electronically. For more information, see the General Instructions for Certain Information Returns and Publication 1179.

Depositing Taxes

In general, employers are required to deposit federal employment taxes if the total tax liability for Form 941 for the current or previous quarter is $2,500 or more. These taxes are required to be deposited using the Electronic Federal Tax Payment System (EFTPS). You can no longer make deposits using paper coupons. A balance due on the Form 941 or 944 of less than $2,500 is not required to be deposited; it may be paid with the return.

Note: *As of November 30, 2009, federal agencies can no longer use FEDTAX II for deposits and must use EFTPS.* Publication 966 *explains the EFTPS system.*

See Notice 2003-20 for guidance on depositing and reporting of income tax withheld upon distributions from eligible deferred compensation plans described in section 457(b).

When to Deposit

An employer will use either the monthly or the semiweekly schedule for deposit of federal employment taxes. These schedules indicate when a deposit is due after a tax liability arises (a pay date). Before the beginning of each calendar year, employers must determine which of the two deposit schedules they are required to use. The deposit schedule used is based on the total tax liability reported on Form 941 or Form 943 during a four-quarter lookback period as discussed below. ***The deposit schedule is not determined by how often employees are paid.***

Lookback Period

The deposit schedule an employer must use for a calendar year is determined from the total taxes reported on Forms 941 (line 8) in a four-quarter "lookback" period that applies to that year. The lookback period begins July 1 of the second preceding year, and ends June 30 of the preceding year. If the employer reported $50,000 or less of taxes for the lookback period, the employer is a monthly schedule depositor; if it reported more than $50,000, the employer is a semiweekly schedule depositor.

The rules for making deposits are summarized in the table on the next page.

Summary of Federal Tax Deposit (FTD) Rules		
If the employer is a…	**And the payroll date is…**	**Then a deposit must be made:**
Monthly schedule depositor *($50,000 or less during the lookback period)*	Any time during the month	On or before the 15th of the month
Semiweekly schedule depositor *(More than $50,000 during the lookback period)*	Saturday, Sunday, Monday, Tuesday	On or before the following Friday
	Wednesday, Thursday, Friday	On or before the following Wednesday

Special Rules:

$2,500 Rule: Accumulated taxes less than $2,500 in a quarter do not have to be deposited if paid with a timely filed return.

$100,000 Next Day Rule: $100,000 or more within a deposit period must be deposited on the next banking day. Monthly depositors become semiweekly depositors on the next day and remain so for the remainder of the year and all of the following year.

Accuracy of Deposits Rule: An employer who inadvertently underdeposits will not be penalized if the shortfall does not exceed $100 or 2% of the amount of employment taxes required to be deposited. Balance due must be deposited by a shortfall make-up date. See IRS Publication 15 for details.

Deposits on Banking Days Only: If a deposit is required to be made on a day that is not a banking day, the deposit is considered timely made if it is made by the close of the next banking day. Legal holidays (days that are legal holidays in the District of Columbia) are considered non-banking days, as are Saturday and Sunday.

Special Rules for Non-Banking Days: Semiweekly depositors have at least three banking days following the close of the semiweekly period to deposit taxes accumulated during the semiweekly period. For more information, see IRS Publication 15.

Deposit Requirements for Nonpayroll (Form 945) Tax Liabilities

The deposit rules and dollar thresholds to figure when deposits for nonpayroll tax withholding are the same as they are for employment taxes; however, they are aggregated separately, and the deposit thresholds above apply separately. Do not combine Form 945 with deposits for employment tax liabilities (Form 941 or Form 944). See the instructions for Form 945 for details on reporting nonpayroll withholding.

For more information on the deposit rules, see IRS Publication 15. For more information on using the Electronic Federal Tax Payment System (EFTPS), see IRS Publication 966.

Calculating Federal Income Tax Withholding

Employers are generally required to withhold federal income tax from the wages paid to employees. The withheld amount is credited to the employees' individual income taxes.

Each employee should submit a signed Form W-4, *Employee's Withholding Allowance Certificate*, when employment begins. The amount of federal income tax withheld on an employee depends on five factors:

1. Payroll period,
2. Employee marital status, as shown on Form W-4,
3. Amount of wages,
4. Number of withholding allowances claimed by the employee on Form W-4, and
5. Additional amounts the employee requests to have withheld.

Publication 15, furnished by the IRS to each employer at the beginning of each calendar year, contains the tax withholding tables and percentage tables to use to determine actual withholding based on the above criteria. Refer to Publication 15 for specific instructions on calculating withholding from your employees.

Federal Unemployment Tax Act

The Federal Unemployment Tax Act (FUTA) provides a federal-state insurance system for workers who lose their jobs. Most private employers pay both a federal and state unemployment tax. States and their political subdivisions are exempt from paying tax under FUTA. However, state and local government employees, with certain exceptions, must be covered by state unemployment insurance. Contact your state employment or labor agency for more information.

Interest and Penalties

Tax that is not paid when due or in the manner required may be subject to civil penalties as well as interest on the amount due.

Employment Tax Penalties

The following are the most commonly assessed penalties related to employment tax. There are penalties for filing a return late and paying or depositing taxes late, unless there is reasonable cause.

IRC Section	Penalty Assessed For:	Penalty Rates:
6651(a)(1)	Failure to file a tax return (failure to timely file)	5% of the tax due per month up to 25%
6651(a)(2)	Failure to pay tax shown on the return (failure to timely pay) (imposed if the amount of tax shown on the return is not paid on or before the prescribed date)	0.5% (one half of one percent) of the tax due per month up to 25%
6651(c)	Both failure to timely file and failure to timely pay	When both penalties apply for any month, the failure to file penalty is assessed at 4.5%
6652(b)	Failure to report tips	Imposes a penalty for tip income unreported to the employer; the penalty is 50% of the employee social security and Medicare tax on the unreported tip income
6656	**Deposit penalties:**	
	1-5 days late	2%
	6-15 days late	5%
	More than 15 days late, but paid by the 10th day after notice and demand (Notice and demand date is the assessment date)	10%
	Taxes still unpaid after the 10th day following notice and demand	15%
	Failure to deposit electronically	10%
6662	Underpayment of employment taxes due to disregard of the rules and regulations (accuracy-related)	20% of the underpayment attributable to negligence or disregard of rules and regulations
6672	Failure to withhold or pay over trust fund taxes	100% of unpaid tax (see below)

Trust Fund Recovery Penalty

Under section 6672, if withheld taxes that must be withheld are not withheld or are not deposited or paid, the trust fund recovery penalty may apply. The penalty is the full amount of the unpaid trust fund tax. This penalty may be imposed on all persons who are determined by the IRS to be responsible for collecting, accounting for, and paying over these taxes, and who acted willfully in not doing so.

A responsible person can be an officer, employee, or volunteer. A responsible person also may include one who signs checks for the business or otherwise has authority to cause the spending of funds. “Willfully” means voluntarily, consciously, and intentionally. A responsible person acts willfully if the person knows that the required actions are not taking place.

Information Reporting Penalties

The following are the most commonly assessed penalties as they relate to information reporting:

IRC Section	Penalty	Rate for Returns Required To Be Filed January 1, 2011, or Later*
6721	Failure to file correct information returns on or before the required filing date or failure to include all information required to be shown on the return (or where there is incorrect information shown)	The penalty for failure to file information returns without all required and correct information (including missing, incorrect and/or unissued TINs) is $100 for each failure to a maximum of $1,500,000 per calendar year
6722	Failure to furnish correct payee statements on or before the date prescribed to the person to whom such statement is required to be furnished, or a failure to include all of the information required to be shown on the payee statement or where the information is incorrect	The penalty is $100 for each failure, not to exceed $1,500,000 per calendar year, when there is failure to furnish a timely and correct payee statement
6723	Failure to comply with other specific information reporting requirements on or before the prescribed time (usually related to failure to furnish a TIN)	The penalty is $50 for each failure, not to exceed $100,000 per calendar year, when there is failure to comply with any information reporting requirement

* - Reduced penalties may apply for returns filed within 30 days, by August 1, or for entities with gross receipts no more than $5,000,000. See the Instructions for Certain Information Returns for more information.

Interest

Interest is assessed on any taxes due and unpaid, in addition to any penalties that may be imposed. However, the law allows an employer who has made an undercollection or underpayment of social security and Medicare taxes or income tax withholding to make an interest free-adjustment (IRC section 6205(a)(1)). The following two requirements must be met:

1) Correction of the error must be made in the period in which the error was ascertained, and

2) Payment of the tax must be made no later than the due date of the return for the return period in which the error was ascertained. Additional tax due as a result of an IRS examination or ruling may qualify for an interest-free adjustment.

Frequently Asked Questions

1) **If board members are paid nominal amounts, for example, under $1,000 per year, must social security and Medicare taxes be withheld?** Generally, yes. Elected and most appointed officials are employees of the public entity they serve, and are generally subject to the withholding rules that apply to other workers. Withhold social security and Medicare taxes for any official who is either 1) covered under a Section 218 Agreement, or 2) not a qualified participant in a public retirement system (also called a "FICA replacement plan"), and therefore subject to mandatory coverage. Any official elected or appointed after March 31, 1986, is subject to Medicare. See Chapter 4 for more information on who is an employee. [IRS]

2) **What is the statute of limitations date for an adjustment or claim for refund of payroll taxes?** The general rule is that an adjustment or claim for refund of any overpayment of federal payroll taxes must be filed within three years from the date the return was due or three years from the date it was filed, if that date is later. For this purpose, a Form 941 return for any calendar quarter is considered filed on April 15 of the following calendar year, if it is in fact filed by that date. [IRS]

3) **What is the social security tax treatment of prison inmate labor?** Generally, services performed by inmates, for the state or local political subdivision that operates the prison are excluded from social security coverage, whether or not performed outside the confines of the prison. Inmates usually are not in an employment relationship with the state or political subdivision. In general, services performed by inmates, as part of the rehabilitative and therapeutic program of the institution, are not usually performed as employees. Services performed by inmates for an entity other than the state or local governmental unit, e.g., a work-release program, may be covered if an employment relationship exists. The relevant factor for determining social security coverage is whether an employer/employee relationship exists between the inmate and the non-governmental employer, not the place where the inmate is incarcerated. Services performed by inmates outside the institution for the same unit of government that operates it are considered performed *in the institution*. For more information, visit irs.gov and enter "prison industry program" in the search box. [IRS]

4) **Are the services of police officers and firefighters emergency services excluded from social security and Medicare coverage?** Police officers and firefighters are **not** considered emergency workers under the mandatory exclusion from social security and Medicare coverage. This exclusion applies only to services of an employee who was hired because of an unforeseen emergency to work in connection with that emergency on a temporary basis (for example, an individual hired to battle a major forest fire or to provide emergency assistance in other similar disasters such as volcano eruption, severe ice storm, earthquake or flood). Regular, long-term police and fire employees are not emergency workers for this

purpose and subject to the same rules as other public employees to determine whether they are covered by social security. [IRS]

5) **How are tax deposits made?** As of January 1, 2011, employment taxes may no longer be made with paper coupons at federal tax depositaries. They must be made electronically, or, in some cases, may be paid with the tax return. See Publication 15, (*Circular E) Employer's Tax Guide*. [IRS]

Chapter 4

Determining Worker Status

It is critical for any entity paying compensation to know whether its workers are properly classified as employees or independent contractors. In some cases, workers may be designated as employees by a Section 218 Agreement. In other cases, workers may be defined as "statutory employees" or "statutory nonemployees" because specific laws address the occupation (see Publication 15-A for more information on these workers). In general, however, the determination of worker status is made by applying an established common-law standard that addresses the facts and circumstances concerning how the work is performed. Whether workers are employees has significant consequences for tax liability and reporting.

Generally, ***when workers are employees***, the government entity that employs them must withhold and pay employment taxes and file employment tax returns. Employment taxes consist of federal income tax withholding, Old-Age, Survivors and Disability Insurance (OASDI), or social security tax and the Hospital Insurance tax (Medicare tax). The social security tax and Medicare tax make up the Federal Insurance Contributions Act (FICA) contributions, which are paid through employer and employee shares. State and local governments generally pay the social security tax on employees covered under Section 218 Agreements and on employees not covered by a public retirement system (mandatory coverage), and generally pay the Medicare portion on all other employees hired after March 31, 1986. Wages paid by state and local governments are not subject to taxes under the Federal Unemployment Tax Act (FUTA) but state unemployment taxes may apply.

When workers are independent contractors, the governmental entity may have information-reporting and backup withholding responsibilities, but it is not required to withhold and pay employment taxes on behalf of those workers.

This chapter deals with the general rules for determining whether workers are employees, and the laws that apply to different categories of public employment.

Workers Covered Under Section 218 Agreements

As discussed in Chapter 1, states can enter into agreements with SSA to provide social security and Medicare coverage for their employees pursuant to section 218 of the Social Security Act (Section 218 Agreements). If a position is covered by a Section 218 Agreement, then anyone holding that position is an employee. Therefore, the first question for a government to ask about a worker's status is whether the worker is in a position covered under a Section 218 Agreement. If Section 218 coverage applies, this fact takes precedence over other considerations, including the common-law tests discussed below and the mandatory coverage rules.

If you are not sure whether the Section 218 Agreement covers a specific position, contact your State Social Security Administrator, or the SSA Regional Office for assistance. If a group of workers is covered under a Section 218 Agreement, the Agreement cannot be terminated or modified to exclude that coverage group.

Employees who are not covered under a Section 218 Agreement are generally subject to social security and Medicare unless they participate in a public retirement system that serves as a FICA replacement plan, discussed in Chapter 6. However, Medicare taxes generally apply to wages of all state and local government employees hired after March 31, 1986. See Chapter 5, **Social Security and Medicare Coverage**, for further information.

Indian tribal governments are not treated as states for purposes of Section 218. See IRC section 7871 for information on the treatment of Indian tribes as governments. For more information about social security coverage, Medicare, and tribal governments, see the IRS Indian Tribal Governments website.

Common-Law Standard – Employee Status for FICA Purposes

Internal Revenue Code (IRC) section 3121(d)(2) states that, for purposes of social security and Medicare, an employee is "any individual who, under the usual common-law rules applicable in determining the employer-employee relationship, has the status of an employee." The IRS has interpreted the common-law test for determining whether a worker is an employee as whether the service recipient (i.e., the government entity) has the right to direct and control the worker as to the manner and means of the worker's job performance. In other words, does the entity have the right to tell the worker not only what shall be done, but how it shall be done?

All the facts and circumstances must be considered in deciding whether a worker is an independent contractor or an employee. The facts fall into three main categories:

1) Whether the entity has the right to control the behavior of the worker;
2) Whether the entity has financial control over the worker; and
3) The relationship of the parties, including how they see their relationship.

These facts are discussed below, with emphasis given to governmental situations.

Behavioral Control

Facts that fall under this category show whether the entity has a right to direct and control how the worker performs the specific task for which he or she is engaged. Many times, when workers perform their tasks satisfactorily, the entity does not appear to exercise much control. The critical question, however, is whether there is a **right to control**. If the entity has the right to do so, it is not necessary that it actually direct and control the manner in which the services are performed.

The following table addresses the elements of behavioral control with respect to government employees:

Instructions, Training and Required Procedures	An employee is generally subject to the government entity's instructions about when, where, and how to work. The employer has established policies, which the workers are required to learn and follow. Daily or ongoing instructions regarding the expected tasks are especially indicative of employee status. Training is a classic means of explaining detailed methods and procedures to be used in performing a task. Periodic or ongoing training about procedures to be followed and methods to be used indicates that the employer wants the services performed in a particular manner. This type of training is strong evidence of an employer-employee relationship. For instance, police officers and firefighters must be trained to comply with departmental rules and regulations. They do not have the independence characteristic of independent contractors. Other examples of training that indicates employment include a state statute requiring that animal control officers receive state-sponsored training, and a statute requiring that inspectors of sanitary facilities be trained and state-certified. These facts are indicative of a right to control. Election workers are trained to follow uniform procedures established for the polling place. They are directed by a supervisor. These facts suggest they would typically be employees. Government employees often work subject to regulations and manuals, which specify how their jobs are to be done. Teachers are required to receive periodic training in departmental policies. They are required to attend meetings, to follow an established curriculum, to use certain textbooks, to submit lesson plans, and to abide by departmental policies concerning professional conduct. However, some types of training or minimal instructions may be provided to either an employee or an independent contractor, including orientation or information sessions about a government entity’s policies and voluntary programs for which there is no compensation.
Government Identification	Government workers may be required to identify themselves by wearing a uniform, driving a marked vehicle, etc. When an individual represents himself or herself as an agent of a government, that gives the individual an appearance of authority. Wearing a uniform, displaying government identification, or using forms and stationery that indicate one is representing a government are highly indicative of employee status.
Nature of Occupation	The nature of the worker’s occupation affects the degree of direction and control necessary to determine worker status. Highly-trained professionals such as doctors, accountants, lawyers, engineers, or computer specialists may require very little, if any, instruction on how to perform their specific services. Attorneys, doctors and other professionals can, however, be employees. In such cases, the entity may not train the individuals or tell them how to practice their professions, but may retain other kinds of control, such as requiring work to be done at government offices, controlling scheduling, holidays, vacations, and other conditions of employment. Again, the government entity should consult state statutes to determine whether a professional position is statutorily created. On the other hand, professionals can be engaged in an independent trade, business, or profession in which they offer their services to the public, including work for

government entities. In this case, they may be independent contractors and not employees. In analyzing the status of professional workers, evidence of control or autonomy with respect to the financial details is especially important, as is evidence concerning the relationship of the parties as discussed below.

Evaluation Systems

Evaluation systems are used by virtually all government entities to monitor the quality of work performed. This is not necessarily an indication of employee status. In analyzing whether a government entity's evaluation system provides evidence of the right to control work performance, consider how the evaluation system may influence the workers' behavior in performing the details of the job. If there is a periodic, formal evaluation system that measures compliance with performance standards concerning the details, the system and its enforcement are evidence of control over the workers' behavior.

Financial Control

This second category includes evidence of whether the entity controls the business and financial aspects of the workers' activities. Employees do not generally have the risk of incurring a loss in the course of their work, but generally receive a salary for as long as they work. An independent contractor has a genuine possibility of profit or loss. Facts showing possibility of profit or loss include: significant investment in equipment, tools or facilities; unreimbursed expenses, including the requirement to provide materials or hiring helpers; working by the day or by the job rather than on a continuous basis; having fixed costs that must be paid regardless of whether the individual works; and payment based on contract price, regardless of what it costs to accomplish the job.

The following table addresses the elements of financial control.

Method of Payment

The method of payment must be considered. An individual who is paid a contract price, regardless of what it costs to accomplish the job, has a genuine possibility of profit or loss and therefore would not generally be considered an employee. An individual who is paid by the hour, week, or month is typically an employee. However, this is not always the case; for example, independent contractor attorneys usually bill by the hour. An individual who is paid by the unit of work, such as a court reporter, may or may not be an independent contractor, depending on the facts.

Offering Services to the Public

Another factor favoring independent contractor status exists when the individual makes his or her services available to the public or a relevant segment of the market. Relevant questions that address this issue include:

- Does the individual advertise?
- Does the individual use a private business logo?
- Does the individual maintain a visible workplace?
- Does the individual work for more than one entity?

Corporate Form of Business

If the individual is incorporated and observes corporate formalities associated with this status, this makes it unlikely that he or she is an employee of the government entity. (A corporate officer will be an employee of the corporation.) The mere fact

of incorporation or use of a corporate name, however, does not transform an employee into an independent contractor. The corporation must serve an intended business function or purpose, or be engaged in business.

Part-Time Status The fact that workers work on a part-time or temporary basis, or work for more than one entity, does not make them independent contractors. A part-time, temporary or seasonal worker may be an employee or an independent contractor under the common-law rules.

Relationship of the Parties

The third category used to determine worker status is evidence of the relationship between the parties, including how they view their relationship. The relationship of the parties is generally evidenced by examining the parties' agreements and actions with respect to each other, paying close attention to those facts that show not only how they perceive their relationship, but also how they represent their relationship to others.

For example, a fact illustrating how the parties perceive their relationship is the intent of the parties as expressed in a written contract. A written agreement describing the worker as an independent contractor is evidence of the parties' intent, and in situations where it is unclear whether a worker is an independent contractor or employee, the intent of the parties, as reflected in the contract, may resolve the issue.

However, a contractual designation, in and of itself, is not sufficient evidence for determining worker status. The facts and circumstances under which a worker performs services are determinative. The substance of the relationship, not the label, governs the worker's status. See Employment Tax Regulation §31.3121(d)-1(a)(3). The following items may reflect the intent of the parties:

- Filing a Form W-2 or withholding payroll taxes for an individual indicates the entity's belief that the worker is an employee.
- A worker doing business in corporate form, with observance of corporate formalities, indicates the worker is not an employee of the government entity.
- Providing employee benefits, such as paid vacation, sick days and health insurance, is evidence that the entity regards the individual as an employee. The evidence is strongest if the worker is provided with benefits under a tax-qualified retirement plan, section 403(b) annuity or cafeteria plan because, by statute, these benefits can be provided only to employees.

The following are key considerations in evaluating the elements involving the relationship of the parties.

Discharge or Termination

The circumstances under which a business and a worker can terminate their relationship have traditionally been considered useful evidence concerning the status of the worker. However, business practices and legal standards governing worker termination have changed since these general principles developed. Under a traditional analysis, a government entity's ability to terminate the work relationship at will, without penalty, provided a highly effective method to control the worker. The ability to fire at will is indicative of employee status. In the traditional independent contractor relationship, the government entity could terminate the relationship only if the worker failed to provide the intended product or service, thus indicating that the business did not have the right to control how the work was performed. In the current environment, however, a government entity rarely has complete flexibility in discharging employees. The reasons a government entity can terminate an employee may be limited by law, by contract, or by its own practices. Consequently, inability to freely discharge a worker, by itself, no longer constitutes persuasive evidence that the worker is an independent contractor.

Termination of Contracts

Historically, a worker's ability to terminate work at will was considered to illustrate that the worker merely provided labor and tended to indicate an employer-employee relationship. In contrast, if the worker terminated work, and payment could be refused, or the worker could be sued for nonperformance, this traditionally tended to indicate an independent contractor relationship. Today, however, it is more common that independent contractors may enter short-term contracts for which nonperformance remedies are inappropriate, or may negotiate limits on their liability for nonperformance. For example, professionals, such as doctors and attorneys, are typically able to terminate their contractual relationship without penalty. Accordingly, the worker's protection from liability for terminating the relationship does not necessarily indicate employee status.

Non-performance of Employees

Employers may successfully sue employees for substantial damages resulting from their failure to perform the services for which they were engaged. As a result, the presence or absence of limits on a worker's ability to terminate the relationship, by itself, is less relevant in determining worker status. On the other hand, a government entity's ability to refuse payment for unsatisfactory work continues to be characteristic of an independent contractor relationship. Because the meaning of the right to discharge or terminate is so often unclear, and depends primarily on contract and labor law, these facts should be viewed with great caution.

Permanency

The permanency of the relationship between the worker and service recipient is somewhat relevant to determining whether there is an employer-employee relationship. If a worker is engaged with the expectation that the relationship will continue indefinitely, rather than for a specific project or period, this is generally considered evidence of intent to create an employment relationship. However, a long-term relationship may also exist between a government entity and an independent contractor. There may be a long-term contract, or contracts may be renewed regularly due to superior service, competitive costs, or lack of alternative service providers. Part-time, seasonal or temporary workers may also be employees under the common law. The fact that workers do not have full-time, permanent status is irrelevant to their classification.

Common-Law Standard - Summary

In many worker classification cases, some facts will support independent contractor status and others will support employee status. Independent contractors are rarely totally unconstrained in the performance of their contracts, and employees almost always have some degree of autonomy. The determination of a worker's status, therefore rests on the weight given to the facts as a whole, keeping in mind that no one factor is determinative.

Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding

In difficult cases, the IRS can provide a determination as to whether a worker is an employee or an independent contractor. To obtain a determination from the IRS, file Form SS-8. Either a governmental entity or a worker may submit Form SS-8. The IRS will acknowledge receipt of the Form SS-8 and will also request information from the other party. If a contract has been executed between the worker and the entity, a copy of the contract should be submitted with Form SS-8. In some cases, the IRS will contact the State Social Security Administrator to determine whether the entity and position are covered by a Section 218 Agreement. The IRS will generally issue a formal determination to the entity and will send a copy to the worker.

Note: *The SS-8 determination is not an examination. It does not reopen a closed examination or change the findings for years previously examined.*

Employee Status for Income Tax Withholding

"Employment" for income tax purposes is generally governed by regulations under Code section 3401. As explained above, for purposes of social security and Medicare (FICA) FICA, employee status is determined under the common-law control test, unless a Section 218 Agreement is in place and specifically covers the position. In general, the common-law factors apply to the determination of whether a worker is an employee for income tax purposes as it does for FICA taxes. The regulations under IRC 3401(c) contain nearly identical language to the regulations under IRC 3121(d)(2), reciting the same "right to control" text that appears in 31.3121(d)-1(c). See Regulations 31.3401(c)-1.

However, IRC §3401(c) contains a specific provision for government employees for income tax withholding purposes; it states that "the term employee includes an officer, employee, or elected official of the United States, a State, or any political subdivision thereof." Therefore, an officer, employee, or elected official of a state or local government is an employee for income tax withholding purposes.

Classification Issues Involving Government Employee

The following discussion addresses some special worker classification situations involving governmental employees.

Public Officials

The term "public official" refers to someone who has authority to exercise the power of the government and does so as an agent and employee of the government. The Internal Revenue Code does not define the term "public official," but Regulation §1.1402(c)-2(b), addressing of self-employment tax, indicates that holders of "public office" are not in a trade or business and are therefore not subject to self-employment tax. This Regulation states that the performance of the functions of a public office does not constitute a trade or business. If self-employment tax is not applicable to the services, the individuals who perform them are presumed to be employees.

An exception to this rule applies for certain public officials paid solely on a fee basis (see Chapter 5). The regulations give the following specific examples of positions that constitute "public office":

- Governor
- Mayor
- Member of a legislature or elected representative (i.e., elective office)
- County commissioner
- State or local judge, or justice of the peace
- County or city attorney
- Marshal, sheriff, constable
- Registrar of deeds
- Tax collector or tax assessor
- Road commissioners
- Members of boards and commissions, such as school boards, utility districts, zoning boards, and boards of health

However, it may not always be clear whether a worker holds public office. In *Metcalf & Eddy v. Mitchell*, 269 U.S. 514 (1926), the U.S. Supreme Court addressed the definition of an officer, and whether consulting engineers hired by states or subdivisions of states were independent contractors or "officers and employees" of a state. The Court ruled that an office is a public station conferred by the appointment of a government. The term "officer" includes the idea of tenure, duration, emolument and duties fixed by law, and where an office is created, the law usually determines its term, its duties, and its compensation. The Court concluded that the consulting engineers were not officers of the state or a subdivision of it, and were independent contractors. Public officials will generally have the characteristics of common-law employees.

Therefore, depending on the facts presented, a worker who is compensated for services performed for a government may be an independent contractor and not a public official or employee.

If there is some question as to whether a worker is a public official and employee, a critical factor to consider is whether there is a provision of the state constitution or a statute establishing the position. State statutes should be reviewed to determine whether they

establish enough control for the individual to be classified as an employee under the common-law test. A statute may state that a specific position is that of a public official, in which case there is likely to be a right to control sufficient to make the individual an employee. Statutes may also specify the duties of a public office and generally establish the officer's superiors and subordinates, if any. Statutes establish an official's term of office and sometimes the compensation. They may require that a public official take an oath of office. Statutes often establish general and specific penalties for dereliction of duty. For instance, members of boards who are paid for each meeting they attend may face termination if they fail to attend a certain number of meetings.

> **Example.** State A establishes the position of city attorney by statute, and indicates that the position holder is an officer and an employee. This statute defines the duties of the position. The city attorney is required to direct all litigation in which the city is a party, including prosecution of criminal cases; to represent the city in all legal matters in which the city or a city officer is a party; to attend meetings of the commissioners, advise commissioners, mayors, etc., on all legal questions, and approve all contracts and legal documents. A city manager appoints, supervises and controls the work of the city attorney. The city attorney must take an oath of office. These facts show the importance of state statutes in establishing a right of direction and control over a public official and thus classifying the individual as a common-law employee.

Elected Officials

For social security and Medicare purposes, elected officials (also referred to as "individuals in elective positions"), are subject to a degree of control that typically makes them employees under the common law, and therefore subject to these taxes. Elected officials are responsible to the public, which has the power to vote them out of office. Elected officials may also be subject to recall by the public or a superior official. Very few elected officials have sufficient independence to be considered independent contractors. Under IRC 3401, wages, for income tax withholding purposes, include all remuneration, other than fees paid to a public official. Because elected officials receive wages, not fees, they are employees for income tax withholding purposes, regardless of any determination for social security and Medicare purposes.

Home Care Service Recipients

A home care service recipient (HCSR) is an individual who receives home care services while enrolled in a program administered by a federal, state, or local government agency that provides funding for that individual's home care services. Home care services include health care and personal attendant care services rendered to the HCSR. Generally, the HCSR is considered the employer of the service provider under the common-law rules. The provision of home care services generally constitutes household employment.

The HCSR may request that the IRS authorize, under section 3504, an agent to act on his or her behalf to withhold, report, and pay the federal employment taxes with respect to the workers who provide home care services. See Revenue Procedure 70-6 and Form 2678, Employer/Payer Appointment of Agent. Special rules apply when a state or local government agency acts as the section 3504 agent. See Revenue Procedure 80-4 and Notice 2003-70. A state or local government agency acting as a section 3504 agent on behalf of a HCSR files an aggregate Form 941 and aggregate Form 940, attaching Schedule R (Form 941), Allocation Schedule for Aggregate Form 941 Filers, and Schedule R (Form 940), Allocation Schedule for Aggregate Form 940 Filers. Agencies must have an employer identification number separate from the one used to report taxes of its own employees for this purpose. The state agent may engage a reporting agent or subagent to perform the reporting and payment of employment taxes that the state agent would otherwise perform on behalf of the service recipient. See Notice 2003-70 for the correct reporting procedures.

Volunteer Firefighters

Compensation paid in an employer-employee relationship is taxable wages (unless an exclusion applies), regardless of whether the workers are termed "volunteers." In some cases, rather than receive salaries, firefighters may receive amounts intended to reimburse them for expenses. They may also receive other cash or in-kind benefits that may be wages. Unless these reimbursements are paid under an ***accountable plan***, discussed in Chapter 3, these reimbursements are taxable as wages.

Amounts that are termed "reimbursements" but that are not paid under an accountable plan are treated as wages and subject to income and social security and Medicare taxes. Therefore, a *per diem* or fixed amount paid to a firefighter (or other worker), that does not reimburse actual, documented expenses, is includible in income and subject to income tax withholding, social security and Medicare.

The services of volunteers are generally not eligible for the exclusion from FICA for emergency workers, discussed in Chapter 5 . IRC §3121(b)(7)(F)(iii) provides that services performed by employees on a temporary basis in the case of fires, storm, snow, earthquake, floor or other similar emergency are exempt from employment. Firefighters who are on call and work part-time or intermittently do not qualify for the emergency worker exclusion. This exception applies only for temporary workers who are hired because of an unforeseen emergency.

Medical Residents

Medical residents are generally common-law employees of the hospitals for which they work, and therefore are subject to social security and Medicare taxes (unless they are excepted by a Section 218 Agreement). IRC 3121(b)(10) provides an exception for students employed by a school, college, or university (SCU) who are enrolled and regularly attending classes at the SCU. However, this exception is not available to full-time employees. Under regulation section 31.3121(b)(10)-2(d)(3)(iii), an employee whose normal work schedule is 40 hours or more per week is always considered a full-time

employee. Therefore, medical residents generally do not qualify to exclude payments for their services from social security and Medicare taxes.

Identity of the Employer for Tax Purposes

In certain cases it is clear that the work in question is performed by employees, but it may not be clear which of two or more entities, organizations, or individuals is the employer. This situation may arise when workers are supplied or paid by one entity but work under the direction of another (for example, leased workers).

The term "employer" is defined in IRC §3401(c), for income tax withholding and reporting purposes, as the person for whom an individual performs any service, of whatever nature, as an employee. However, an exception is provided if the person for whom the individual performs the services does not have control of the payment of the wages. In this situation, the term "employer" means the person having legal control of the payment of the wages. See IRC §3401(d)(1) and Regulation 31.3401(d)-1(f).

When a question is raised about the identity of the employer, all facts relating to the employment must be considered. If there is any provision in a statute or ordinance that authorizes the employment by a government entity of the individual, and the individual is hired under this authority, the individual is generally an employee of that governmental entity. Any statutory provisions relating to the relationship should be reviewed. If there is no applicable statutory authority, the identity of the employer must be determined under the common-law control test.

Employee Status for Other Purposes

A state or federal agency may make determinations of employee status for Workers' Compensation, minimum wage, or other purposes. The state or federal agency may apply different standards from those used to determine worker classification for federal employment tax purposes. Characterizations of individuals as employees based on state or non-tax laws should be weighed with caution, and in some cases disregarded, because the laws or regulations involved may use different definitions of an employee for their purposes.

Independent Contractor Reporting Responsibilities

Independent contractors are subject to social security and Medicare taxes under the Self-Employment Contributions Act (SECA). Generally, payments to independent contractors of $600 or more during a calendar year must be reported on Form 1099-MISC, Miscellaneous Income. Independent contractors are required to provide a taxpayer identification number (TIN) to the entity that pays them. Form W-9, *Request for Taxpayer Identification Number*, contains the required certification and can be used for this purpose.

For more information about requirements for information reporting to independent contractors, see the Instructions for Form 1099-MISC.

Workers who have been treated as independent contractors but are later determined to be employees will need to file amended returns if they reported income on Form 1040, Schedule C, and calculated self-employment tax (SECA) on Schedule SE. A worker in this situation should use Form 8919, *Uncollected Social Security and Medicare Tax on Wages*, to figure and report the employee share of the FICA tax. Entities that misclassify employees as independent contractors may be held liable for back taxes, penalties and interest.

Worker Providing Services as an Employee and as an Independent Contractor

Individuals who are employees with respect to some services may not be employees with respect to other services they provide. For example, a teacher may be retained to remove snow from school property. This individual may be an employee as a teacher but an independent contractor for the snow-removal activity. Apply the common-law rules separately to each activity to establish whether it is an independent trade or business. Revenue Ruling 58-505 explains that for an individual to work in two capacities (employee and contractor), the services must not be interrelated. Stated differently, an individual does not work in two capacities when the same type of work, such as legal services, is divided into two components, one in an employee capacity, and one in an independent contractor capacity. The services and remuneration for the two activities must be separate.

Section 530 Relief

State and local government entities under examination by the IRS may be entitled to relief from employment tax for certain workers under Section 530 of the Revenue Act of 1978 ("Section 530"). If applicable, Section 530 terminates an entity's federal employment taxes, including social security and Medicare, income tax withholding, and any penalties attributable to the liability. See Revenue Procedure 85-18. This relief is not available for services covered by a Section 218 Agreement.

If the requirements for relief are met, the entity may obtain relief from liability for income tax withholding for prior years. However, Section 530 relief from income tax withholding will not apply with respect to wages paid after the date on which the entity is advised that the workers are covered under a Section 218 Agreement. This is because the entity would have begun withholding FICA taxes, which constitutes treatment of the workers as employees. See Revenue Procedure 85-18, section 3.03(C) and 3.04.

Section 530 provides relief for an entity that treated workers as nonemployees if the entity had a reasonable basis for the classification and acted consistently on that basis. To qualify for Section 530 relief, the entity must have a reasonable basis for treating the worker as an independent contractor. Section 530 provides three safe harbors for satisfying the reasonable basis requirement:

1) Published ruling or judicial precedent;
2) Prior IRS examination of the taxpayer (if after 1996, the examination must have included a review of worker classification); or
3) Longstanding recognized practice of a significant segment of the industry. Alternatively, an entity may establish some other reasonable basis. For more information, see Revenue Procedure 85-18.

In addition, the entity must:

1) Have filed all federal tax returns (including information returns) on a basis consistent with treatment of the worker as a nonemployee; and
2) Not have treated the worker, or any other worker in a substantially similar position, as an employee.

Tax Consequences for Workers

In some cases, a government entity may be entitled to relief under Section 530, but workers find, through a determination letter or some other means, that they have been misclassified and are employees. Section 530 does not extend relief to workers. It does not convert them from employees to independent contractors. Misclassified employees are liable for the employee share of social security and Medicare taxes rather than for SECA (self-employment) tax. (See Form 8919, *Uncollected Social Security and Medicare Tax on Wages*.) If they have been filing income tax returns as independent contractors, they should file amended returns for years for which the statute of limitations is open. As employees, they are not entitled to deduct employee business expenses on Schedule C. Because their employers are entitled to continue treating them as independent contractors, the workers will not be subject to income tax, social security or Medicare withholding, and will generally have to make estimated tax payments to cover their tax liabilities.

For more information about the requirements for Section 530 relief, see Publication 1976, *Do You Qualify for Relief Under Section 530?*

Note: *Section 530 is not part of the Internal Revenue Code. It was originally intended as an interim relief measure, but was extended indefinitely in 1982*.

Frequently Asked Questions

1) **What are the consequences of misclassifying a worker?** Generally, when an employer erroneously classifies an employee as an independent contractor and does not withhold federal payroll taxes, the employer is liable for the employer and employee shares of all applicable federal payroll taxes, as well as various penalties and interest. [IRS]

2) **What do you do if you cannot determine whether a worker is an employee?** The state or local entity and/or the worker can request a formal determination by

submitting to the IRS Form SS-8, *Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding*. When Form SS-8 is submitted to the IRS, all the facts are analyzed and the determination of the worker's status is presented to the worker and the service recipient. [IRS]

3) **Are volunteers considered employees?** The common-law tests apply to determining the status of individuals regardless of whether they are deemed "volunteers." If an individual considered a volunteer meets the common-law tests, any form of compensation or benefit he or she receives is considered wages, unless a specific exception applies. [IRS]

4) **What effect does the presence of a Section 218 Agreement have on worker status?** If an existing Section 218 Agreement classifies a position as that of an employee, covered by the Agreement, then an individual in that position is an employee, subject to FICA and income tax withholding; the common-law tests are not considered. Positions not covered by a Section 218 Agreement should be evaluated under the common-law tests. [SSA/IRS]

Chapter 5

Social Security and Medicare Coverage

As discussed in Chapter 3, cash or noncash compensation for services is subject to income, social security, and Medicare taxes unless certain exceptions apply. In addition to the exceptions for certain payments, state and local employees may be exempted from social security (and in some cases, Medicare) taxes based on coverage under a public retirement system. A public employee may be covered for social security and Medicare, Medicare only, or may be exempt from both. The flowchart in Chapter 1, "Social Security and Medicare Coverage of State and Local Employees," illustrates the process for determining the social security and Medicare coverage that applies to an employee. This chapter addresses various categories of employees and rules by which coverage is established, including the process for obtaining coverage under a Section 218 Agreement ("Agreement"). As a supplement to the social security coverage information provided in this publication, refer to the State and Local Government Employers page on the SSA website. Additional information is also available on the IRS FSLG home page.

All state and local government employees fall into one of three categories with respect to social security coverage:

1) Employees under Section 218 coverage (also called "voluntary coverage"). These employees are covered for social security by a voluntary Section 218 Agreement between the State Administrator and the SSA. They may or may not participate in a public retirement system. This chapter discusses coverage under Section 218 Agreements. (Public retirement systems are discussed in Chapter 6.)

2) Employees under mandatory social security coverage. These employees are required to be covered for amounts that are deemed to be wages, because they are not members of a qualifying public retirement system and are not covered by a Section 218 Agreement. Government employees not covered by a public retirement system or social security are subject to mandatory coverage after July 1, 1991.

3) Employees with no social security coverage. These employees are covered by a qualifying public retirement system, and are therefore exempt from mandatory social security. They are not covered by a Section 218 Agreement.

Each of the three categories of employees is discussed below.

1) Employees Under Section 218 Coverage

State and local government employees can be covered for social security and Medicare through a Section 218 Agreement between the state and the SSA. This agreement may provide any of the following:

- Coverage for groups of employees in positions covered by a retirement system
- Coverage for groups of employees in positions not covered by a retirement system
- Coverage for employees in positions that are excluded from mandatory coverage provisions, but are optional exclusions under Section 218 Agreements (for example, student services).
- Medicare Hospital Insurance (HI)-only coverage for employees hired prior to April 1, 1986, who are members of a public retirement system.

Each state's original Agreement incorporates the basic provisions, definitions, and conditions for coverage. Only the State Social Security Administrator can initiate a request for Section 218 coverage on behalf of an entity in the state. Additional coverage can be provided by modifications. Each modification, like the original Agreement, is binding upon all parties.

In order to establish an Agreement, authority must exist under state law (state enabling legislation) to enter into an Agreement and to extend coverage under an Agreement. The types and extent of coverage provided under an Agreement must be consistent with federal and state laws.

State and local government employees who are covered under an Agreement have the same benefits, rights, and responsibilities as employees who have mandatory social security coverage. The cost to the employer of providing social security protection for state and local government employees is the same as that for employees in mandatory coverage.

Coverage under an Agreement must be provided for groups of employees. An Agreement may be modified to increase, but ***not*** to decrease, the extent of coverage. (An exception applies to election worker services and solely fee-based positions; see **Optional Section 218 Exclusions** below.)

Termination of Agreements

Before legislation was enacted in 1983, states could terminate coverage for any group of employees covered under the state's Section 218 Agreement. A state did this by providing a two-year advance notice to the federal government. Once it was terminated, the coverage for this group of employees could not be reinstated. The 1983 Social Security Amendments rescinded this provision and prohibited states from terminating coverage on or after April 20, 1983, but permitted states to cover again any group terminated before this date.

Coverage Groups

Coverage under Section 218 Agreements can be extended only to groups of employees, referred to as coverage groups. Once an employee position is covered under a Section 218 Agreement, any employee filling that position is a member of the coverage group for social security and Medicare. There are two types of coverage groups: **1)** an **absolute,** or

non-retirement, coverage group (employees not in a retirement system); and **2)** a **retirement system coverage group**. Each state decides, within federal and state law, which groups to include under its Agreement, and when their coverage begins. The state can choose to cover non-retirement system groups, retirement system groups, or both.

Absolute Coverage Groups (Non-Retirement System Groups)

An **absolute coverage group** includes the services of employees in positions not covered by a retirement system, except those whose services are mandatorily or optionally excluded from social security and Medicare coverage. They may also be referred to as **non-retirement system groups** or **Section 218(b)(5) groups**. A state may extend Section 218 coverage to an absolute retirement system group without considering the desires of the employees. An absolute coverage group may consist of any of the following:

- All employees of a state engaged in performing services in connection with governmental (nonproprietary) functions
- All employees of a state engaged in performing services in connection with a single proprietary function
- All employees of a political subdivision of a state engaged in performing services in connection with governmental (nonproprietary) functions
- All employees of a political subdivision of a state engaged in performing services in connection with a single proprietary function
- Certain civilian employees working with the National Guard of a state
- Individuals employed under an agreement between a state and the United States to perform services as inspectors of agricultural products

Retirement System Coverage Group

A retirement system coverage group consists of employees working in positions covered by a public retirement system (FICA replacement plan), as provided in section 218(d)(4) of the Social Security Act (Act). Such a group may be provided social security and Medicare coverage under an Agreement only if approved by a referendum. The Act gives the state the option, for referendum purposes, of breaking down a retirement system into its components. If a retirement system covers positions of employees of one or more political subdivisions of the state, the state has the following choices. It may hold a referendum for:

1) All employees in positions under the retirement system
2) State employees in positions under the system
3) Employees of one or more political subdivisions in positions under the system
4) Any combination of the groups in (2) and (3)
5) Employees of a hospital that is an integral part of a political subdivision
6) Employees of two or more hospitals (each hospital must be an integral part of the same political subdivision); or
7) Employees of each institution of higher learning

The referendum for retirement system employees is conducted either on a majority vote basis (allowed in all states), or on a divided system basis (allowed in certain states).

Majority Vote Referendum

Under this type of referendum, social security and Medicare coverage may be extended to employees in positions covered by a retirement system only if a majority of the eligible employees vote in favor of such coverage. A majority of ***all*** of the eligible employees under the system (not a majority of the eligible employees casting votes), must vote in favor of coverage. All states are authorized by federal law to use the majority vote referendum procedures. Although the referendum itself is a state matter, federal law requires that the following conditions be met to establish coverage:

1) Eligible employees are given not less than 90 days notice of the referendum
2) An opportunity to vote is given, and limited to eligible employees who were in an employment relationship with the employer both on the date the notice was given and on the date the referendum is held
3) The referendum is held by secret ballot
4) The referendum is supervised by the governor (or his/her designee)
5) A majority of the retirement system's eligible employees vote for coverage

Divided System Retirement Referendum

In addition to the majority vote referendum procedure, certain states and all interstate instrumentalities are authorized to divide a retirement system based on whether the employees in positions under the retirement system want coverage. Under the divided vote referendum, only those employees who vote "yes" and all future employees who become members of the retirement system will be covered. Members who vote "no" are not covered as long as they maintain continuous employment in a position within the same public retirement system coverage group.

The states having this authority under Section 218(d)(6)(c) of the Act are:

Alaska	Illinois	New Jersey	Tennessee
California	Kentucky	New Mexico	Texas
Connecticut	Louisiana	New York	Vermont
Florida	Massachusetts	North Dakota	Washington
Georgia	Minnesota	Pennsylvania	Wisconsin
Hawaii	Nevada	Rhode Island	

These "divided vote" states may choose between a divided system vote and a majority vote referendum.

States authorized to use the divided vote retirement system referendum to extend coverage may use either of two voting procedures:

1) ***Simplified One-Step Method:*** Poll all eligible members and divide the system into two parts, with each member placed in either the "Yes" or "No" group based on his or her choice (simplified one-step referendum), or

2) ***Original Two-Step Method:*** Subdivide the retirement system into two parts or systems – "Yes" and "No" groups - based on individual members' choices and then, after the individuals are separated based on this preference, conduct a majority vote referendum among the "Yes" group. These individuals can then change their original poll vote.

The conditions for a divided vote referendum are the same as those given for the majority vote referendum with two exceptions: (1) the ballots are not secret, because the individuals choosing coverage must be identified, and (2) the individual must be in an employment relationship and a member of the retirement system when the vote is held (but not necessarily when the referendum notice was given).

At the discretion of the state, employees who become members of the retirement system after the referendum (division) date and before the execution of the modification extending coverage to the retirement system coverage group may be given a choice to receive coverage.

The referendum procedures must be conducted under the direction of the State Social Security Administrator.

Continuation of Coverage Rules

Once coverage is provided for state and local government employees, it generally continues unless an event occurs that results in termination of the coverage, such as a change in employer. The continuation rules are applied for each type of coverage group as follows:

Absolute Coverage Group: Social security and Medicare coverage for non-retirement system groups continues as long as the continuing governmental entity exists. This is true even if the positions are later placed under a retirement system. (This provision includes police and firefighter positions that were first covered as an absolute coverage group.)

Majority Vote Retirement System Group: Following a favorable majority vote referendum, services under the retirement system, including positions brought under the retirement system in the future, are compulsorily covered for social security under the State's Section 218 Agreement. Social security and Medicare coverage will continue as long as the continuing governmental entity exists, even though the positions are later removed from under the retirement system, the system is abolished, or the positions are placed under an additional retirement system.

Divided Vote Retirement System Group: If the use of procedure (2) above – the original two-step referendum – results in a favorable majority, then the entire "Yes" group ***and*** all future members of the retirement system are covered.

As a result of procedure (1) – the simplified one-step referendum – all those retirement system members who voted "Yes" and all future retirement system members are covered for social security. If all current retirement system members vote against social security coverage (the "No" group), then only future retirement system members will be covered for social security and make up the "Yes" group.

Under a divided retirement system, employees carry the "no" or "yes*"* vote with them if they transfer to another position within the same retirement system coverage group. Social security coverage is not terminated because the positions are later covered under an additional retirement system.

If the divided vote retirement system is later abolished or positions are removed from coverage under it, the "Yes" group (those employees who voted "Yes" in the referendum and those subsequently hired retirement system members) continue to be covered for social security. New employees hired into positions after the removal from, or abolishment of, the former retirement system, are not covered for social security because they would not be considered new members of that former retirement system.

Section 218 Coverage Exclusions

When a state or local government entity voluntarily enters into the state's Section 218 Agreement with the Social Security Administration, it is important to determine which employee services will be excluded from social security coverage. If services are excluded, any employees performing these services are not covered by the Agreement.

Certain services – known as **mandatory exclusions –** are excluded from voluntary social security coverage by Section 218(c)(6) of the Social Security Act.

Other services, however, are **optional exclusions** under Section 218(c)(3), (5) and (8) and, therefore, may be covered under a voluntary Section 218 Agreement. Coverage under a Section 218 Agreement supersedes all other considerations. If optional exclusion services are covered under a Section 218 Agreement, these amounts are subject to social security and Medicare tax.

Mandatory Section 218 Exclusions

Federal law requires the exclusion of the following services from section 218 coverage under Section 218(c)(6) of the Social Security Act:

- **Services performed by individuals hired to be relieved from unemployment.** The intent of the program establishes whether the program is designed to relieve individuals from unemployment. This is usually determined from the statutes or

other authorities that established the program. The exclusion does not include services performed by individuals under programs, such as work-study, where the primary purpose is to provide work experience and training to increase the employability of the person, because the primary intent of such programs is not to relieve them from unemployment.

- **Services performed in a hospital, home or other institution by a patient or inmate thereof as an employee of a state or local government**. Generally, these services are performed by individuals who are not normally in an employment relationship with the state or political subdivision. In the case of work performed by inmates in a state prison or local jail, they are excluded from coverage, whether or not the services are performed outside the confines of the prison or jail, because in either case the inmates are normally not in such an employment relationship with the state or political subdivision. However, services performed by inmates outside the prison or jail for an entity other than the state or local government operating the prison or jail, such as on a work-release program, may be covered if an employment relationship exists. The employer for tax purposes is determined under the common-law rules, discussed in Chapter 4. **Note:** Services performed by patients or inmates as part of the rehabilitative or therapeutic program of the institution are not usually considered to be services performed by employees.

- **Covered transportation service.** This includes services performed by transportation system employees who are covered for Social Security under Section 210(k) of the Social Security Act.

- **Other services that would be excluded if performed for a private employer because the work is not defined as employment under Section 210(a) of the Social Security Act.** This includes services performed by a nonresident alien temporarily residing in the U.S. holding an F-1, J-1, M-1 or Q-1 visa, when the services are performed to carry out the purpose for which the alien was admitted to the U.S. (A state may optionally include certain agricultural services under a Section 218 Agreement.) See the section Foreign Students, Teachers and Apprentices later.

- **Services performed by an employee hired on a temporary basis in case of fire, storm, snow, earthquake, flood or similar emergency.** This exclusion applies only to those who are hired on a temporary basis in response to a specific emergency. It does not include workers considered temporary for other reasons, or individuals in a continuous employment relationship who perform services related to emergencies on a regular or continuing basis.
- **Service described in section 210(a)(7)(F) of the Social Security Act that is included as "employment" under section 210(a).** Services by individuals not covered by a public retirement system and subject to mandatory coverage are excluded from coverage under a Section 218 Agreement.

Caution: Mandatory exclusions apply to **voluntary** social security coverage situations (through a Section 218 Agreement) and should not be confused with the different set of exclusions that applies to **mandatory** social security coverage situations.

Optional Section 218 Exclusions

Under a Section 218 Agreement, a state has the option to exclude from social security coverage the services listed below when they are performed by members of any coverage group, including retirement system coverage groups. If the Agreement does not specifically exclude these services, they are covered.

The following are positions and services that may be excluded at the option of the state:

- **All services in any class or classes of elective positions.** These are positions filled by an election; they also may be referred to as "elected officials." The election may be by a legislative body, a board or committee, or by the qualified electorate of a jurisdiction. The method of selection must constitute an election under state law. The election may be conducted through open voting by the electorate at large, or by a chosen body from a list of candidates. Generally, elective positions fall into three classes: executive, legislative, and judicial.

- **All services in any class or classes of part-time positions.** A part-time position is one for which the number of work hours normally required by the position in a week or a pay period is less than the normal time requirements for the majority of the positions in the employing entity. The part-time position exclusion is based on the normal time requirements of the position and not the time spent by an employee in the position. If a position is established as a full-time position, but the employee works part-time in this position, the exclusion does not apply. Conversely, if a position is established as a part-time position and the employee works full time in this position, the services of the employee are excluded. Whether seasonal or temporary positions that require full-time services for a period of short duration are part-time positions depends on the definition of part-time established for the coverage group. Where the part-time position exclusion is taken, the state should include a definition of "part-time" in the modification if one has not been previously established.

  Note: *The definition of "part-time" under a Section 218 Agreement provisions may be different from the definition of "part-time" used to determine whether an individual is a qualified participant in a public retirement system (discussed in Chapter 6).*

Example: A city provides social security coverage to some of its employees under a Section 218 Agreement, but excludes services performed in part-time positions. The Section 218 Agreement defines part-time positions as positions normally requiring less than 50 hours of service per month. The city must apply the definition in the Section 218 Agreement to determine which employees are excluded from social security coverage under the Agreement. Any employees excluded from coverage under the Agreement may then be subject to mandatory coverage.

- **All services in any class or classes of positions compensated solely by fees received directly from the public, by an individual who is treated by the municipality as self-employed.** See the section **Fee-Based Public Officials**, later.

- **Agricultural labor, but only those services that would be excluded if performed for a private sector employer.** A state that initially excludes agricultural labor may later modify its agreement to cover it. However, if agricultural labor is not excluded initially, it cannot be excluded later. If a state has not taken the agricultural exclusion, then all remuneration for agricultural labor is covered for social security.

- **Services performed by students enrolled and regularly attending classes at the school, college or university for which they are working.** The student exclusion applies only during periods of regular school attendance, whether during the regular academic year or in summer session. The exclusion does not apply to work done during summer vacation if the student is not attending a summer session. Services performed by students during holidays, weekends, seasonal breaks, and between semesters falling within the academic year when classes are not scheduled, are excluded.

- **Services performed by election officials or election workers paid less than the calendar year threshold amount mandated by law.** (If the state's Section 218 Agreement does not have an election-worker exclusion or the entity has an Agreement that does not exclude election workers, social security and Medicare taxes apply from the first dollar paid.) See the section **Election Officials and Election Workers**, later.

Note: *Effective July 2, 1991, elective and part-time positions, although optionally excluded under a Section 218 Agreement, must be covered under a qualifying public retirement system or else they will be covered for social security under the mandatory social security provisions.*

Optional exclusions can be taken by the state in any combination and applied to both absolute and retirement system coverage groups. Any services a state excludes can be

included later if permitted by federal and state law and the state's Agreement. Generally, if one of the types of work listed above has been included in a coverage group, it cannot later be removed from coverage, except for services performed by (1) election officials/workers, and (2) solely fee-based positions.

Optional exclusions apply only to voluntary social security coverage under a Section 218 Agreement; there are no optional exclusions from mandatory coverage.

Note: *The 1972 Amendments to the Social Security Act allowed states a limited period to exclude services in part-time positions and services performed by students, in cases where this exclusion was not initially chosen. An additional window to make this election was provided by Public Law 105-277, enacted October 21, 1998, which allowed states a limited period to exclude the services of students employed by the public school, college or university where they are regularly attending classes. In those states exercising this option, the student exclusion was effective July 1, 2000. Where a state used either or both of these special one-time provisions for excluding services that had been covered previously, it cannot again cover these services under a Section 218 Agreement.*

2) Employees Under Mandatory Social Security Coverage

Public Law 101-508 mandated full social security coverage beginning July 2, 1991, for state and local government employees who are not members of a qualifying public retirement system (also called a "FICA replacement plan") and who are not covered under a Section 218 Agreement, unless a specific exclusion applies under the law.

If an employee is mandatorily covered for social security, then becomes a member of a qualifying public retirement system, mandatory coverage ends; social security coverage would apply only if the position becomes covered by a Section 218 Agreement.

If an employee becomes a member of a public retirement system and is covered for social security under a Section 218 Agreement, the employee continues to be covered for social security and Medicare.

The determination of whether an employee is covered by mandatory social security is made on an individual basis. For example, a Section 218 Agreement may exclude part-time positions, and a public retirement system may exclude part-time employees for the same entity. If an employee is excluded from section 218 coverage because of work performed in a part-time position, (as defined under the Agreement), and is also excluded from membership in a public retirement system because of part-time status, that employee is subject to mandatory social security.

> **Example:** A city has a Section 218 Agreement that excludes part-time positions requiring less than 18 hours of work a week. City cafeteria positions require employees to work only 3 hours per day, or 15 hours per week. The city's public retirement system does not allow

membership for employees unless they work 25 hours or more per week. The cafeteria workers are subject to mandatory social security.

Exclusions from Mandatory Social Security Coverage

Under Section 210(a) of the Social Security Act, the following categories of employees are not subject to mandatory social security coverage, even if they are not covered by a public retirement system:

- **Services performed by individuals hired to be relieved from unemployment.** The intent of the program establishes whether the program is designed to relieve individuals from unemployment. This is usually determined from the statutes or other authorities that established the program. The exclusion does not include services performed by individuals under programs, such as work-study, where the primary purpose is to provide work experience and training to increase the employability of the person, because the primary intent of such programs is not to relieve them from unemployment.

- **Services performed in a hospital, home or other institution by a patient or inmate thereof as an employee of a state or local government**. Generally, services performed by inmates in a state prison or local jail are excluded from coverage. This is true whether or not the services are performed outside the confines of the prison or jail, because the inmates are not normally in an employment relationship with the state or political subdivision. However, services performed by inmates outside the prison or jail for an entity other than the state or local government operating the prison or jail, such as on a work-release program, may be covered if an employment relationship exists. The employer for tax purposes is determined under the common-law rules, discussed in Chapter 4. ***Note:*** Services performed by patients or inmates as part of the rehabilitative or therapeutic program of the institution are generally not employment.

- **Services performed by an employee hired on a temporary basis in case of fire, storm, snow, earthquake, flood or similar emergency.** This exclusion applies only to those workers who are hired on a temporary basis in response to a specific emergency. It does not include workers considered temporary for other reasons, or individuals in a continuous employment relationship who perform services related to emergencies on a regular or continuing basis.

- **Services performed by election officials or election workers paid less than the calendar year threshold amount mandated by law, unless a Section 218 Agreement covers election workers.** See the section **Election Officials and Election Workers,** below**.**

- **Services in positions compensated solely by fees that are subject to self-employment tax (SECA), unless a Section 218 Agreement covers these services.** See the section **Fee-Based Public Officials**, below.

- **Services performed by a nonresident alien temporarily residing in the U.S. holding an F-1, J-1, M-1 or Q-1 visa, when the services are performed to carry out the purpose for which the individual was admitted to the U.S.** See the section **Foreign Students, Teachers and Apprentices** below.

- **Services performed by students enrolled and regularly attending classes at the school, college or university where they are working, unless a Section 218 Agreement covers student services.**

- **Services that would be excluded if performed for a private employer because the work is defined as employment under Section 210(a) of the Social Security Act, unless a Section 218 Agreement covers certain agricultural services.**

Note: *Coverage under a Section 218 Agreement always takes precedence over other employment circumstances. When considering whether the mandatory social security coverage and exclusion rules apply to a worker's services, first determine whether the services are covered by a Section 218 Agreement.*

Election Officials and Election Workers

Prior to the 1967 Social Security Amendments, there was no specific provision for the exclusion of election officials or election workers. The Social Security Act was amended for years beginning with 1968 to allow states to modify their Agreements to exclude the services of election officials and election workers whose pay was below an annually determined threshold amount.

The Federal Insurance Contributions Act (FICA) tax exclusion for election officials and election workers is $1,600 for the calendar year beginning January 1, 2015, unless those wages are subject to social security and Medicare at a lower threshold under the state's Section 218 Agreement.

If the entity is covered by a Section 218 Agreement, the Agreement determines the treatment of election workers for FICA purposes. The Agreement may specify a lower threshold amount for election officials and election workers (for example, $50 a calendar quarter or $100 a calendar year). In these states, the social security and Medicare tax applies when the amount specified in the state's Agreement is met. States may modify the Agreement to exclude the services of election officials and election workers paid less than the threshold amount mandated by law. Such modifications are effective in the calendar year the modification is mailed or delivered to the Social Security Administration.

If the Section 218 Agreement does not exclude election workers from coverage, or does not provide a threshold for coverage, social security and Medicare taxes apply from the first dollar paid. If the entity is not covered under a Section 218 Agreement, the rules for

mandatory social security and Medicare under Section 210(a)(7)(F) of the Social Security Act apply.

The election official/worker thresholds under mandatory social security for calendar years prior to 2016 are as follows:

2013-2015	$1,600
2009-2012	$1,500
2008	$1,400
2006-2007	$1,300
2002-2005	$1,200
2000-2001	$1,100
1995-1999	$1,000
1978-1994	$ 100

For calendar years 1968 through 1977, the threshold was $50 per calendar quarter.

Generally, Form W-2 is required for these workers; however, if the worker received only wages for election work and the total is less than $600 total for the year, Form W-2 is not required and no withholding of social security or Medicare tax is required. The amount paid is includible in the gross income of the worker. Revenue Ruling 2000-6 provides reporting procedures for payments to election officials and election workers in several different situations.

Contact your State Social Security Administrator concerning the status of election officials and election workers under the state's Section 218 Agreement. Additional information and threshold amounts can be found on the SSA website.

Fee-Based Public Officials

A fee-based public official receives and retains remuneration directly from the public. An individual who receives payment for services from government funds in the form of wages or salary is not a fee-based public official, even if the compensation is called a fee.

Beginning in 1968, services performed in positions compensated solely by fees are excluded from coverage under Section 218 Agreements unless the state specifically covers these services. If a state covered these positions before 1968, it may modify its Agreement to exclude these positions prospectively. The exclusion is effective the first day of the year following the year in which the modification is mailed or delivered by other means to SSA. If a state covered and later excluded these positions, the state cannot again cover these positions.

Fee-Basis Exclusion – Positions Compensated Solely by Fees

Services in positions compensated solely by fees are excluded from coverage under Section 218 Agreements (except where the state specifically included these services) and are covered as self-employment and subject to self-employment tax (SECA).

Fee-Basis Exclusion – Position Compensated by Salary and Fees

Generally, a position compensated by a salary and fees is considered a fee-basis position if the fees are the principal source of compensation, unless a state law provides that a position for which any salary is paid is not a fee-basis position.

If the state law does include this provision, none of the compensation, including the salary, is covered wages under the state's Section 218 Agreement. In this case, the salary payment, while excluded under the Agreement, is subject to mandatory social security if the official is not a qualified participant in a public retirement system.

Police Officers and Firefighters

Beginning August 16, 1994, ***all*** states were allowed to extend Section 218 social security and Medicare or Medicare-only coverage to police officer and firefighter positions covered under a retirement system through a referendum procedure conducted by the state. (Prior to August 16, 1994, only 23 states, and all interstate instrumentalities, were specifically authorized by Congress to do so.) Those states were:

Alabama	Kansas	North Carolina	Tennessee
California	Maine	North Dakota	Texas
Florida	Maryland	Oregon	Vermont
Georgia	Mississippi	Puerto Rico	Virginia
Hawaii	Montana	South Carolina	Washington
Idaho	New York	South Dakota	

As noted earlier, all states may use the majority vote referendum procedure. Some states are also authorized under the Act to use the divided retirement system referendum, discussed earlier. (Interstate instrumentalities may use the majority or divided retirement system referendum procedures.) As with other retirement system employees, before referendums can be held and coverage extended to police officer and firefighter positions already covered by a retirement system, there must first be authority to provide such coverage under state law (state statutes and/or the enabling act) and the federal-state agreement (via a modification to the state's Section 218 Agreement).

Generally, state statutes and court decisions establish the definition of police officer and firefighter positions. For social security purposes, the terms do not include services in positions that, although connected with police and firefighting functions, do not meet the definitions of police officer and firefighter positions.

Note: *Police officers and firefighters are* ***not*** *considered emergency workers for purposes of the mandatory exclusion from social security and Medicare coverage for such workers. This exclusion applies only to services of an employee who was hired because of an unforeseen emergency to do work in connection with that emergency on a temporary basis to provide emergency assistance in fires or other disasters such as severe ice storm, earthquake, volcano eruption or flood.*

Police and Firefighter Positions Not Covered Under a Retirement System

If police officer and firefighter positions are not covered under a retirement system, these positions are mandatorily covered for social security and Medicare unless the positions were already covered under a Section 218 Agreement as part of a non-retirement system coverage group.

Foreign Students, Teachers and Apprentices

Individuals admitted to the United States under an F-1, J-1, M-1 or Q-1 visa are generally exempt from both social security and Medicare taxes. Wages earned within the United States are subject to income tax, whether or not the workers are U.S. citizens. Nonresident students who are not U.S. citizens, permanent residents or resident aliens for tax purposes may be able to take advantage of treaty exemptions to exclude a portion of their U.S. source income from withholding. For more information on specific treaty provisions, contact the IRS or SSA. The following IRS publications have additional information on social security and Medicare coverage for foreign workers:

- Publication 515, *Withholding of Tax on Nonresident Aliens and Foreign Entities*
- Publication 519, *U.S. Tax Guide for Aliens*
- Publication 901, *U.S. Tax Treaties*

3) Employees With No Social Security Coverage

The final category of workers includes those who are not subject to any voluntary or mandatory social security coverage at all. This can only occur where the workers are covered by a qualifying public retirement system ("FICA replacement plan") and are not covered by a Section 218 Agreement. Employers of these workers will not withhold social security taxes or show any "social security wages" on Form W-2; they are generally covered for Medicare. Public retirement systems are the subject of Chapter 6.

Identifying Covered Employment

In addition to determining whether specific employees are members of a social security coverage group, questions may arise as to whether certain positions constitute employment. These determinations may be based on decisions regarding specific issues to which either federal or state law is applicable. It is important to know whether federal or state law is applied in making a determination on a specific issue. Generally, questions involving interpretation or application of state law are resolved by the authorized legal officers of the state in accordance with applicable state and local laws, regulations and the state court decisions. Jurisdiction for some of the major questions is indicated in the table below:

Federal Law:
Does an employer-employee relationship exist?
Who is the employer?
Are the earnings wages?
What are emergency services?
What are student services?

State Law:
Who is an officer of a state or political subdivision?
Is an entity a political subdivision?
Is a function governmental or proprietary?
Is a position under a retirement system?
Which employees are eligible for membership in a retirement system?
Who is an employee for purposes of retirement system participation?

Although federal law determines whether earnings are wages subject to social security and Medicare, state laws have a bearing on the issue of employment, such as whether a position is that of a public official of a state. Where this is the case, an opinion of the state legal officer may be requested. The state's opinion will be given weight in making the decision, but it will not be determinative of the issue. Before contacting IRS or SSA, contact the State Social Security Administrator for guidance.

The federal courts provide the ultimate determination of how social security and tax laws will apply in a given situation.

Note: *Federal Circuit Court decisions are binding only in the circuit in which they are issued. For a map of federal Circuit Court jurisdictions, see the interactive map at www.uscourts.gov/court_locator.aspx.*

Identity of the Employer for Social Security Coverage Purposes

Because entities have different social security and retirement plan situations, it is important to determine which of two or more entities, organizations, or individuals is the employer. In some cases, certain individuals, referred to as "leased workers," are supplied

or paid by one entity but work under the direction of another. Generally, if there is a provision in a statute or ordinance that creates a position and the individual is hired or elected under this authority, the individual is an employee of the state or political subdivision to which the provision applies. If there is no such authority, the employer is the entity that has the right to control the worker in the performance of the work, i.e., the common-law employer.

The employing entity is responsible for withholding and paying social security and Medicare taxes on its employees' wages, as well as reporting to SSA the amount of wages paid. These withholding, paying and reporting requirements apply to wages of individuals subject to mandatory social security and Medicare, as well as to wages of individuals covered under a Section 218 Agreement. See Publication 15.

Indian Tribal Governments and Section 218

Indian Tribal Governments, while treated as states for other purposes, are not treated as states for social security and Medicare tax purposes under Internal Revenue Code (IRC) section 7871. Thus, Indian tribal governments do not enter into Section 218 Agreements with SSA and may not participate in a public retirement system as an alternative to paying social security and Medicare tax under the provisions of IRC section 3121(b)(7)(F).

Mandatory Medicare Coverage

Prior to April 1, 1986, state and local government employees could only be covered for Medicare through a voluntary Section 218 Agreements between the state and the federal government. This changed with the enactment of the Consolidated Omnibus Budget Reconciliation Act (COBRA) of 1985, which mandated that all state and local employees hired or rehired after March 31, 1986, must be covered for Medicare, and pay Medicare taxes regardless of their membership in a retirement system. Employees covered by social security under a Section 218 Agreement are automatically covered for Medicare. Public employees already covered under a Section 218 Agreement are covered under Medicare and subject to the tax. Employees who are not covered by social security, but are subject to the Medicare-only portion of FICA, are referred to as Medicare Qualified Government Employees (MQGE). Reporting procedures for MQGE employees are covered in Chapter 3.

Employees who have been in continuous employment with the employer since March 31, 1986, who are not covered under a Section 218 Agreement nor subject to the mandatory social security and Medicare provisions, remain exempt from both social security and Medicare taxes, provided they are members of a public retirement system. (See Continuing Employment Exception, below.)

The flowchart "Social Security and Medicare Coverage for State and Local Government Employees" in Chapter 1 shows how to determine whether Medicare coverage applies.

Continuing Employment Exception

Services performed after March 31, 1986, by an employee who was hired by a state or political subdivision employer before April 1, 1986, are exempt from mandatory Medicare tax if the employee is a member of a qualifying public retirement system and ***all*** of the following requirements are met:

- The employee was performing regular and substantial services for remuneration for the state or political subdivision employer before April 1, 1986, and
- The employee was a bona fide employee of that employer on March 31, 1986, and
- The employment relationship with that employer was not entered into for purposes of avoiding the Medicare tax, and
- The employment relationship with that employer has been continuous since March 31, 1986.

In general, the following employment changes are considered continuous employment and qualify the employee for the exception:

1) From a state agency to another state agency in the same state.
2) From an employer of one political subdivision to an employer in the same political subdivision.

The following are **not** considered continuous employment for this purpose:

1) From a state agency to a political subdivision of that state.
2) From a political subdivision to a state agency.
3) From one political subdivision to another.
4) From a state agency to an agency of another state.

See Revenue Ruling 86-88, Revenue Ruling 88-36, (in the Appendix) and Revenue Ruling 2003-46 for more information about the continuing employment exception.

The Centers for Medicare & Medicaid Services (CMS) is the federal agency that administers the Medicare program. For more information, see the CMS website.

Services Not Subject to Mandatory Medicare Coverage

The following are not subject to mandatory Medicare tax even though the services are performed by an employee hired after March 31, 1986. ***(Note: These are the same services that are excluded from mandatory social security coverage, discussed earlier.)***

- Services performed by individuals hired to be relieved from unemployment. (This does not include many programs financed from federal funds where the primary purpose is to give the employee work experience or training.)
- Services performed in a hospital, home or other institution by a patient or inmate thereof as an employee of a state or local government employer.

- Services performed by an employee on a temporary basis in case of fire, storm, snow, earthquake, flood or other similar emergency.
- Services performed by non-resident aliens with F-1, J-1, M-1 and Q-1 visas.
- Services in positions compensated solely by fees that are subject to SECA, the Self-Employment Contributions Act (unless a Section 218 Agreement covers these services).
- Services performed by a student enrolled and regularly attending classes at the school, college or university where he or she is working (unless a Section 218 Agreement covers student services).
- Services performed by an election worker or official whose pay in a calendar year is less than the amount mandated by law (unless a Section 218 Agreement covers election workers).
- Services that would be excluded if performed for a private employer because it is not work defined as employment under Section 210(a) of the Social Security Act (unless a Section 218 Agreement covers certain agricultural services).

See the sections on **Mandatory Exclusions** and **Optional Exclusions** in this chapter for more details on these exclusions.

Voluntary Medicare Coverage

A Section 218 Agreement can be executed to provide Medicare-only coverage for employees who are qualified participants in a public retirement system and not covered under a Section 218 Agreement and not subject to the mandatory Medicare provisions. Contact your State Social Security Administrator for further information. (A list of State Administrators is available at www.ncsssa.org.)

Frequently Asked Questions

1) **Are any services excluded from mandatory social security and Medicare coverage?** Yes. The same exclusions apply to mandatory social security and mandatory Medicare; this list appears in this chapter under the discussion of mandatory social security and again under the discussion of mandatory Medicare. see the lists in this chapter. However, some services excluded from mandatory coverage under provisions of the Internal Revenue Code may be covered by a Section 218 Agreement. [IRS, SSA]

2) **If a local government has a public retirement system that qualifies as a FICA replacement plan and does not have a Section 218 Agreement, can employees elect to participate in social security on a voluntary basis?** No. An employee can only participate in social security if the position is covered either by the mandatory provisions or by a Section 218 Agreement. Only the State Social Security Administrator can initiate a request for Section 218 coverage. [SSA]

3) **Does a college student employed by a university during the summer months qualify for the student social security and Medicare exception from**

mandatory social security if he/she is not regularly enrolled and attending classes at the university during that time? If an individual is not enrolled in classes during school breaks of more than five weeks, including summer breaks, the student social security and Medicare exception does not apply (other than during payroll periods of a month or less that fall wholly or partially within the academic term). See Revenue Procedure 2005-11, sections 7.04 and 7.05. [IRS]

4) **Are elected and appointed officials considered employees?** For income tax purposes, elected (or elective) and most appointed officials are defined by section 3401(c) of the Internal Revenue Code as employees of the public entity they serve (e.g., mayors, members of the legislature, county commissioners, city council members and board or commission members). In general, elected as well as appointed officials will meet the common-law tests to be considered employees. Regardless of the common-law tests, some positions may be defined as employment by state statute. Some fee-basis officials are by law treated as self-employed. An elected or appointed official who is an employee is subject to rules for mandatory social security and Medicare unless covered under a Section 218 Agreement or a qualified participant in a retirement system. All officials elected or appointed to their positions after March 31, 1986, are subject to Medicare withholding. See Chapter 4. [IRS]

5) **How is "termination of employment" defined for purposes of determining whether the continuing employment exception for Medicare tax is applicable?** Whether an employment relationship has terminated is a question of fact that must be determined on the basis of all the relevant facts and circumstances. Great weight, however, will be given to the personnel rules of the state employer or political subdivision employer to determine whether an employment relationship has been terminated. (Revenue Ruling 86-88.) [IRS]

6) **An employee who was hired before April 1, 1986, by the state transferred after March 31, 1986, to another state agency. The transfer was made without terminating the employee's employment with the state. Does the employee qualify for the continuing employment exception?** Yes. An employee hired before April 1, 1986, by a state employer who transfers after March 31, 1986, to another state employer of the same state may qualify for the continuing employment exception, provided the transfer was made without a termination of the employee's overall employment relationship with that state. The same rule applies to an employee hired before April 1, 1986, by a political subdivision employer, who transfers after March 31, 1986, to another employer of that same political subdivision. However, an employee hired before April 1, 1986, does not qualify for the continuing employment exception if after March 31, 1986, the employee transfers from a state employer to a political subdivision employer or from a political subdivision employer to a state employer. Likewise, an employee does not qualify for the exception if the employee transfers from a political subdivision employer in one political subdivision to a political

subdivision employer in a different political subdivision, or from a state employer in one state to a state employer in a different state. [IRS]

7) **Can employees who were hired prior to April 1, 1986, and who are not currently paying into Medicare, enroll in Medicare in the future?** Individual employees can never elect voluntarily to participate in social security or Medicare. State or local public employers can voluntarily choose to cover one or more groups of employees under Medicare-only, even if they are otherwise exempt because of the continuing employment exception. To elect such coverage, the state or local government (through the state) must enter into a modification of the state's Section 218 Agreement. Contact your State Social Security Administrator for further information about a Medicare-only modification. If an individual's state or local government employment is not covered under social security or Medicare, the individual may not be insured (i.e., have enough work credits) for Medicare based on his/her own wages. That individual may be entitled to coverage based on sufficient other work that is covered for social security, or Medicare on his/her own earnings record or that of an insured spouse. [SSA]

Chapter 6

Social Security and Public Retirement Systems

Effective July 2, 1991, Congress made social security coverage mandatory for state and local government employees who are neither covered by a Section 218 Agreement nor qualified participants in a public retirement system (also referred to as a "FICA replacement plan"). States can provide employees with membership in a public retirement system as an alternative to mandatory social security coverage.

As a supplement to the social security and public retirement systems information provided in this publication, refer to the FSLG web site.

This chapter provides information about the requirements a retirement system must meet to qualify as an alternative to social security coverage.

Public Retirement Systems (FICA Replacement Plans)

A public retirement system, as defined in Internal Revenue Code (IRC) section 3121(b)(7)(F) and Regulation 31.3121(b)(7)-2, is a pension, annuity, retirement or similar fund or system maintained by a state or local government that provides a retirement benefit to the employee that is comparable to the benefit provided under the Old-Age portion of the Old-Age, Survivors and Disability Insurance (social security) part of FICA. To be a retirement system for this purpose, the plan must provide a minimum retirement benefit. In this context, the term "employer" is used to refer to a state, political subdivision, or instrumentality. The term "employee" is used here only to refer to an employee of a state, political subdivision, or instrumentality.

Note: *A "public retirement system" for this purpose is not required to be a qualified plan within the meaning of the Employee Retirement Income Security Act of 1974 (ERISA). The ERISA provisions relate to the tax treatment of contributions and benefits of employee plans, and are irrelevant to the coverage issues addressed here. To avoid confusion, this publication does not use the term "qualified" to refer to public retirement systems. For mandatory coverage purposes, the employee may be a member of any type of retirement system, including a system that is nonqualified under ERISA (for example, a section 457 plan), as long as the plan provides the minimum level of benefits required for a public retirement system. These requirements are discussed below and in Regulation 31.3121(b)(7)-2(e) and in Revenue Procedure 91-40.*

For purposes of determining whether mandatory coverage applies for an employee holding more than one position, social security is NOT a public retirement system.

> **Example:** An individual holds two positions with the same political subdivision. The wages earned in one position are subject to social

security and Medicare tax pursuant to a Section 218 Agreement; the other position is not covered. The social security system is not a retirement system for this purpose. Thus, mandatory social security coverage applies to service in the other (non-218) position unless the employee is a member of a public retirement system with respect to that position. See Regulation 31.3121(b)(7)-2(e)(1).

In general, there are two types of public retirement systems that may meet the minimum benefit requirement — the **defined contribution** plan and the **defined benefit** plan.

Defined Contribution Plan

A defined contribution plan provides an individual account for each participant and provides benefits based solely on the amount contributed to the participant's account, and any income, expenses, gains or losses that may be allocated to that participant's account. See IRC section 414(i).

A defined contribution plan that satisfies the definition of a retirement system under Regulation 31.3121(b)(7)-2(e)(2)(iii) must provide for an allocation to the employee's account of ***at least 7.5 percent of the employee's compensation during any period under consideration***. A variety of plan types could meet the requirement; for example, plans established under IRC sections 401(a), 403(b), or 457. Contributions from both the employer and the employee may be used to make up the 7.5 percent. Matching contributions by the employer may be taken into account for this purpose. A plan with only employee contributions would also satisfy the minimum benefit requirement, provided the contributions constitute at least 7.5 percent of compensation. However, the 7.5 percent cannot include any earnings on the account.

Definition of Compensation

For a defined contribution plan, the definition of "compensation" used to determine whether the benefit is sufficient must include at least the employee's base pay, provided that the definition of "base pay" is reasonable. Thus, for example, a defined contribution retirement system may disregard any of the following: overtime pay, bonuses, or single-sum amounts received on account of death or separation from service, amounts received under a bona fide vacation, compensatory time or sick pay plan, or amounts received under severance pay plans. Any compensation in excess of the social security contribution wage base for that year ($118,500 in 2015) may also be disregarded for this purpose.

> **Example:** A political subdivision maintains an elective defined contribution plan that is a retirement system within the meaning of IRS regulations. The plan is on a calendar year. In 2014, an employee contributes to the plan at a rate of 7.5 percent of base pay. Assume that the employee compensation will reach the social security maximum contribution base in October. The employee is a qualified participant in the

plan for the entire plan year, even if the employee ceases to contribute to the plan after reaching the maximum contribution base. See Regulation 31.3121(b)(7)-2(e)(2)(iii)(B).

Generally, for an employee who holds more than one position with the same employer, all compensation with that employer is considered in applying the 7.5 percent test. However, at the employer's option, compensation from only one position may be considered, if that position is not part-time, temporary, or seasonal. See Regulation 31.3121(b)(7)-2(c)(2)(iv).

Reasonable Interest Rate Requirement

Generally, a defined contribution retirement system must credit the employee's account with earnings at a reasonable rate, under all the facts and circumstances. Alternatively, employees' accounts may be held in a separate trust subject to general fiduciary standards and credited with actual earnings of the trust fund. Whether the interest rate is reasonable is determined after reducing the rate to adjust for the payment of any administrative expenses. See Regulation 31.3121(b)(7)-2(e)(2)(iii)(C).

Defined Benefit Plan

For purposes of determining whether it qualifies as a public retirement system, a defined benefit plan is any plan other than a defined contribution plan. A defined benefit plan determines benefits on the basis of a formula, generally based on age, years of service and salary level.

A defined benefit retirement system that qualifies as an alternative to social security provides for a retirement benefit to the employee that is comparable to the benefit provided by the social security part of FICA. Generally, a plan meets the requirement if the benefit under the system is ***at least 1.5 percent of average compensation during an employee's last three years of employment, multiplied by the employee's number of years of service.*** Apply the formulas in Revenue Procedure 91-40 and the IRS regulations to determine whether a defined benefit retirement system meets this requirement.

Who Is a Qualified Participant?

For an employee to be excluded from mandatory social security coverage, the employing entity must maintain a retirement system within the meaning of IRC section 3121(b)(7)(F), and the employee must also be a qualified participant in that system, as defined in IRC section 3121(b)(7)(F) and Regulation 31.3121(b)(7)-2(d). This test must be applied to each employee separately. An entity may maintain a retirement system in which not every employee is a qualified participant. For both a defined contribution plan and for a defined benefit plan, the determination of whether an individual is a qualified participant is made as services are performed; however, there are different tests to determine participation, as discussed below.

Qualified Participant in a Defined Contribution Retirement System

An employee is a qualified participant in a defined contribution retirement system with respect to services performed on a given day if, ***on that day,*** the employee has satisfied all conditions (other than vesting) for receiving an allocation to his or her account (exclusive of earnings) that meets the minimum retirement benefit requirement. The benefit must be calculated with respect to compensation during a period ending on that day and beginning on or after the beginning of the plan year of the retirement system. This is the case regardless of whether the allocations were made or accrued before the effective date of IRC section 3121(b)(7)(F).

> **Example 1:** A state-owned hospital maintains a non-elective defined contribution plan that is a retirement system within the meaning of IRS regulations. Under the terms of the plan, employees must be employed on the last day of a plan year in order to receive any allocation for the year. Employees may not be treated as qualified participants in the plan before the last day of the year.
>
> **Example 2:** The situation is the same as in Example 1, except that under the terms of the plan, an employee who terminates service before the end of a plan year receives a pro rata portion of the allocation he or she would have received at the end of the year, e.g., based on compensation earned since the beginning of the year. If the pro rata allocation available on a given day would meet the minimum retirement benefit requirement with respect to compensation from the beginning of the plan year through that day (or some later day), the employee is treated as a qualified participant in the plan on that day.
>
> **Example 3:** A political subdivision maintains an elective defined contribution plan that is a retirement system within the meaning of IRS regulations. The plan operates on a calendar year. It has two open seasons—in December and June—when employees can change their contribution elections. In December, an employee elects not to contribute to the plan. In June, the employee elects (beginning July 1) to contribute a uniform percentage of compensation for each pay period to the plan for the remainder of the plan year. The employee is not a qualified participant in the plan during the period January-June, because no allocations are made to the employee's account during that time. If the level of contributions during the period of July-December meets the minimum retirement benefit requirement with respect to compensation during that period, however, the employee is treated as a qualified participant during that period.
>
> **Example 4:** Assume the same facts as in Example 3, except that the plan allows participants to cancel their elections in cases of economic hardship. In October, the employee suffers an economic hardship and cancels the

election, effective November 1. If the contributions during the period July-October are high enough to meet the minimum retirement benefit requirement with respect to compensation during that period, the employee is treated as a qualified participant during that period. In addition, if the contributions during the period July-October are high enough to meet the requirements for the entire period July-December, the employee is treated as a qualified participant in the plan throughout the period July-December, even though no allocations are made to the employee's account in the last two months of the year. There is no requirement that the period used to determine whether an employee is a qualified participant on a given day remain the same from day to day, as long as the period begins on or after the beginning of the plan year and ends on the date the determination is being made. See Regulation 31.3121(b)(7)-2(d)(1)(ii).

Qualified Participant in a Defined Benefit Retirement System

An employee is a qualified participant in a ***defined benefit retirement system*** with respect to services performed on a given day if (1) on that day, the employee is (or ever has been) an actual participant in the retirement system and (2) on that day, the employee actually has a total accrued benefit that meets the minimum retirement benefit requirement. An employee may not be treated as an actual participant or as actually having an accrued benefit for this purpose to the extent that such participation or benefit is subject to any conditions (other than vesting) that have not been satisfied. The disqualifying conditions might include a requirement that the employee attain a minimum age, perform a minimum period of service, make an election in order to participate, or be present at the end of the plan year in order to be credited with an accrual.

> **Example**: A political subdivision maintains a defined benefit plan that is a retirement system within the meaning of IRS regulations. Under the terms of the plan, service during a plan year is not credited for accrual purposes unless a participant has at least 1,000 hours of service during the year. For purposes of determining whether mandatory social security coverage applies, benefits that accrue only upon satisfaction of this 1,000-hour requirement may not be taken into account in determining whether an employee is a qualified participant in the plan before the 1,000-hour requirement is satisfied. See Regulation 31.3121(b)(7)-2(d)(1)(i).

Part-Time, Seasonal, Temporary Employees

Special rules apply to part-time, seasonal and temporary employees for purposes of determining whether they are qualified participants in a public retirement system. To be exempt from mandatory social security coverage, these employees must not only be qualified participants; ***they must be fully vested in their benefits.*** This means the benefits cannot be forfeited. If a part-time, seasonal or temporary employee (as defined below) is not a qualified participant in a public retirement system with benefits fully

vested from the first day of employment, that employee is subject to mandatory social security and Medicare tax until the employee becomes fully vested.

The special vesting requirement is considered to be met if a part-time, seasonal or temporary employee in a defined contribution plan has the right to receive a single sum payment of at least 7.5 percent of the compensation the employee earned while covered under the retirement system (plus interest) when the employee separates from employment.

Part-Time Employees

For purposes of applying the qualified participant test, part-time employees are those who normally work 20 hours or less per week. (This definition of "part-time" should not be confused with a definition of "part-time" that may be used for a Section 218 Agreement.) If mandatory coverage applies, part-time positions cannot be excluded; but part-time positions may be excluded from coverage under a Section 218 Agreement, at the option of the state. Contact the State Social Security Administrator to determine the definition of part-time positions under the state's Section 218 Agreement.

A special rule provides that a teacher employed by a post-secondary educational institution (e.g., a community or junior college, post-secondary vocational school, college, university or graduate school) is not considered part-time if the teacher normally teaches classroom hours of one-half or more of the number of classroom hours normally considered to be full-time employment.

> **Example:** A community college treats a teacher as a full-time employee if the teacher is assigned to work 15 classroom hours per week. A new teacher is assigned to work eight classroom hours per week. Because the assigned classroom hours of the teacher are at least one-half of the hours designated by the school as constituting full-time employment, the teacher is not a part-time employee. See Regulation 1.3121(b)(7)-2(d)(2)(iii)(A).

Seasonal Employees

For purposes of applying the qualified participant test, a seasonal employee is any employee who normally works on a full-time basis less than five months in a year. Thus, for example, individuals who are hired by a political subdivision during the tax return season in order to process incoming returns and work full-time over a three-month period are seasonal employees. See Regulation 31.3121(b)(7)-2(d)(2)(iii)(B).

Temporary Employees

For purposes of applying the qualified participant test, a temporary employee is one who performs services under a contractual arrangement that is expected to last two years or less. Under this rule, a teacher under an annual contract may or may not be a temporary

employee. Possible contract extensions must be considered in determining the duration of a contractual arrangement if there is a significant likelihood that the employee's contract will be extended. Contract extensions are considered likely to occur if, on average, 80 percent of similarly situated employees have had bona fide offers to renew their contracts in the immediately preceding two academic or calendar years. Contract extensions are also considered significantly likely to occur if the employee has a history of contract extensions in the current position. See Regulation 31.3121(b)(7)-2(d)(2)(iii)(C).

Individuals Employed in More Than One Position

If an employee is not covered by a Section 218 Agreement, but is a member of a retirement system with respect to one full-time position, the employee is generally treated as a member of a retirement system with respect to any other position with the same employer.

> **Example:** An individual is employed full-time by a county and is a qualified participant in its retirement plan with regard to that employment. In addition to this full-time employment, the individual is employed part-time in another position with the same county. The part-time position is not covered by the county retirement plan. Nevertheless, if the individual is a qualified participant in the retirement plan with respect to the full-time position, the part-time position is excluded from mandatory social security coverage. See Regulation 31.3121(b)(7)-2(c)(2).

This rule does not apply to employment by two different employers.

> **Example.** An individual is employed full-time by a state and is a member of its retirement plan, and is also employed part-time by a city located in the state, but does not participate in the city's retirement plan. The services of the individual for the city are not excluded from mandatory social security coverage, because the determination of whether services constitute employment for such purposes is made separately with respect to each political subdivision for which services are performed. See Reg. 31.3121(b)(7)-2(c)(2).

Whether an employee is a part-time, seasonal or temporary employee is generally determined on the basis of service in each position in which allocations or benefits were earned. This determination generally does not take into account service in other positions with the same or different public employers. However, all of an employee's service in other positions with the same or different employers may be taken into account for purposes of determining whether an employee is a part-time, seasonal or temporary employee with respect to benefits under the retirement system provided that:

- The employee's service in the other positions is or was covered by the same retirement system;

- All service aggregated for purposes of determining whether an employee is a part-time, seasonal or temporary employee (and related compensation) is aggregated under the system for all purposes in determining benefits (including vesting); and
- The employee is treated at least as favorably as a full-time employee under the retirement system for benefit accrual purposes.

> **Example:** Assume that an employee works 15 hours per week for a county and 10 hours per week for a municipality, and that both of these employers contribute to the same statewide public employee retirement system. Assume further that the employee's service in both positions is aggregated under the system for all purposes in determining benefits (including vesting). If the employee is covered under the retirement system with respect to both positions and is treated for benefit accrual purposes at least as favorably as full-time employees, then the employee is not considered a part-time employee of either employer. The requirement of being fully vested for determining the applicability of mandatory social security coverage does not apply. See Regulation 31.3121(b)(7)-2(d)(2)(iii)(D).

Alternative Lookback Rule

Under an alternative lookback rule, an employee may be treated as a qualified participant in a retirement system throughout a calendar year if he or she was a qualified participant in the system at the end of the plan year of the system ending in the preceding calendar year.

> **Example.** An employee is a qualified participant in a retirement plan of a city on the last day of the plan year, May 31, 2014. If the alternative lookback rule is used, no liability for social security tax exists for the employee for calendar year 2015. See Regulation 31.3121(b)(7)-2(d)(3)

For the first year of participation, an employee who participates in the retirement system may be treated as a qualified participant during the year only if it is reasonable to believe that the employee will be a qualified participant on the last day of the plan year.

Former Participants

In general, the rules regarding qualified participants apply to **former participants** who continue to perform services for the employer or who return after a break in service. Thus, for example, a former employee, with a deferred benefit under a defined benefit retirement system, who is reemployed by the same employer but does not resume participation in the retirement system, may continue to be a qualified participant in the system after becoming reemployed if the individual's total accrued benefit under the system meets the minimum retirement benefit requirement (taking into account all periods of service, including current service). If this is so, the employer is not required to withhold and pay social security tax, or make additional payments to the retirement

system on his behalf. The individual's status as a qualified participant must be continually reevaluated, however, for employment of more than a short period. See Regulation 31.3121(b)(7)-2(d)(4)(i).

Rehired Annuitants

A rehired annuitant is a retiree who is rehired by his or her employer or another employer that participates in the same retirement system as the former employer. A rehired annuitant is either receiving a retirement benefit from that retirement system, or has reached retirement age under the retirement system.

Rehired annuitants are excluded from mandatory social security coverage.

> **Example.** A teacher retires from service with a school district that participated in a statewide teachers' retirement system and did not have a Section 218 Agreement. She begins to receive benefits from the system, and later becomes a substitute teacher in another school district that participates in the same statewide system. The employee is treated as a rehired annuitant and is not subject to mandatory social security tax. The teacher is subject to Medicare tax. See Regulation 31.3121(b)(7)-2(d)(4)(ii).

However, if an employee is rehired to perform services in a state or local government position that is covered for social security under a Section 218 Agreement, services in that position are covered for social security. If an individual returns to work for an employer under mandatory coverage, the employment is subject to the mandatory coverage.

Note: *Retirees rehired after March 31, 1986, are subject to the Medicare tax regardless of whether they qualify as rehired annuitants for social security purposes.*

Frequently Asked Questions

1) **What is a "public retirement system" for purposes of of the mandatory coverage rules?** A "public retirement system" (sometimes referred to as a "FICA replacement plan or simply as a "retirement system") is a pension or other retirement plan maintained by a public employer that meets the requirements of IRC Section 3121(b)(7)(F). See Revenue Procedure 91-40 in the Appendix, and Section 31.3121(b)(7)-2 of the Employment Tax Regulations. These requirements must be met for a retirement system to be used as an alternative to mandatory social security coverage. A retirement system may be a pension, annuity, retirement or similar fund or system established by a state or political subdivision. The system need not be created by the legislature of the state, nor does it have to be a plan under which the benefits are guaranteed by the state constitution. A retirement system can include a group annuity policy purchased by the state or political subdivision from a private insurance company. Whether a

system qualifies as a "public retirement system" does not depend on whether it meets the requirements be a qualified plan under the Employees' Retirement Income Security Act of 1974 (ERISA). [IRS]

2) **What does it mean to be a qualified participant in a retirement system**? To be a qualified participant, a member must actually participate in the system. An employee who is eligible for an optional system, but decides not to participate, will be subject to mandatory social security tax. Under an alternate rule, an employer is entitled to treat an employee as a qualified participant for the entire year if he or she was a qualified participant in the retirement system on the last day of the plan year ending in the previous calendar year. [IRS]

3) **How are part-time, seasonal and temporary workers defined for purposes of determining whether they are qualified participants in a public retirement system under IRC section 3121(b)(7)(F)?** A part-time employee normally works 20 hours or less per week. A seasonal employee may work full-time, but for less than five months a year. In the case of teachers above the high-school level, part-time is defined as less than one-half the classroom hours designated as full-time by the school. A temporary employee performs services under a contractual arrangement of two years or less. Possible contract extensions must be considered in determining the duration of a contractual arrangement if there is a significant likelihood that the employee's contract will be extended. Future contract extensions are considered likely if (1) on average 80 percent of similarly situated employees have had bona fide offers to renew their contracts in the immediately preceding two academic or calendar years, or (2) the contract history of an employee indicates that the employee is not a temporary employee. [IRS]

4) **Are there special vesting rules for part-time, seasonal and temporary workers?** For part-time, seasonal and temporary employees to be qualified participants in an employer-sponsored retirement plan, they must be immediately and fully (100 percent) vested in the plan. The vesting requirement for a defined contribution plan is met if an employee has a nonforfeitable right to receive a payment equal to 7.5 percent of the compensation the employee earned while participating in the system plus a reasonable rate of interest. [IRS]

5) **If a local government participates in a statewide retirement system, is the plan considered "established" by the employer?** Yes. The fact that each local government is a separate employer for tax purposes is irrelevant. Even though the plan is not maintained by the local government, it is offered through that entity as an employer and is considered established by the employer. [IRS]

6) **For new employees, entering a retirement system**, i**s there any waiting period for coverage during which mandatory social security and Medicare taxes do not have to be paid?** If a full-time employee can be enrolled in the plan by the first day of the first full calendar month of service, social security and Medicare taxes do not have to be paid during the partial month in which he or she begins

work. This rule does not apply to part-time, seasonal and temporary employees. [IRS]

7) **Is a retirement system that does not cover all employees a "retirement system" within the meaning of Regulations section 31.3121(b)7-2?** A retirement system is not required to cover all employees; it may be a retirement system for some employees and not for others. The coverage determination is made separately for each individual. [IRS]

8) **A teacher who is a participant in a retirement system during the academic year also works a few hours per week in the summer in the school library. The library job is not covered by a Section 218 Agreement or by the public retirement system because it does not fall during the normal 10-month school year. Are the wages for the summer job subject to social security and Medicare taxes?** The wages are not subject to social security taxes because the teacher is a qualified participant in the public retirement system with respect to her full-time job. A teacher who is expected to be employed on a continuing basis qualifies for treatment as employed simultaneously in multiple positions with the same entity. Consequently, the determination may be made solely by reference to service in the teacher's full-time position. The Medicare tax applies, unless the employee is was hired prior to April 1, 1986, and qualifies for the continuing employment exception. [IRS]

9) **A teacher retires from a school district, starts collecting a pension under the state retirement system, and returns to work for the same school district as a bus driver. The bus driving position is not covered by a Section 218 Agreement and is not covered by the state retirement system. Is the employee subject to mandatory social security tax on the wages as a bus driver?** No. The employee is a rehired annuitant. He is deemed to be a qualified participant in the retirement system without regard to whether he continues to accrue a benefit. He is subject to Medicare tax because the continuing employment exception cannot apply because the original employment relationship terminated at retirement. [IRS]

Chapter 7

Social Security Administration

This chapter discusses the functions of the Social Security Administration (SSA) that relate to employer tax and information reporting responsibilities.

SSA is the primary income security agency for Americans. It administers the federal Old-Age, Survivors and Disability Insurance (OASDI) program, the largest income-maintenance program in the United States. The Supplemental Security Income (SSI) program provides monthly benefits designed to replace, in part, the loss of income due to retirement, disability or death. The SSI program provides or supplements the income of aged, blind or disabled individuals with limited income and resources. Children, as well as adults, can receive payments because of disability or blindness.

Organization

SSA's organization features centralized management in Baltimore, Maryland, and a nationwide network of 10 regional offices overseeing approximately 1,230 field offices (FOs), 162 hearing offices, 35 teleservice centers, 6 processing centers and a national data operations center in Wilkes-Barre, Pennsylvania.

All components within SSA's central office perform a supporting role to SSA FOs by providing direction, guidance and material resources. FOs are located in cities and rural communities across the nation and are the agency's main personal point of contact with beneficiaries and the public. Additionally, the Social Security Disability Insurance (SSDI) program depends on the work of 54 offices of Disability Determination Services in all 50 states, the District of Columbia, Guam and Puerto Rico.

For questions about social security coverage for specific workers or groups of workers, public employers should first consult the State Social Security Administrator for the state. Public employers who have questions regarding electronic filing or other SSA reporting processes or reporting applications, should contact the appropriate Employer Services Liaison Officer (ESLO) listed at the SSA ESLO page on the SSA website. Questions related to employer or employee tax liability should be directed to the IRS.

Inquiries regarding state and local coverage issues should be directed to the State and Local Coverage Specialist for your state or territory. A list is provided on the SSA state and local government employer's page. For other inquiries, see the SSA home page.

Parallel Social Security Office (PSSO)

The PSSO, in most cases located in the state capital, is the on-site representative of the SSA to the state under the leadership of the Regional Commissioner. The PSSO:

- Conducts day-to-day negotiations with the state;
- Assists the state in drafting Section 218 Agreements and modifications;
- Reviews agreements and modifications from the state for technical accuracy and appropriate documentation before forwarding to the Regional Office; and
- Makes coverage and wage determinations, as appropriate.

To locate a PSSO, use the SSA local office search.

Regional Office (RO)

RO staff works under the direction of the Regional Commissioner (RC). The RO provides leadership and technical direction in the coverage area for the state and local program within the region, consistent with established policy. Within the RO structure is the Assistant Regional Commissioner (ARC), who has ongoing responsibility for state and local coverage activities within the region. The Regional Office:

- Interprets, reviews, processes and executes Section 218 Agreements and modifications;
- Reviews supporting documentation to state notices to remove legally dissolved entities from coverage under Section 218 Agreements;
- Makes and reviews coverage and wage determinations consistent with established policy;
- Provides guidance and advice to states on proposed legislation and regulations that may have impact on the state's Section 218 Agreement;
- Interprets and advises states on established policies and procedures;
- Refers to Central Office questions for which no policy has been established, or for which present policy may require a change that may have national impact;
- Maintains file of original agreements and modifications;
- Maintains the summaries of state agreements; and
- Handles inquiries and answers questions about electronic filing and paper reporting of wages.

Office of Income Security Programs (OISP)

OISP is primarily responsible for administering the state and local coverage program. Organizationally, OISP is located under the Deputy Commissioner, Retirement and Disability Policy.

Social Security Earnings Records

The social security number (SSN) is used for posting and maintaining the earnings and employment records of persons covered under the social security program. Employers withhold social security and Medicare taxes from employee paychecks and, with the employer tax, deposit these amounts or pay them with the tax return. (See Chapter 3 for information on reporting and deposit rules.) By the end of February (the end of March if

Form W-2 data is submitted electronically), employers file wage reports with the SSA showing the wages paid to each employee during the preceding year. SSA shares this information with the IRS. SSA also sends weekly updates to IRS with information on newly established SSN records and corrected information for previously established SSN records. Reported earnings are posted to the worker's earnings record.

When a worker or a worker's family member applies for social security benefits, the worker's earnings record is used to determine the eligibility for benefits and the amount of any cash benefits payable. It is thus critical that employers maintain accurate, up-to-date SSN information on their employees to make sure each employee's earnings are correctly posted to that employee's earnings record.

Under the Federal Insurance Contributions Act (FICA), social security and Medicare benefits are financed through taxes paid by employees and their employers. The social security and Medicare tax rates are set by law. The tax rate on wages for the Old-Age, Survivors and Disability Insurance (OASDI) program applies to earnings up to an annual maximum amount. This amount, called the earnings base, is adjusted annually based on changes in average wages. Medicare Hospital Insurance (HI) taxes are paid on total earnings; there is no wage base limit for Medicare tax. The Supplementary Medical Insurance (SMI) part of Medicare is financed by monthly premiums charged to beneficiaries and by payments from general federal revenues.

Earning Credits

Individuals become eligible for social security benefits and Medicare hospital insurance based on credits for work covered by social security and/or Medicare. (In 2015, one credit is earned for each quarter with $1,220 in earnings, for up to four quarters per year.) The amount of earnings required for each credit increases each year to reflect average wage increases. The table below shows the required amounts for recent years.

Credits earned remain on the worker's social security earnings record, regardless of periods of no earnings. The number of credits an individual needs to be eligible for social security and Medicare benefits depends on age and the type of benefit. Most people need 40 credits (10 years of work) to qualify for benefits. Younger people need fewer credits to be eligible for disability benefits, or for their family members to be eligible for survivors' benefits in case of death.

Beginning in 1957, basic pay earned from active military duty or training in military service may earn social security credits. In addition, military service before 1957 may qualify a person for additional earnings credits. A determination of these additional credits is made at the time a person applies for benefits.

State and local government employees covered for Medicare-only must earn the same number of credits to qualify for Medicare as required for social security benefits.

If a question arises concerning the employment relationship of a worker for claims purposes, SSA determines whether there was a common-law employer-employee relationship for the purpose of determining the benefits of the claimant.

Retirement Income

Full social security retirement benefits are payable to individuals with 40 credits (10 years of work) at full retirement age (FRA). An individual can elect social security retirement benefits as early as age 62, but in that case, the individual's monthly benefit is reduced by an established percentage. In 2003, FRA began to increase in gradual steps from age 65 to 67. This provision affects people born in 1938 and later.

If an individual receives social security benefits before reaching FRA, benefits are further reduced if the individual continues to work and earn more than an annual exempt amount. The annual exempt amount changes each year. A worker can earn up to that amount and not experience any additional reduction of social security benefits. If the worker is under FRA and earns over the exempt amount, the benefits will be reduced $1 for every $2 in earnings above the exempt amount. In the year the individual reaches FRA, benefits will be reduced $1 for every $3 in earnings above the exempt amount.

A spouse or former spouse may qualify for benefits upon a worker's retirement or disability. Benefits are paid as early as age 62, or at any age if the spouse is caring for the worker's child. In this case the child must be under 16 or disabled and receive benefits on the worker's record. A spouse's benefits will be one-half or less of FRA monthly benefit.

The table below indicates earnings requirements and exempt amounts for recent years.

	2011	**2012**	**2013**	**2014**	**2015**
Earnings required for one credit	$1,120	$1,130	$1,160	$1,200	$1,220
Exempt annual amount - under full retirement age	$14,160	$14,640	$15,120	$15,480	$15,720
Exempt amount - year attaining normal/full retirement age	$37,680	$38,880	$40,080	$41,400	$41,880
Full retirement age or older	No limits effective January 2000.				

Benefits for divorced spouses age 62 or older may be payable if the insured former spouse is eligible for retirement benefits, even though not yet retired. Unmarried children under the age of 18 (under 19 if in high school) or any age if disabled before age 22 may qualify for social security benefits on a retired or disabled parent's social security record.

Note: *Although the full retirement age for social security may vary, Medicare (HI) eligibility is age 65 for everyone. Eligibility for HI is based on benefits as a retired worker, as a spouse of a retired or disabled worker, or as a spouse of a deceased worker. The individual qualifies even if the individual is not receiving monthly social security retirement benefits because the individual or the individual's spouse continues to work.*

Special rules apply to uninsured persons who are at least 65 but who are not eligible for HI under the regular rules. See Chapter 5.

Effect on Benefits from Work not Covered by Social Security

There are two situations in which receipt of a pension based on employment not covered by social security will affect the amount of a social security benefit. Employees who participated in a public retirement system and also have a social security benefit based on another retirement system should be aware of these provisions.

The ***Windfall Elimination Provision (WEP)*** affects the way the social security retirement or disability benefit is computed for some individuals with non-covered employment.

The ***Government Pension Offset (GPO)*** affects the amount of the social security benefit received by a spouse or widow(er).

Windfall Elimination Provision (WEP)

The WEP affects some individuals who receive a monthly pension based in whole or in part on work not covered by social security. The weighting in the social security benefit formula is intended to help people who spend most of their working lives in low-paying jobs by providing them with a benefit that is higher in relation to their prior earnings than the benefit provided for workers with high career earnings. Before 1983, people who worked mainly in jobs not covered by social security had their benefits calculated as if they were long-term, low-wage workers.

Therefore, prior to the WEP, the benefit formula created an unintended advantage for workers who had pensions from non-covered employment in addition to social security coverage. It benefited people who worked for only a portion of their careers in jobs covered by social security but had their benefits computed as if they were long-term, low-wage workers. WEP was enacted to eliminate this unintended advantage by providing for a different, less heavily weighted benefit formula for persons who receive a pension based on non-covered employment.

If you receive a pension based on work not covered by social security, your social security retirement or disability benefit is computed using a modified benefit formula. The resulting benefit amount is lower than you would receive if you did not also receive a pension based on non-covered employment.

The modified formula applies to those who reach age 62 or become disabled after 1985 and first become eligible after 1985 for a monthly pension based in whole or in part on work not covered by social security. You are considered eligible to receive a pension if you meet the requirements of the pension, even if you continue to work.

Workers with relatively low pensions are less affected by the law because the reduction in the social security benefit cannot be more than one-half of that part of the pension attributable to earnings not covered by social security.

The Windfall Elimination Provision does not apply to:

- A federal worker performing service on January 1, 1984, who becomes newly covered under social security on January 1, 1984, under the mandatory coverage provision in PL 98-21;
- An employee of a non-profit organization who is exempt from social security coverage on December 31, 1983, and who becomes covered for the first time as an employee of that organization on January 1, 1984, under the mandatory coverage provision of PL 98-21;
- Pensions based on earnings under the Railroad Retirement Act;
- Pensions based entirely on non-covered employment before 1957;
- Persons who have 30 or more years of substantial earnings under social security; or
- Survivor benefits.

For more information about the WEP, see the SSA Windfall Elimination Provision page.

Government Pension Offset (GPO)

The Government Pension Offset (GPO) applies to a worker who gets a government pension that is based on employment not covered by social security and is also eligible for social security as a spouse or widow(er). Two-thirds of the government pension is used to offset any spouse's or widow(er)'s social security benefit.

Before the GPO provisions were enacted in December 1977, many government employees qualified for a pension from their government agencies and for a spouse's benefit from social security, even though they were not dependent on that spouse.

This situation was considered unfair to employees in social security covered positions because social security rules require that an individual's benefit as a spouse or widow(er) be offset dollar for dollar by the amount of his/her own social security retirement benefit.

> **Example.** Under GPO rules, a woman eligible for $1,200 in social security retirement benefits on her own work record and also eligible for a spousal benefit of $900 receives only the higher of the two benefits - $1,200 in this case. But before enactment of the GPO provision, if that woman was a government employee who did not pay into social security and who earned a $1,200 government pension, there was no offset; and she would receive the $900 social security wife's benefit as well as her $1,200 government pension. The GPO provision was enacted to prevent such inequities.

For applications filed before April 1, 2004, state and local government workers needed to be covered by social security only on the last day of employment with the government entity in order to be exempt from GPO. Many teachers, in particular, were able to take advantage of this exemption. Congress further tightened the GPO provision, and on March 2, 2004, the President signed the Social Security Protection Act of 2004.

The Social Security Protection Act of 2004 required that beginning with applications filed April 1, 2004, state and local government workers be covered by social security throughout their last 60 months of employment with the government entity in order to be exempt from the GPO. If the worker's last day of government employment was covered by both social security and the pension system, and the last day occurred before July 1, 2004, the worker is exempt from GPO with respect to all current and future applications for spouse's or widow(er)'s benefits. For example, a teacher whose last day of government employment in June 2004 was covered under social security and the pension system would be exempt from the GPO regardless of when he/she filed for benefits.

The Act did provide a transition for workers whose last day of government employment occurred within 5 years after the date of enactment (March 2, 2004). Any state or local government worker whose last day of government employment occurred after June 30, 2004, and before March 2, 2009, could have the requirement for 60 months of social security covered government employment reduced. For these workers, the requirement for 60 consecutive months of social security covered employment was reduced (but not to less than one month) by the total number of months that the worker had in social security covered government service under the same retirement system before March 2, 2004. If the 60-month period was reduced, the remaining months of service needed to fulfill the requirement must have been performed after March 2, 2004.

> **Example.** Ms. Jones was working in a non-covered position at the time of enactment of the GPO, but had previously worked in a social security covered job in the same retirement system for 12 months in 1997. Because she had previously worked in social security covered employment for 12 months, the requirement that her last 60 months of employment be in a social security covered position would be reduced to 48 months, or four years. If Ms. Jones began working after March 2, 2004, in social security-covered employment under the same retirement system as her prior government work, **and** worked continuously in the covered position for at least the final 48-month period of her employment, **and** her last day of employment was before March 2, 2009, Ms. Jones would have been exempt from the GPO offset.

All other non-covered state and local government workers who first switched to government employment covered by social security and their pension plan after June 30, 2004, had to work in covered government employment for the entire final 60-month period of their government employment in order to avoid the GPO.

The Government Pension Offset does not apply to pension benefits that are:

- Not based on earnings, or
- Based on earnings in a job where the retiree was paying social security taxes, and
    a) the recipient filed for and was entitled to a benefit as a spouse, widow, or widower, before April 1, 2004; or
    b) the last day of employment that the pension is based on is before July 1, 2004; or
    c) the retiree paid social security taxes on earnings during the last 60 months of government service.

Benefits as a spouse, widow or widower will also not be reduced by the GPO if the individual:

- Is a federal employee who elected to switch from the Civil Service Retirement System (CSRS) to the Federal Employees' Retirement System (FERS) after December 31, 1987; and either:

    a) filed for and were entitled to spouse's, widow's or widower's benefits before April 1, 2004; or
    b) the last day of service (that your pension is based on) is before July 1, 2004; or
    c) paid social security taxes on earnings for 60 months or more during the period beginning January 1988 and ending with the first month of entitlement to benefits; or

- Received or was eligible to receive a government pension before December 1982 and met all the requirements for social security spouse's benefits in effect in January 1977; or

- Received or was eligible to receive a federal, state or local government pension before July 1, 1983, and were receiving one-half support from the spouse.

For more information, see the GPO Fact Sheet on the SSA website.

Savings Plans for WEP or GPO Purposes

The WEP and GPO apply to pensions provided by state and local government entities. Some public employers not covered by social security have established alternative retirement plans, such as a savings plan, instead of a conventional pension plan.

A plan is considered a savings plan and is not a pension for WEP/GPO purposes if:

- An employee voluntarily contributes to a plan that is separate from and in addition to a primary retirement plan;
- The employer makes no contributions to the plan;
- The withdrawals from the plan do not exceed the employee's contributions (plus interest); and

- Withdrawals are not based upon age, length of service or earnings.

In addition to savings plans, the following are not considered pensions for purposes of the WEP and GPO:

- A social security retirement or disability benefit
- An early incentive retirement payment

A survivor annuity is exempt from the Windfall Elimination Provision; however, social security survivor benefits may be affected by the Government Pension Offset.

> **Example 1:** A part-time employee for a city is not covered by a Section 218 Agreement or mandatory social security. In July 1991, the employee elected to participate in the state's public employees deferred compensation plan in lieu of mandatory social security coverage. The employee, upon retirement, will receive a payment from the deferred compensation plan based on employee and employer contributions to the plan, as this is the only plan to which the employee contributes. This plan is not considered a savings plan and the payment will be considered a pension and subject to the GPO or WEP provisions.

> **Example 2:** A state employee is not covered by a 218 Agreement, but is covered by a state employee retirement system and has also elected to make contributions to a deferred compensation plan. The payment from this deferred compensation plan is separate from and in addition to the primary retirement plan. The employer made no contributions to the deferred compensation plan and the payment from the deferred compensation plan is not based on age, length of service or earnings. While the payment from the retirement system is subject to GPO or WEP, the payment from the deferred compensation plan is not.

SSA Publication 05-10045, covering the WEP, and SSA Publication 05-10007, covering the GPO, address these topics further. You can also request these publications from the Social Security Administration by calling 1-800-772-1213. Employers assisting in retirement planning are urged to provide copies of these publications to their employees.

Medicare

SSA is the primary public contact point regarding eligibility and premium issues for the Centers for Medicare & Medicaid Services (CMS), which is responsible for administering the Medicare program. SSA staff determines, and answers questions regarding Medicare eligibility. SSA also maintains records of Medicare eligibility and collects Medicare Part B premiums through withholding from social security payments.

The Medicare tax supports a federally-funded health insurance program for people 65 years of age and older and people with certain disabilities. Medicare has four parts:

- Hospital insurance (Part A) that helps pay for inpatient care in a hospital or skilled nursing facility (following a hospital stay), some home health care and hospice care.
- Medical insurance (Part B) that helps pay for doctors' services and many other medical services and supplies that are not covered by hospital insurance.
- Medicare Advantage (Part C) plans, available in many areas through third-party insurers. People with Medicare Parts A and B can choose to receive all of their health care services through one of these provider organizations under Part C.
- Prescription drug coverage (Part D) that helps pay for medications doctors prescribe for treatment.

You can get more information about Medicare at the CMS site www.medicare.gov.

Medicaid

Medicaid provides free or low-cost health insurance coverage to qualifying individuals and families. In 32 states and the District of Columbia, eligibility for SSI benefits confers automatic entitlement to Medicaid. SSA provides information and referral services in support of Medicaid and is directly funded by the states and CMS.

For more information, see the CMS Medicaid site at cms.gov/MedicaidGenInfo/.

Reporting Wages to SSA

As discussed in Chapter 3, all employers are responsible for collecting social security numbers from employees, filing tax returns to the Internal Revenue Service, filing annual wage reports (Forms W-2) with the Social Security Administration, and furnishing copies of Forms W-2 to employees. To avoid costly errors, it is crucial that Form W-2 filing be accurate.

All Forms W-2 sent to SSA are subject to:

- Balancing and validation programs to determine whether the reports are accurate and can be "read" by SSA systems; and
- Employee name and social security number (SSN) verification.

Reports that have errors, do not match, or do not meet edit conditions are returned to the employer (or submitter) for correction and resubmission.

Employers failing to meet filing requirements by the deadlines are subject to IRS late filing penalties (see Chapter 3).

Note: *If the initial report was filed timely and later returned for corrections, the employer will be subject to late filing penalties if the corrected report is not resubmitted by the due date.*

Electronic Wage Reporting

Employers with Internet access can submit their W-2 files using SSA's SSA Business Services Online. This option is fast, free and secure. For security, a PIN and a password are required before you submit your W-2 file over this web page; most registrations can be completed on the web page. For more information, visit the SSA employer page or call your ESLO (see list at website).

Social Security Statement

SSA sends a statement annually to workers and former workers aged 25 and older who have paid social security taxes during their working years. This statement shows all earnings on which a worker has paid social security taxes during his/her working years. The statements should be examined closely by the employee to ensure all earnings are properly credited. If the earnings shown on the statement are not correct, the employee should call SSA at 1-800-772-1213.

Note: *Individuals who have worked only in non-covered employment (no social security and Medicare taxes) will not receive a Social Security Statement.*

The Medicare portion of the Social Security Statement reflects the amount of earnings that was taxed and an estimate of the amount of taxes paid to support the Medicare program. The taxes are estimated because SSA does not keep records of Medicare taxes paid. If an employee had both social security earnings and government earnings that qualified for Medicare in the same year, the statement would reflect an estimate of the combined Medicare taxes paid.

Workers may access on-line benefit planning tools at the SSA planning page. These can be used to project potential benefits using various earnings scenarios.

Verifying Employee Names and Social Security Numbers

After wage reports have been entered into SSA's system, each employee name and social security number (SSN) is compared to SSA's records to verify that it is correct. Matched wage reports are updated to the individual employee's record; reports that do not match are identified and the employer or employee is contacted and asked to provide a corrected name or SSN to SSA. Additionally, IRS may impose a penalty of up to $100 per misreported name and SSN. Accurate crediting of earnings to individual records is essential to the correct payment of social security benefits; this is one reason obtaining a correct name and SSN is very important. See IRS Publication 15, for a discussion of requirements for new hires.

Social Security Number Verification Service

The Social Security Number Verification Service (SSNVS) is a free, internet-based service of the SSA Business Services Online (BSO) where employers and third-party submitters can verify their employees' names and SSNs against SSA's records. For more

information on SSNVS, see the SSA SSNVS Handbook. Employers are required to register with SSA to use the service.

With SSNVS, you may verify up to 10 names and SSNs online and receive immediate results. There is no limit to the number of times the SSN Verification web page may be used within a session. You may upload electronic files of up to 250,000 names and SSNs and will usually receive results the next government business day.

In addition to SSNVS, the BSO offers Registration Services and Employer Services. Registration Services offers a User Identification Number (User ID) assignment, password selection and various registration maintenance functions. Employer Services offers Form W-2 file upload, W-2 and W-2c online key-in functions (no special software or forms required) and the ability to track files and view processing results and notices. See the SSA BSO page for more information.

Note: *SSNVS should only be used for the purpose for which it was intended. SSA will verify SSNs and names solely to ensure that the records of current or former employees are correct for the purpose of completing Form W-2.*

Verifying Employment Eligibility

Under the Immigration and Nationality Act, employers must verify the identity and employment eligibility of anyone hired for employment in the United States. This includes citizens and non-citizens.

Form I-9 Employment Eligibility Verification, was developed by the former Immigration and Naturalization Service (INS) to verify that persons are eligible to work in the United States. Completion of this form is required for every employee hired after November 6, 1986. The functions of the INS are now carried out by the U.S. Citizenship and Immigration Service (USCIS). The USCIS operates I-9 Central, a free website providing employers and employees access to resources, tips and guidance to properly complete Form I-9 and better understand the Form I-9 process.

USCIS also operates an electronic employment eligibility verification system, E-Verify, for employers. If you have questions about Form I-9, contact E-Verify Customer Support at 1-888-464-4218 or the E-Verify web page.

You can download copies of Form I-0 from www.uscis.gov. USCIS Publication M-274, Handbook for Employers, includes Form I-9 and addresses questions relating to the form and employment issues related to immigration. Print copies are available to employers at USCIS regional and district offices, as well as local Government Printing Office bookstores. For questions not addressed in the Handbook, visit the USCIS website at www.uscis.gov or call (202) 375-5283.

Correcting Wage Reports

Once information returns have been filed with SSA, you must make any corrections using Form W-2c and Form W-3c.

Forms W-2c may be filed on paper or via electronic transmission. Electronic submissions should be formatted following the instructions in SSA Publication 42-007, Specifications for Filing Forms W2 Electronically (EFW2), are available on SSA's website or from any Employer Service Liaison Officer (ESLO). A list of the ESLOs is also available at this site.

Note: *As of February 28, 2006, SSA no longer accepts magnetic media submissions for wage reports. If you are required to file 250 or more Forms W-2c during a calendar year, you must file them electronically unless IRS grants you a waiver. For information on filing Form 8508, Request for Waiver From Filing Information Returns Electronically, contact IRS at 1-866-455-7438, or visit www.irs.gov.*

If the employee has a name change, the employee must notify SSA and request a new social security card. ***Never*** change an employee's name in your payroll system until the employee has shown you a new social security card showing the change. See IRS Publication 15 (Circular E) for rules on name changes.

If an error is identified before Form W-2 is filed with the SSA, but after providing the form to the employee, changes should be shown on a new original form. This form should be marked "Reissued Statement" at the top. Be sure to change the information submitted to SSA as well, either by marking the original paper W-2 "VOID" at the top (if you submit on paper) or by correcting the data file before filing electronically.

Form W-3c must accompany Copy A of Forms W-2c when they are sent to SSA. A separate Form W-3c must be used for each type of Form W-2 being corrected and must accompany a single Form W-2c or multiple Forms W-2c. Large numbers of Forms W-2c may also be filed electronically. Contact your ESLO for details.

Common Reporting Errors

Incorrect or missing Employer Identification Number (EIN). SSA and IRS maintain records by the EIN. Reports received with missing or erroneous EINs may be credited to the wrong record and result in IRS assessing penalties for failure to file correct reports.

Incorrect employee names and social security numbers. SSA cannot credit earnings to an employee's record unless the employee's name and social security number on the wage report matches the name and number in the SSA files. Use the name exactly as it is shown on the employee's social security card.

Wage reports for years after employee's death. Payments on behalf of a deceased employee made after the year of death cannot be credited as wages for social security

purposes. Such payments should be reported to the employee's estate on Form 1099-MISC, Miscellaneous Income. See Section 3.

Errors resulting in out-of-balance reports. Errors may occur due to application of an incorrect wage base for social security or a wage base limitation to the Medicare wages.

Tips. If an employee has tips, they must be reported in the "Social security tips" field of Form W-2). They are **not** included in the "Social security wages" field. These two fields are added together by SSA to obtain the total social security earnings.

Omitted wage or tax fields on wage reports. All fields must be completed.

Wrong tax year form used. SSA optical scanning and imaging systems are modified annually to meet changes in Form W-2 formats. The version of Form W-2 for the year reported must be used or SSA may be unable to read the form, or post the earnings to the wrong year.

Unscannable reports. Reports that are not scannable by the SSA's optical equipment are more costly to process and subject to error.

Failure to file Copy A of Form W-2 with SSA. Employers must always file Copy A of Form W-2 with SSA, unless they submit the same data electronically.

"Void" indicator on Form W-2 checked in error. SSA will not credit wages shown on any Form W-2 that is void.

Wrong tax year entered. Make sure you show the correct tax year on the code "RE" records. Dollar totals ("RT" Record) are used by SSA to determine whether the report is in balance; and, if it is not, to show where the error may be found. Make sure you report employee names and social security numbers correctly.

Missing/Incorrect submitter (Code "RA"). This information helps SSA properly identify and control each report. It provides contact information for use if there is a problem with the submission.

Unreadable reports. Reports must meet the requirements set out in EFW2 to be processable on SSA's electronic equipment. Unprocessable reports will be returned to the transmitter for correction and returned to SSA. Failure to return the correction reports timely may result in IRS penalty assessment.

Incorrect or omitted Medicare wage/tip amounts. Medicare wages/tips must be shown separately from social security wages on Forms 941 filed with the IRS. All Medicare wages/tips are subject to Medicare taxes.

Showing non-covered amounts as social security and/or Medicare wages. Examples of non-covered amounts include employee earnings that exceed the wage base for social security and payments to an independent contractor shown as wages. See "Special Rules

for Various Types of Services and Payments" in Publication 15 for information on other non-covered payments.

Failure to file Form W-2c and/or Form W-3c with SSA when adjusting prior year earnings on Form 941 and/or Form 941c. Adjustments of tax liability filed with IRS that are based on changes in social security and/or Medicare wages must be matched by the filing of Forms W-2c and W-3c with SSA to allow entry of the wage changes on the employee's social security earnings records.

Filing of duplicate or partially duplicate Forms 941. Social security and/or Medicare wages shown on duplicate Forms 941 may lead to costly and otherwise unnecessary reconciliations between SSA, the IRS and the employer.

Publications and Forms – Social Security Administration

To request SSA publications, telephone 1-800-772-1213 (toll-free), or TTY 1-800-325-0778, or e-mail to mailto:OPLM.OSWM.RQCT.Orders@ssa.gov. You can also download most forms and publications from the SSA employer page.

Publication/F	Title
SS-5	Application for a Social Security Card
Social Security Number Verification Service (SSNVS) Handbook	
SSA 42-007	Specifications for Filing Forms W-2 Electronically (EFW2)
SSA 42-014	Specifications for Filing Forms W-2c Electronically (EFW2)
Form SSA-1945	Statement Concerning Your Employment in a Job Not Covered by Social Security

Other SSA Services

SSA Speaker's Bureau

SSA can arrange to have speakers available for wage reporting seminars, pre-retirement sessions and other employer-sponsored onsite meetings with employees to discuss social security matters. For more information, contact any Social Security office or call 1-800-772-1213. For a local SSA office near you, see SSA contact page.

Employer Training Seminars

Each year, Employer Service Liaison Officers (ESLOs) provide a series of free training seminars to annual wage reporters. Call your local ESLO to find out when a seminar is held in your area. Or check the website for a list of seminars held around the nation.

Key SSA Web Pages

Employer Reporting Instructions and Information

This SSA website addresses employer reporting and other interests.

Social Security Online

SSA's home page that lists available online services such as benefit planners, Social Security Statements, Medicare card replacement, etc.

State and Local Government Employers

This site is for state and local government employers who are responsible for withholding, reporting and paying social security and Medicare taxes for public employees.

POMS State and Local Coverage Handbook

Explains the provisions applicable to State Social Security Administrators and Social Security's regional and parallel office (PSSO) staffs to administer the social security and

Research, Statistics and Policy Analysis

The research and policy analysis information on the SSA website is the result of a collaborative effort among three ORDP offices—the Office of Research, Demonstration, and Employment Support, the Office of Research, Evaluation, and Statistics, and the Office of Retirement Policy. All three offices work together to conduct research and policy analysis and disseminate the results of their research in a variety of publications that are available on the website.

Frequently Asked Questions

1) **If the IRS is responsible for answering questions on withholding and paying social security and Medicare taxes, why do we get reporting information from SSA and why do we have to send IRS Forms W-2 to SSA?** SSA is responsible for keeping records of earnings, and for determining eligibility and amounts for individuals applying for retirement, disability or survivor benefits. The amount of benefits an individual receives is based in part on that individual's earnings over his or her working career. The information on an individual's earnings record is taken directly from the social security and Medicare wage fields on the Form W-2 sent to SSA by the employer. After SSA processes this information, it is forwarded to the IRS. Either IRS or SSA can help you with Form W-2 reporting questions. [IRS/SSA]

2) **How does an employee verify the information that SSA shows on her/his earnings record?** A Social Security Statement is mailed annually to workers and former workers aged 25 and older who have worked in covered employment. There is no charge for this service. [SSA]

3) **What information can be provided by SSA to State Social Security Administrators to help them perform their responsibilities?** SSA may provide interpretations of the Social Security Act, Social Security regulations, rulings, the state Section 218 Agreement and its modifications, as they apply to a public employer. [SSA]

4) **Whom should I call when I have questions about Annual Wage Reporting?** Call your local SSA Employer Services Liaison Officer. See Chapter 7, or go to the SSA website for contact information. [SSA]

5) **My employees are paying into the State Teachers' Retirement System and some have enough social security credits from former employment to be eligible for social security benefits. Will they receive benefits from both?** Yes, but the Windfall Elimination Provision may reduce social security benefits. Additionally, spouses' benefits may be reduced by the Government Pension Offset formula. See Chapter 6, Social Security and Public Retirement Systems. [SSA]

Chapter 8

Internal Revenue Service

The Internal Revenue Service (IRS), an agency of the U.S. Department of Treasury, is charged with the administration of the tax laws passed by Congress. This includes assisting taxpayers with education, account issues, and filing responsibilities, as well as conducting compliance and enforcement activities. For many years, the IRS was organized geographically with a national office in Washington and regional, district and local offices throughout the country. With the Restructuring and Reform Act of 1998, the Internal Revenue Service began a major reorganization in an effort to improve compliance and customer service. This restructuring marked the most sweeping overhaul of the agency since 1952. The reorganization and its impact on federal, state, and local government entities are discussed in this chapter.

More information about the programs and responsibilities of the IRS is available at www.irs.gov. For information about the IRS office of Federal, State, and Local Governments, see the FSLG web site.

Organization

National Headquarters for the Internal Revenue Service, in Washington, DC, develops nationwide policies and programs for the administration of the agency. The chief executive of the agency is the IRS Commissioner. Several functions report directly to the Commissioner, including:

- Chief Counsel
- Appeals
- National Taxpayer Advocate
- Communications and Liaison
- Office of Research, Analysis, and Statistics
- Equity, Diversity & Inclusion

With the 1998 reorganization, the IRS is now organized around four specific "customer bases," or groups of taxpayers with generally common interests and needs. Each operating division has a Commissioner and its own Counsel to provide legal expertise and guidance. This structure replaces the system of Regional and District Offices that existed under the previous, geographically-based organization.

The following are the four customer-based operating divisions:

Wage and Investment (W&I) is focused on individual taxpayers and income tax returns.

Small Business/Self-Employed (SB/SE) is oriented to S-corporations, partnerships, small corporations and sole proprietors.

Large Business and International (LB&I), deals with the largest businesses and international tax issues. (This was formerly the Large and Mid-Size Business division).

Tax Exempt and Government Entities (TE/GE) serves all government organizations as well as nonprofit and other exempt organizations. Most or all of the contact with the IRS that a government entity has will be with TE/GE, so it is discussed in more detail below. TE/GE has responsibility for providing assistance and education to taxpayers, as well as performing compliance activities related to these organizations.

Tax Exempt and Government Entities Operating Division

The Tax-Exempt and Government Entities (TE/GE) Operating Division was established in late 1999 and replaced the former office of Assistant Commissioner (Employee Plans and Exempt Organizations). It serves three distinct customer segments:

- Employee Plans (EP)
- Exempt Organizations (EO)
- Government Entities (GE)

TE/GE deals with entities that are or may be exempt from certain taxes under the Internal Revenue Code. Customers range from small local community organizations and municipalities to major universities, large pension funds, state governments, federal agencies, Indian tribal governments and issuers of tax-exempt bonds. These organizations represent a large economic sector with unique needs. They are governed by often complex, highly specialized provisions of the tax law.

The Government Entities (GE) segment contains three offices serving distinct customer bases:

- Federal, State, and Local Government (FSLG)
- Indian Tribal Governments (ITG)
- Tax-Exempt Bonds (TEB)

Federal, State, and Local Governments: Provides a clear point of contact for all government entities (other than Indian tribal governments) for their tax issues with the primary focus on information return reporting and employment tax issues. FSLG is responsible for administering the tax laws affecting these entities and ensuring compliance. It also develops and delivers communication and education programs and provides easily accessible and equitable voluntary compliance programs for its government customers.

The Federal, State and Local Governments website contains the most recent technical developments and links to additional information, including:

- How to contact an FSLG Specialist in your area

- How to e-mail FSLG with a question
- A toolkit providing all basic federal tax reporting materials in one location
- Links to text of recent IRS rulings and announcements
- Fact sheets and frequently asked questions
- FSLG *Fringe Benefit Guide* (Publication 5137)
- *Quick Reference Guide for Public Employers* (Publication 5138)
- The semiannual FSLG Newsletter
- Announcements and registration information for educational events
- Explanation of the compliance process (examinations and compliance checks)
- Archived webinar and phone forum presentations on tax topics
- Links to related sites of interest

Indian Tribal Governments: Helps Indian tribes deal with their federal tax matters, and provides a single point of contact for assistance and service. The Specialists in this area address issues and provide guidance to Indian tribes, whose concerns may relate to tribal governments as employers, distributions to tribal members, and the establishment of governmental programs, trusts, and businesses. For more information visit the Indian Tribal Governments website.

Tax-Exempt Bonds: Provides information to the tax-exempt bond community in the form of education and outreach programs. This office encourages voluntary compliance through rulings and agreements. It also administers and conducts the tax-exempt bond examination program. For more information, visit the Tax Exempt Bond website.

Customer Account Services

If you are authorized to represent a taxpayer, you can call toll-free at (877) 829-5500 concerning the following as they relate to government entities:

- Account-related questions
- Request for general information letter concerning tax exemption of a government
- Request for private letter ruling
- FSLG telephone numbers
- Local FSLG Offices

Note: *Although the State Administrator is responsible for maintaining and interpreting your Section 218 Agreement, federal disclosure laws prohibit the State Administrator from inspecting your tax information without your consent. If you would like the State Administrator to assist you with a Section 218 Agreement or related social security coverage issue, you can expedite the process by completing Form 8821, Tax Information Authorization, and filing it with the IRS.*

You may contact your local FSLG Specialist for assistance with any of the following:

- General information about a Section 218 Agreement between your state and the Social Security Administration

- Classification of a worker as an employee or independent contractor
- Form SS-8, *Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding*
- Special employment tax rules for public employees (election workers, emergency workers, public officials, etc.)
- Withholding from nonresident aliens
- Other federal tax issues for government entities

Publications and Forms — Internal Revenue Service

You can download most IRS forms and publications from the IRS website. To order by phone, call 1-800-829-3676 (toll-free). To request forms by fax, call 1-703-368-9694 from your fax machine. Forms and publications are also available at IRS walk-in offices.

Publication	Title
1	*Your Rights as a Taxpayer*
15	*Circular E, Employer's Tax Guide*
15-A	*Employer's Supplemental Tax Guide*
15-B	*Employer's Tax Guide to Fringe Benefits*
80	*Circular SS, Federal Tax Guide for Employers in the U.S. Virgin Islands, Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands*
463	*Travel, Entertainment, Gift and Car Expenses*
515	*Withholding of Tax on Nonresident Aliens and Foreign Entities*
571	*Tax-Sheltered Annuity Plans (403(b) Plans)*
594	*The IRS Collection Process*
910	*IRS Guide to Free Tax Services*
947	*Practice Before the IRS and Power of Attorney*
957	*Reporting Back Pay and Special Wage Payments to the Social Security Administration*
1141	*General Rules and Specifications for Substitute Forms W-2 and W-3*
1179	*General Rules and Specifications for Substitute Forms 1096, 1098, 1099, 5498, and Certain Other Information Returns*
1976	*Do You Qualify for Relief Under Section 530?*
2108A	*On-Line Taxpayer Identification Number (TIN) Matching Program*
4268	*Employment Tax Desk Guide* (available only at www.irs.gov/tribes)

Form	Title
SS-4	*Application for Employer Identification Number*
SS-8	*Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding*
W-2	*Wage and Tax Statement*
W-2c	*Corrected Wage and Tax Statement*
W-3	*Transmittal of Wage and Tax Statements*
W-3c	*Transmittal of Corrected Wage and Tax Statements*
W-4	*Employee's Withholding Allowance Certificate*
W-9	*Request for Taxpayer Identification Number and Certification*
941	*Employer's Quarterly Federal Tax Return*
941-X	*Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund*
943	*Employer's Annual Tax Return for Agricultural Employees*
944	*Employer's Annual Federal Tax Return*
944-X	*Adjusted Employer's Annual Federal Tax Return or Claim for Refund*
945	*Annual Return Of Withheld Federal Income Tax*
945-A	*Annual Record of Federal Tax Liability*
1042	*Annual Withholding Tax Return for U.S. Source Income of Foreign Persons*
1042-S	*Foreign Person's U.S. Source Income Subject to Withholding*
1096	*Annual Summary and Transmittal of U.S. Information Returns*
1099-MISC	*Miscellaneous Income*
2848	*Power of Attorney and Declaration of Representative*
8233	*Exemption from Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual*
8821	*Tax Information Authorization*

The IRS website also offers the following free of charge:

- Forms and Publications on CD/DVD
- IRS press releases and fact sheets
- TeleTax (automated) information on about 100 tax topics (1-800-829-4477)
- Educational Materials

Telephone assistance is available at 1-800-829-1040.

Frequently Asked Questions

1) **What information can IRS provide to a governmental unit about its social security coverage and tax liability?** The IRS is responsible for assessing and collecting all taxes, and interpreting and applying the tax law. By contacting Customer Account Services, an authorized person can receive tax information about an entity. Your local Federal, State, and Local Government (FSLG) Specialist can assist you with tax law questions, including identifying the services subject to income and social security taxes. Questions about Section 218 Agreement coverage should be directed to your State Social Security Administrator.

2) **What information can IRS provide to State Social Security Administrators to help them perform their responsibilities, especially when an audit or review is to be conducted of a public employer in his/her state?** Section 6103 of the IRC governs the disclosure of tax information by the IRS to other federal and state agencies. Without the consent of the taxpayer, no provision in section 6103 authorizes the IRS to share specific taxpayer information with State Social Security Administrators. However, in performing a tax investigation, the IRS may request information from the State Social Security Administrator. State administrators are encouraged to share information, consistent with state law, with the IRS to help resolve matters of mutual interest. Your State Social Security Administrator can better assist you if you consent to make your federal tax information available for the Administrator's review. A government entity can grant a State Administrator access to its tax information by completing Form 8821, Tax Information Authorization. [IRS]

3) **Can I arrange for the State Social Security Administrator to receive my tax information or discuss it with the IRS?** If you have a Section 218 Agreement to provide social security coverage for your employees, you may wish to have the State Social Security Administrator consulted or otherwise involved in the examination. The State Administrator is not considered an official responsible for the administration of state or federal tax laws under section 6103; therefore, there is no provision in the law allowing the IRS to disclose tax information in this situation. If you are reviewing an issue with the IRS involving section 218 coverage, and you wish to have the State Administrator or a representative participate in the discussion, you should complete either **Form 2848**, *Power of Attorney or Declaration of Representative*, or **Form 8821**, *Tax Information Authorization*, as appropriate. These forms are discussed on the Disclosure Laws page on the FSLG website.

Chapter 9

State Social Security Administrators

SSA Regulation 20 CFR §404.1204 requires each state to designate at least one state official to act for the state in administering that state's Section 218 Agreement. This official, the State Social Security Administrator, acts for the state with respect to its responsibilities for maintaining and administering the provisions of the agreement and for the proper application of Social Security and Medicare.

The designated State Social Security Administrator (State Administrator) acts for the state in negotiations with the Social Security Administration. This includes acting for the state with respect to the initial Section 218 Agreement and modifications, the performance of the state's responsibilities under the Agreement, and in all state dealings concerning the administration of the Agreement. Each state's Section 218 Agreement ("Agreement"), and Social Security Regulations 404.1204, provide a legal obligation for each state to designate such an official. In many states, however, the actual day-to-day responsibilities are delegated to the staff of the designated state official.

The state is responsible for notifying SSA of any changes regarding its designated state official. That official should send a notification to the SSA Regional and Parallel Social Security Offices for that state.

The extent of the responsibilities of the State Administrator vary from state to state. The location of State Social Security Administrators' offices and the extent and scope of their responsibilities are determined by each state. Details on each state are contained in the respective state's enabling legislation, citations for which are listed in the Appendix of this Guide. Frequently, a State Administrator has other responsibilities, including those related to non-218 entities as well. A detailed list of basic State Administrator responsibilities is available on the Social Security Administration's POMS web at the Program Operations Manual System (POMS) web page. Also see the SSA State and Local Government Employer web page.

For Section 218 Agreement purposes, the State Administrator:

- Administers and maintains the federal-state Section 218 Agreement that governs voluntary social security and Medicare coverage by state and local government employers in the state;
- Negotiates modifications to the original Agreement to include additional coverage groups, corrects errors in modifications; conducts referendums and identifies additional political subdivisions that join a covered retirement system;
- Maintains in a secured location the state's master Agreements, modifications, dissolutions and intrastate agreements;
- Provides SSA with notice and evidence of the legal dissolution of covered state or political subdivision entities;

- Resolves coverage and taxation questions related to the Agreement and modifications with SSA and IRS; and
- Negotiates with SSA to resolve social security contribution payment and wage reporting questions concerning wages paid before 1987;
- Informs SSA of name, title, and address of designated officials involved in Section 218 administration, and notifies SSA of any changes;
- Informs SSA of any changes in a government entity's legal status, such as name changes, dissolutions, or consolidations.
- Communicates regularly with SSA, IRS, employers, and stakeholders on Section 218-related issues;
- Provides information to state and local public employers covered under Agreements in accordance with the Act; and
- Determines necessary funding and staffing for administration of Section 218 program.

Note: *Section 6103 of the Internal Revenue Code (IRC) governs the disclosure of tax information by the IRS to other federal and state agencies. Without the consent of the taxpayer, no provision in section 6103 authorizes the IRS to share specific taxpayer information with State Social Security Administrators. However, in performing a tax investigation, the IRS may request information from the State Social Security Administrator.*

The State Administrator is the principal state official responsible for these functions. The Administrator serves as the main resource to state and local employers for information and advice about social security coverage, taxation and many reporting issues. SSA, IRS, public employers and employees should contact the designated Administrator to help resolve coverage questions concerning groups or individual employees. More detailed information is available at the SSA POMS web page.

By allowing the State Administrator to inspect your tax information, you can significantly expedite the process of resolving any coverage or federal tax issues with the IRS. A government entity may consent to have a State Administrator or representative review tax information by filing Form 8821, Tax Information Authorization, and filing it with the IRS.

National Conference of State Social Security Administrators (NCSSSA)

The ever-changing and complex social security coverage statutes, withholding requirements, reporting obligations and associated employment tax regulations require constant monitoring and interpretation. For more than 50 years the National Conference of State Social Security Administrators (NCSSSA) has provided an effective network of communication for federal, state, and local governments concerning social security coverage and federal employment tax policy.

With the enactment of Section 218 to the Act in 1950, states could exercise the option of providing social security coverage for state and local employees. By the end of 1951, 30

states had executed Section 218 Agreements with the federal government. The responsibility for administering the social security program varied from state to state, depending on the particular state's enabling legislation.

State Administrators began to operate in an area where no precedent existed. It became apparent that a forum was needed where the administrators could address the many problems and questions posed by the new program. The first forum between State Social Security Administrators and federal officials was held in January 1952, in Bloomington, Indiana. As a result, the NCSSSA was established to provide a unified state perspective at the federal level to provide an on-going medium for problem-solving and to maintain an open forum for the development of new policy.

Since its formation in 1952, the NCSSSA has worked closely with SSA and IRS to address social security (and later Medicare) coverage and employment tax issues raised by state and local employers and State Social Security Administrators throughout the United States. The NCSSSA works with the federal officials to ensure that legislative and regulatory changes address state and local concerns. The NCSSSA provides leadership to state and local governments through accurate interpretation of federal laws and regulations, communication of federal tax policy, and resolution of problems arising at the state and local level. The NCSSSA hosts national workshops and annual meetings where SSA and IRS officials address the concerns of state and local government representatives in a face-to-face format. NCSSSA officials represent public sector employers on various SSA and IRS committees and work groups.

Audits and Reviews of Public Employers

When the IRS or SSA conducts an audit or review of a public employer, it may contact the State Administrator for that state to clarify the employer's status, including:

- Whether the employees are covered under a Section 218 Agreement; and, if so,
- The specific exclusions (mandatory **and** optional) that are applicable to that entity that must be taken into account during the audit or review, including any that are unique to individual employees (for example, whether any employees are subject to the Medicare continuing employment exemption).

For further information about the NCSSSA, contact your State Social Security Administrator. (See the list at NCSSSA's website, www.ncsssa.org.)

Glossary

Absolute Coverage Group (also called a "non-retirement coverage group) - for Section 218 coverage purposes, a group of employees whose positions are not covered under a public retirement system; also referred to as a "non-retirement system coverage group" or a "Section 218(b)(5) coverage group".

Alternative Lookback Rule – An optional method for determining whether an employee can be treated as a qualified participant in a retirement plan for purposes of determining whether mandatory social security applies. Under this rule, an employer may treat an employee as a qualified participant in the first year of employment if it is reasonable to believe the employee will be a qualified participant on the last day of the plan year. An employer may treat an employee as a qualified participant in a calendar year if the employee was a qualified participant at the end of the previous plan year. See Section 31.3121(b)(7)-2(d)(3), Employment Tax Regulations.

Continuing Employment Exception – Provision for exclusion of an employee from Medicare tax and coverage for services of a state or local government employee who is not covered by a Section 218 Agreement and is a participant in a public retirement system and meets all of the following requirements:

- The employee was performing regular and substantial services for remuneration for the employer before April 1, 1986;
- The employee was a bona fide employee on March 31, 1986;
- The employment relationship was not entered into for purposes of avoiding the Medicare tax; and
- The employment relationship with the employer has not been terminated after March 31, 1986.

Coverage Groups – Categories of state and local government employees with respect to a Section 218 Agreement. There are two types of coverage groups:

1. ***Absolute coverage groups***, composed of employees in positions not covered under a retirement system; and

2. ***Retirement system coverage groups***, composed of employees in positions covered by a retirement system.

The Social Security Act gives each state the right, within the limits of state and federal laws, to decide which coverage groups are to be included under its Agreement and any modifications to the Agreement.

Defined Benefit Plan – An employer plan that determines retirement benefits under a formula, generally based on age, years of service and salary level.

Defined Contribution Plan – An employer plan that provides for an individual account for each participant and for benefits based solely on the amount contributed to the participant's account, and any income, expenses, gains, losses and forfeitures of accounts of other participants that may be allocated to the participant's account.

Earnings Record - The information maintained by the Social Security Administration for an individual indicating social security and Medicare covered wages and self-employment income. Each individual's record is accessed by social security number (SSN).

Employee – Generally any individual who, under the usual common-law rules applicable in determining the employer-employee relationship, is subject to the employment tax requirements of Internal Revenue Code (IRC) 3121 and 3401. The term is defined for social security and Medicare purposes in Sections 210(j) and 218(b)(3) of the Social Security Act and IRC section 3121(d).

Employer Identification Number (EIN) – A unique nine-digit identification number assigned by IRS to state and local governments, businesses, and other entities for tax-filing and reporting purposes, including withholding and paying FICA taxes. An entity can obtain an EIN by filing Form SS-4, Application for Employer Identification Number, with the IRS.

Entity – A separate legal "person," that is not an individual; includes a corporation, partnership, LLC, or a political unit, including a state, a political subdivision, a wholly-owned instrumentality, a municipality, etc.

Federal Insurance Contributions Act (FICA) – Federal statute providing for payroll tax deduction to fund social security and Medicare coverage.

Federal Unemployment Tax Act (FUTA) – Federal statute imposing tax on employers in order to provide for payments of unemployment compensation to workers who have lost their jobs. States and political subdivisions of a state are exempt from paying FUTA, but under state unemployment law, most state and local government employees must be covered for state unemployment insurance.

Fee-Based Public Official – A public official who receives and retains remuneration directly from members of the public; for example, a justice of the peace. An official who receives payment for services from government funds in the form of a wage or salary is not a fee-based public official, even if the compensation is called a fee.

FICA - Federal Insurance Contributions Act; refers to social security and Medicare taxes withheld from wages to fund the social security system.

FICA Replacement Plan – Alternate name for a public retirement system, as described in the regulations for section 3121(b)(7)(F). Refers to a pension, annuity, retirement, or

similar fund or system established by a state or political subdivision for the purpose of providing retirement benefits to employees. See Public Retirement System.

FRA (Full Retirement Age) – The age at which unreduced social security benefits are payable. Depending on the date of birth, an individual's FRA ranges from 65 to 67.

Full Social Security – Coverage for both the Old-Age, Survivors, and Disability Insurance (OASDI) program and Medicare Hospital Insurance (HI). Both the employer and employee pay these taxes.

FUTA - Federal Unemployment Tax Act; refers to tax paid by employers to fund unemployment insurance. Government employers are generally not subject to FUTA.

Governmental Function – Activity normally associated with the authority of government, legislative, executive, judicial, such as the control and prevention of crime, promoting the general welfare, and providing for public safety. Income derived from any essential governmental function is exempt from federal income tax under IRC section 115.

Government Pension Offset (GPO) – A reduction in the social security benefits that applies to individuals who (1) receive a government pension from work not covered for social security and (2) are eligible for social security as a spouse or widow(er). Two-thirds of the government pension offsets any spouse's or widow(er)'s social security benefit.

HI - Hospital Insurance (Medicare Part A).

Indian Tribal Government – The governing body of any federally recognized tribe, band, community, village or group of Indians or Alaska Natives that is determined by the Secretary of the Treasury, with the Secretary of the Interior, to exercise governmental functions, under IRC section 7701(a)(40). Under IRC section 7871, an Indian tribal government is treated as a state for certain purposes. Likewise, a subdivision of an Indian tribal government is treated as a political subdivision of a state if that the subdivision has been delegated the right to exercise one or more of the substantial governmental functions of the Indian
Tribal government. However, a tribal government is not a "state" for purposes of Section 218 and is not eligible for a Section 218 Agreement.

Interstate Instrumentality – An independent legal entity organized by two or more states to carry out one or more governmental functions. For purposes of a Section 218 Agreement, an interstate instrumentality has the status of a state.

IRC - Internal Revenue Code.

IRS - Internal Revenue Service.

Mandatory Exclusions – Categories of services that are not covered for social security under Sections 210 and 218 of the Social Security Act. These exclusions should not be confused with the the different set of exclusions that apply to those services not covered under the Section 210 mandatory social security provisions.

Mandatory Medicare (HI) – Medicare tax and coverage not included as part of a Section 218 Agreement; imposed on all state and local government employees hired or rehired after March 31, 1986.

Mandatory Social Security – Required social security coverage for state and local government employees who are not members of a public retirement system and who are not covered by a Section 218 Agreement; effective July 2, 1991.

Medicare – Federally established health insurance program for people age 65 and older and certain people with disabilities. Part A (Hospital Insurance – HI) is financed through employer and employee taxes on covered wages/self-employment or by individual payment of monthly premiums. Part B (Supplemental Medical Insurance – SMI) is financed by individuals paying monthly premiums.

Medicare Qualified Government Employment (MQGE) – Services of state and local government employees subject to Medicare tax but not to social security tax.

Modification – An amendment to an original Section 218 Agreement to extend coverage to additional groups of employees or to implement changes in federal and state laws. Each modification, like the original Agreement, is a legally binding document.

MQGE – Medicare Qualified Government Employment.

NCSSSA (National Conference of State Social Security Administrators) – Professional association of State Social Security Administrators. These state officials are authorized by state law to administer Section 218 Agreements with the Social Security Administration and responsible for all other activities associated with federal and state laws addressing social security and Medicare coverage of state and local public employers. Additional duties of individual State Administrators vary from state to state.

Non-Covered Employment – Employment not covered by social security under the Social Security Act and the Internal Revenue Code.

Nonproprietary Function – Governmental activity integral to the operation of a state or political subdivision, e.g., maintaining order or levying tax; distinguished from activity in the nature of a private or commercial venture).

Old-Age, Survivors and Disability Insurance Program (OASDI) – Program administered by the Social Security Administration, providing monthly benefits to retired and disabled workers, their spouses and children, and to survivors of insured workers.

Optional Exclusions – Categories of services that, under social security law, may be included or excluded from coverage under a Section 218 Agreement at the option of the state.

Parallel Social Security Office (PSSO) – The SSA office, usually located in the state capital, responsible for day-to-day negotiations with the states on state and local coverage issues.

Pension Plan – A plan that provides systematically for the payment of definitely determinable benefits to employees over a period of years, usually for life, after retirement. Retirement benefits are generally determined by factors such as an employee's years of service, age, and compensation.

Political Subdivision – A separate legal entity of a state that has governmental powers and functions. Examples of political subdivisions include a county, city, town, village, school district and other similar governmental entities.

Proprietary Function – Function of a governmental entity, such as a business venture for profit or in competition with private industry, or other discretionary act on behalf of citizens, that by its nature is not an integral governmental activity.

PSSO – Parallel Social Security Office.

Public Retirement System – **(**Also called a "FICA replacement plan") A plan, fund or system established by a state or political subdivision for the purpose of providing retirement benefits to employees that meets the tests under IRC section 3121(b)(7)(F) and section 31.3121(b)(7)-2(e) of the Employment Tax Regulations. A public retirement system may be a pension, annuity, retirement, or similar system. For this purpose, it is irrelevant whether a public retirement system is a "qualified plan" within the meaning of the Employees' Retirement Income Security Act of 1974 (ERISA).

Qualified Participant – An individual who is (or has been) an actual participant in a public retirement system and who has a total accrued benefit under the retirement system that meets the minimum retirement benefit requirements of IRC section 3121(b)(7) and regulations thereunder. Section 31.3121(b)(7)-2(d) of the Employment Tax Regulations establishes standards for defined contribution retirement systems. See Rev. Proc. 91-40 in the Appendix, for safe-harbor formulas for defined benefit retirement systems.

Retirement System – See Public Retirement System.

Retirement System Coverage Group – A group of employees whose positions are covered under a retirement system by referendum under the provisions of Section 218(d). The retirement system does not need to meet the tests under IRC Section 3121(b)(7)(F) and Section 31.3121(b)(7)-2(e) of the Employment Tax Regulations to secure coverage under a Section 218 Agreement.

SECA - Self Employment Contributions Act.

Section 218 Agreement – Voluntary agreement between a state and the Commissioner of Social Security (prior to March 31, 1995, the Secretary of Health and Human Services); allows states to voluntarily provide social security and Medicare or Medicare-only coverage for the services of state and local government employees. The Section 218 Agreements cover positions, not individuals; if the position is covered under the agreement, then any employee filling that position is subject to FICA taxes.

Self-Employment Contributions Act (SECA) – Federal statute imposing tax on the net earnings of self-employed individuals, to fund social security and Medicare.

Social Security Act (Act) – Federal statute providing Old-Age, Survivors and Disability Insurance (OASDI) and Hospital Insurance (Medicare), as well as other benefits.

Social Security Administration (SSA) – An independent agency in the executive branch of the federal government responsible for administering the Old-Age, Survivors and Disability (OASDI) insurance program and for determining eligibility for Medicare benefits.

Social Security Statement – Annual statement issued by SSA to workers, with information about their individual social security and Medicare earnings as reported by employers, with estimates of the different types of benefits for which they and their family may qualify.

Social Security Number (SSN) – The identification number assigned by the Social Security Administration to individuals. It must always be used in reporting an individual's earnings and in correspondence regarding specific employees. Each individual's earnings record is maintained under this number.

State – For purposes of a Section 218 Agreement, one of the fifty states, Puerto Rico, the Virgin Islands and interstate instrumentalities. The term, for this purpose, does not include the District of Columbia, Guam or American Samoa.

State Social Security Administrator (SSSA) – The principal state official authorized by state law to administer the Section 218 Agreement with the Social Security Administration, responsible for all other activities associated with applicable federal and state laws addressing social security and Medicare by state and local public employers in the state.

Taxpayer Identification Number (TIN) – The number used to identify employee (SSN) or employer (EIN) for tax reporting purposes.

Wage Base – The maximum amount of wages of each worker that is subject to the OASDI portion of social security tax in any calendar year. The social security wage base is adjusted annually. There has been no wage base limit for Medicare since 1994.

Wholly-Owned Instrumentality – An entity created by or pursuant to state statute to carry on a governmental function of a state or political subdivision. It is an independent legal entity with the power to hire, supervise, and discharge its employees and, generally, it may sue and be sued, may enter into contracts, and may hold or transfer property in its own name. Normally a wholly-owned instrumentality of a state or political subdivision does not exercise governmental powers, e.g., the police power, the taxing power and the power of eminent domain. An instrumentality can also be created by a state and a political subdivision, by more than one political subdivision, or by more than one state. See "Interstate Instrumentality."

Windfall Elimination Provision (WEP) – A social security benefit formula that may be applied to workers who receive both a social security retirement or disability benefit AND a pension based on work not covered under social security. The WEP benefit formula produces a lower social security retirement or disability insurance benefit.

Appendix

The following pages contain important documents referred to in the text. Many other related documents may be found at the web sites www.irs.gov and www.ssa.gov.

VOLUNTARY AGREEMENTS FOR COVERAGE OF STATE AND LOCAL EMPLOYEES

Purpose of Agreement

SEC. 218. *[42 U.S.C. 418]* (a)(1) The Commissioner of Social Security shall, at the request of any state, enter into an agreement with such state for the purpose of extending the insurance system established by this title to services performed by individuals as employees of such state or any political subdivision thereof. Each such agreement shall contain such provisions, not inconsistent with the provisions of this section, as the state may request.

(2) Notwithstanding section 210(a), for the purposes of this title the term "employment" includes any service included under an agreement entered into under this section.

Definitions

(b) For the purposes of this section--

(1) The term "State" does not include the District of Columbia, Guam, or American Samoa.

(2) The term "political subdivision" includes an instrumentality of (A) a State, (B) one or more political subdivisions of a State, or (C) a State and one or more of its political subdivisions.

(3) The term "employee" includes an officer of a State or political subdivision.

(4) The term "retirement system" means a pension, annuity, retirement, or similar fund or system established by a State or by a political subdivision thereof.

(5) The term "coverage group" means (A) employees of the State other than those engaged in performing service in connection with a proprietary function; (B) employees of a political subdivision of a State other than those engaged in performing service in connection with a proprietary function; (C) employees of a State engaged in performing service in connection with a single proprietary function; or (D) employees of a political subdivision of a State engaged in performing service in connection with a single proprietary function. If under the preceding sentence an employee would be included in more than one coverage group by reason of the fact that he performs service in connection with two or more proprietary functions or in connection with both a proprietary function and a nonproprietary function, he shall be included in only one such coverage group. The determination of the coverage group in which such employee shall be included shall be made in such manner as may be specified in the agreement. Persons employed under section 709 of title 32, United States Code, who elected under section 6 of the National Guard Technicians Act of 1968 to remain covered by an employee retirement system of, or plan sponsored by, a State or the Commonwealth of Puerto Rico, shall, for the purposes of this Act, be employees of the State or the Commonwealth of Puerto Rico and (notwithstanding the preceding provisions of this paragraph), shall be deemed to be a separate coverage group. For purposes of this section, individuals employed pursuant to an agreement, entered into pursuant to section 205 of the Agricultural Marketing Act of 1946 (7 U.S.C. 1624) or section 14 of the Perishable Agricultural Commodities Act, 1930 (7 U.S.C. 499n), between a State and the United States Department of Agriculture to perform services as inspectors of agricultural products may be

deemed, at the option of the State, to be employees of the State and (notwithstanding the preceding provisions of this paragraph) shall be deemed to be a separate coverage group.

Services Covered

(c)(1) An agreement under this section shall be applicable to any one or more coverage groups designated by the State.

(2) In the case of each coverage group to which the agreement applies, the agreement must include all services (other than services excluded by or pursuant to subsection (d) or paragraph (3), (5), or (6) of this subsection) performed by individuals as members of such group.

(3) Such agreement shall, if the State requests it, exclude (in the case of any coverage group) any one or more of the following:

(A) All services in any class or classes of (i) elective positions, (ii) part-time positions, or (iii) positions the compensation for which is on a fee basis;

(B) All services performed by individuals as members of a coverage group in positions covered by a retirement system on the date such agreement is made applicable to such coverage group, but only in the case of individuals who, on such date (or, if later, the date on which they first occupy such positions), are not eligible to become members of such system and whose services in such positions have not already been included under such agreement pursuant to subsection (d)(3).

(4) The Commissioner of Social Security shall, at the request of any State, modify the agreement with such State so as to (A) include any coverage group to which the agreement did not previously apply, or (B) include, in the case of any coverage group to which the agreement applies, services previously excluded from the agreement; but the agreement as so modified may not be inconsistent with the provisions of this section applicable in the case of an original agreement with a State. A modification of an agreement pursuant to clause (B) of the preceding sentence may apply to individuals to whom paragraph (3)(B) is applicable (whether or not the previous exclusion of the service of such individuals was pursuant to such paragraph), but only if such individuals are, on the effective date specified in such modification, ineligible to be members of any retirement system or if the modification with respect to such individuals is pursuant to subsection (d)(3).

(5) Such agreement shall, if the State requests it, exclude (in the case of any coverage group) any agricultural labor, or service performed by a student, designated by the State. This paragraph shall apply only with respect to service which is excluded from employment by any provision of section 210(a) other than paragraph (7) of such section and service the remuneration for which is excluded from wages by subparagraph (B) of section 209(a)(7).

(6) Such agreement shall exclude--

(A) service performed by an individual who is employed to relieve him from unemployment,

(B) service performed in a hospital, home, or other institution by a patient or inmate thereof,

(C) covered transportation service (as determined under section 210(k)),

(D) service (other than agricultural labor or service performed by a student) which is excluded from employment by any provision of section 210(a) other than paragraph (7) of such section,
(E) service performed by an individual as an employee serving on a temporary basis in case of fire, storm, snow, earthquake, flood, or other similar emergency, and
(F) service described in section 210(a)(7)(F) which is included as "employment" under section 210(a).

(7) No agreement may be made applicable (either in the original agreement or by any modification thereof) to service performed by any individual to whom paragraph (3)(B) is applicable unless such agreement provides (in the case of each coverage group involved) either that the service of any individual to whom such paragraph is applicable and who is a member of such coverage group shall continue to be covered by such agreement in case he thereafter becomes eligible to be a member of a retirement system, or that such service shall cease to be so covered when he becomes eligible to be a member of such a system (but only if the agreement is not already applicable to such system pursuant to subsection (d)(3)), whichever may be desired by the State.

(8)(A) Notwithstanding any other provision of this section, the agreement with any State entered into under this section may at the option of the State be modified at any time to exclude service performed by election officials or election workers if the remuneration paid in a calendar year for such service is less than $1,000 with respect to service performed during any calendar year commencing on or after January 1, 1995, ending on or before December 31, 1999, and the adjusted amount determined under subparagraph (B) for any calendar year commencing on or after January 1, 2000, with respect to service performed during such calendar year. Any modification of an agreement pursuant to this paragraph shall be effective with respect to services performed in and after the calendar year in which the modification is mailed or delivered by other means to the Commissioner of Social Security.

(B) For each year after 1999, the Commissioner of Social Security shall adjust the amount referred to in subparagraph (A) at the same time and in the same manner as is provided under section 215(a)(1)(B)(ii) with respect to the amounts referred to in section 215(a)(1)(B)(i), except that--

(i) for purposes of this subparagraph, 1997 shall be substituted for the calendar year referred to in section 215(a)(1)(B)(ii)(II), and
(ii) such amount as so adjusted, if not a multiple of $100, shall be rounded to the next higher multiple of $100 where such amount is a multiple of $50 and to the nearest multiple of $100 in any other case.

The Commissioner of Social Security shall determine and publish in the Federal Register each adjusted amount determined under this subparagraph not later than November 1 preceding the year for which the adjustment is made.

Positions Covered By Retirement Systems

(d)(1) No agreement with any State may be made applicable (either in the original agreement or by any modification thereof) to any service performed by employees as members of any coverage group in positions covered by a retirement system either (A) on the date such agreement is made applicable to such coverage group, or (B) on the date of enactment of the succeeding paragraph of this subsection (except in the case of positions

which are, by reason of action by such State or political subdivision thereof, as may be appropriate, taken prior to the date of enactment of such succeeding paragraph, no longer covered by a retirement system on the date referred to in clause (A), and except in the case of positions excluded by paragraph (5)(A)). The preceding sentence shall not be applicable to any service performed by an employee as a member of any coverage group in a position (other than a position excluded by paragraph (5)(A)) covered by a retirement system on the date an agreement is made applicable to such coverage group if, on such date (or, if later, the date on which such individual first occupies such position), such individual is ineligible to be a member of such system.

(2) It is hereby declared to be the policy of the Congress in enacting the succeeding paragraphs of this subsection that the protection afforded employees in positions covered by a retirement system on the date an agreement under this section is made applicable to service performed in such positions, or receiving periodic benefits under such retirement system at such time, will not be impaired as a result of making the agreement so applicable or as a result of legislative enactment in anticipation thereof.

(3) Notwithstanding paragraph (1), an agreement with a State may be made applicable (either in the original agreement or by any modification thereof) to service performed by employees in positions covered by a retirement system (including positions specified in paragraph (4) but not including positions excluded by or pursuant to paragraph (5)), if the governor of the State, or an official of the State designated by him for the purpose, certifies to the Commissioner of Social Security that the following conditions have been met:

(A) A referendum by secret written ballot was held on the question of whether service in positions covered by such retirement system should be excluded from or included under an agreement under this section;

(B) An opportunity to vote in such referendum was given (and was limited) to eligible employees;

(C) Not less than ninety days' notice of such referendum was given to all such employees;

(D) Such referendum was conducted under the supervision of the governor or an agency or individual designated by him; and

(E) A majority of the eligible employees voted in favor of including service in such positions under an agreement under this section.

An employee shall be deemed an "eligible employee" for purposes of any referendum with respect to any retirement system if, at the time such referendum was held, he was in a position covered by such retirement system and was a member of such system, and if he was in such a position at the time notice of such referendum was given as required by clause (C) of the preceding sentence; except that he shall not be deemed an "eligible employee" if, at the time the referendum was held, he was in a position to which the State agreement already applied, or if he was in a position excluded by or pursuant to paragraph (5). No referendum with respect to a retirement system shall be valid for purposes of this paragraph unless held within the two-year period which ends on the date of execution of the agreement or modification which extends the insurance system established by this title to such retirement system, nor shall any referendum with respect to a retirement system be valid for purposes of this paragraph if held less than one year after the last previous referendum held with respect to such retirement system.

(4) For the purposes of subsection (c) of this section, the following employees shall be deemed to be a separate coverage group--

(A) all employees in positions which were covered by the same retirement system on the date the agreement was made applicable to such system (other than employees to whose services the agreement already applied on such date);

(B) all employees in positions which became covered by such system at any time after such date; and

(C) all employees in positions which were covered by such system at any time before such date and to whose services the insurance system established by this title has not been extended before such date because the positions were covered by such retirement system (including employees to whose services the agreement was not applicable on such date because such services were excluded pursuant to subsection (c)(3)(B)).

(5)(A) Nothing in paragraph (3) of this subsection shall authorize the extension of the insurance system established by this title to service in any policeman's or fireman's position.

(B) At the request of the State, any class or classes of positions covered by a retirement system which may be excluded from the agreement pursuant to paragraph (3) or (5) of subsection (c), and to which the agreement does not already apply, may be excluded from the agreement at the time it is made applicable to such retirement system; except that, notwithstanding the provisions of paragraph (3)(B) of such subsection, such exclusion may not include any services to which such paragraph (3)(B) is applicable. In the case of any such exclusion, each such class so excluded shall, for purposes of this subsection, constitute a separate retirement system in case of any modification of the agreement thereafter agreed to.

(6)(A) If a retirement system covers positions of employees of the State and positions of employees of one or more political subdivisions of the State, or covers positions of employees of two or more political subdivisions of the State, then, for purposes of the preceding paragraphs of this subsection, there shall, if the State so desires, be deemed to be a separate retirement system with respect to any one or more of the political subdivisions concerned and, where the retirement system covers positions of employees of the State, a separate retirement system with respect to the State or with respect to the State and any one or more of the political subdivisions concerned. Where a retirement system covering positions of employees of a State and positions of employees of one or more political subdivisions of the State, or covering positions of employees of two or more political subdivisions of the State, is not divided into separate retirement systems pursuant to the preceding sentence or pursuant to subparagraph (C), then the State may, for purposes of subsection (e) only, deem the system to be a separate retirement system with respect to any one or more of the political subdivisions concerned and, where the retirement system covers positions of employees of the State, a separate retirement system with respect to the State or with respect to the State and any one or more of the political subdivisions concerned.

(B) If a retirement system covers positions of employees of one or more institutions of higher learning, then, for purposes of such preceding paragraphs there shall, if the State so desires, be deemed to be a separate retirement system for the employees of each such institution of higher learning. For the purposes of this subparagraph, the term "institutions

of higher learning" includes junior colleges and teachers colleges. If a retirement system covers positions of employees of a hospital, which is an integral part of a political subdivision, then, for purposes of the preceding paragraphs there shall, if the State so desires, be deemed to be a separate retirement system for the employees of such hospital.
(C) For the purposes of this subsection, any retirement system established by the State of Alaska, California, Connecticut, Florida, Georgia, Illinois, Massachusetts, Minnesota, Nevada, New Jersey, New Mexico, New York, North Dakota, Pennsylvania, Rhode Island, Tennessee, Texas, Vermont, Washington, Wisconsin, or Hawaii, or any political subdivision of any such State, which, on, before, or after the date of enactment of this subparagraph, is divided into two divisions or parts, one of which is composed of positions of members of such system who desire coverage under an agreement under this section and the other of which is composed of positions of members of such system who do not desire such coverage, shall, if the State so desires and if it is provided that there shall be included in such division or part composed of members desiring such coverage the positions of individuals who become members of such system after such coverage is extended, be deemed to be a separate retirement system with respect to each such division or part. If, in the case of a separate retirement system which is deemed to exist by reason of subparagraph (A) and which has been divided into two divisions or parts pursuant to the first sentence of this subparagraph, individuals become members of such system by reason of action taken by a political subdivision after coverage under an agreement under this section has been extended to the division or part thereof composed of positions of individuals who desire such coverage, the positions of such individuals who become members of such retirement system by reason of the action so taken shall be included in the division or part of such system composed of positions of members who do not desire such coverage if (i) such individuals, on the day before becoming such members, were in the division or part of another separate retirement system (deemed to exist by reason of subparagraph (A)) composed of positions of members of such system who do not desire coverage under an agreement under this section, and (ii) all of the positions in the separate retirement system of which such individuals so become members and all of the positions in the separate retirement system referred to in clause (i) would have been covered by a single retirement system if the State had not taken action to provide for separate retirement systems under this paragraph.
(D)(i) The position of any individual which is covered by any retirement system to which subparagraph (C) is applicable shall, if such individual is ineligible to become a member of such system on August 1, 1956, or, if later, the day he first occupies such position, be deemed to be covered by the separate retirement system consisting of the positions of members of the division or part who do not desire coverage under the insurance system established under this title.
(ii) Notwithstanding clause (i), the State may, pursuant to subsection (c)(4)(B) and subject to the conditions of continuation or termination of coverage provided for in subsection (c)(7), modify its agreement under this section to include services performed by all individuals described in clause (i) other than those individuals to whose services the agreement already applies. Such individuals shall be deemed (on and after the effective date of the modification) to be in positions covered by the separate retirement system consisting of the positions of members of the division or part who desire coverage under the insurance system established under this title.

(E) An individual who is in a position covered by a retirement system to which subparagraph (C) is applicable and who is not a member of such system but is eligible to become a member thereof shall, for purposes of this subsection (other than paragraph (8)), be regarded as a member of such system; except that, in the case of any retirement system a division or part of which is covered under the agreement (either in the original agreement or by a modification thereof), which coverage is agreed to prior to 1960, the preceding provisions of this subparagraph shall apply only if the State so requests and any such individual referred to in such preceding provisions shall, if the State so requests, be treated, after division of the retirement system pursuant to such subparagraph (C), the same as individuals in positions referred to in subparagraph (F).

(F) In the case of any retirement system divided pursuant to subparagraph (C), the position of any member of the division or part composed of positions of members who do not desire coverage may be transferred to the separate retirement system composed of positions of members who desire such coverage if it is so provided in a modification of such agreement which is mailed, or delivered by other means, to the Commissioner of Social Security prior to 1970 or, if later, the expiration of two years after the date on which such agreement, or the modification thereof making the agreement applicable to such separate retirement system, as the case may be, is agreed to, but only if, prior to such modification or such later modification, as the case may be, the individual occupying such position files with the State a written request for such transfer. Notwithstanding subsection (e)(1), any such modification or later modification, providing for the transfer of additional positions within a retirement system previously divided pursuant to subparagraph (C) to the separate retirement system composed of positions of members who desire coverage, shall be effective with respect to services performed after the same effective date as that which was specified in the case of such previous division.

(G) For the purposes of this subsection, in the case of any retirement system of the State of Florida, Georgia, Minnesota, North Dakota, Pennsylvania, Washington, or Hawaii which covers positions of employees of such State who are compensated in whole or in part from grants made to such State under title III, there shall be deemed to be, if such State so desires, a separate retirement system with respect to any of the following:

(i) the positions of such employees;

(ii) the positions of all employees of such State covered by such retirement system who are employed in the department of such State in which the employees referred to in clause (i) are employed; or

(iii) employees of such State covered by such retirement system who are employed in such department of such State in positions other than those referred to in clause (i).

(7) The certification by the governor (or an official of the State designated by him for the purpose) required under paragraph (3) shall be deemed to have been made, in the case of a division or part (created under subparagraph (C) of paragraph (6) or the corresponding provision of prior law) consisting of the positions of members of a retirement system who desire coverage under the agreement under this section, if the governor (or the official so designated) certifies to the Commissioner of Social Security that--

(A) an opportunity to vote by written ballot on the question of whether they wish to be covered under an agreement under this section was given to all individuals who were members of such system at the time the vote was held;

(B) not less than ninety days' notice of such vote was given to all individuals who were members of such system on the date the notice was issued;
(C) the vote was conducted under the supervision of the governor or an agency or individual designated by him; and
(D) such system was divided into two parts or divisions in accordance with the provisions of subparagraphs (C) and (D) of paragraph (6) or the corresponding provision of prior law.

For purposes of this paragraph, an individual in a position to which the State agreement already applied or in a position excluded by or pursuant to paragraph (5) shall not be considered a member of the retirement system.

(8)(A) Notwithstanding paragraph (1), if under the provisions of this subsection an agreement is, after December 31, 1958, made applicable to service performed in positions covered by a retirement system, service performed by an individual in a position covered by such a system may not be excluded from the agreement because such position is also covered under another retirement system.

(B) Subparagraph (A) shall not apply to service performed by an individual in a position covered under a retirement system if such individual, on the day the agreement is made applicable to service performed in positions covered by such retirement system, is not a member of such system and is a member of another system.

(C) If an agreement is made applicable, prior to 1959, to service in positions covered by any retirement system, the preceding provisions of this paragraph shall be applicable in the case of such system if the agreement is modified to so provide.

(D) Except in the case of State agreements modified as provided in subsection (l) and agreements with interstate instrumentalities, nothing in this paragraph shall authorize the application of an agreement to service in any policeman's or fireman's position.

Effective Date of Agreement

(e)(1) Any agreement or modification of an agreement under this section shall be effective with respect to services performed after an effective date specified in such agreement or modification; except that such date may not be earlier than the last day of the sixth calendar year preceding the year in which such agreement or modification, as the case may be, is mailed or delivered by other means to the Commissioner of Social Security.

(2) In the case of service performed by members of any coverage group--
(A) to which an agreement under this section is made applicable, and
(B) with respect to which the agreement, or modification thereof making the agreement so applicable, specifies an effective date earlier than the date of execution of such agreement and such modification, respectively,

the agreement shall, if so requested by the State, be applicable to such services (to the extent the agreement was not already applicable) performed before such date of execution and after such effective date by any individual as a member of such coverage group if he is such a member on a date, specified by the State, which is earlier than such date of execution, except that in no case may the date so specified be earlier than the date such agreement or such modification, as the case may be, is mailed, or delivered by other means, to the Commissioner of Social Security.

(3) Notwithstanding the provisions of paragraph (2) of this subsection, in the case of services performed by individuals as members of any coverage group to which an

agreement under this section is made applicable, and with respect to which there were timely paid in good faith to the Secretary of the Treasury amounts equivalent to the sum of the taxes which would have been imposed by sections 3101 and 3111 of the Internal Revenue Code of 1986 had such services constituted employment for purposes of chapter 21 of such Code at the time they were performed, and with respect to which refunds were not obtained, such individuals may, if so requested by the State, be deemed to be members of such coverage group on the date designated pursuant to paragraph (2).

Duration of Agreement

(f) No agreement under this section may be terminated, either in its entirety or with respect to any coverage group, on or after the date of the enactment of the Social Security Amendments of 1983.

Instrumentalities of Two or More States

(g)(1) The Commissioner of Social Security may, at the request of any instrumentality of two or more States, enter into an agreement with such instrumentality for the purpose of extending the insurance system established by this title to services performed by individuals as employees of such instrumentality. Such agreement, to the extent practicable, shall be governed by the provisions of this section applicable in the case of an agreement with a State.

(2) In the case of any instrumentality of two or more States, if--

(A) employees of such instrumentality are in positions covered by a retirement system of such instrumentality or of any of such States or any of the political subdivisions thereof, and

(B) such retirement system is (on, before, or after the date of enactment of this paragraph) divided into two divisions or parts, one of which is composed of positions of members of such system who are employees of such instrumentality and who desire coverage under an agreement under this section and the other of which is composed of positions of members of such system who are employees of such instrumentality and who do not desire such coverage, and

(C) it is provided that there shall be included in such division or part composed of the positions of members desiring such coverage the positions of employees of such instrumentality who become members of such system after such coverage is extended,

then such retirement system shall, if such instrumentality so desires, be deemed to be a separate retirement system with respect to each such division or part. An individual who is in a position covered by a retirement system divided pursuant to the preceding sentence and who is not a member of such system but is eligible to become a member thereof shall, for purposes of this subsection, be regarded as a member of such system. Coverage under the agreement of any such individual shall be provided under the same conditions, to the extent practicable, as are applicable in the case of the States to which the provisions of subsection (d)(6)(C) apply. The position of any employee of any such instrumentality which is covered by any retirement system to which the first sentence of this paragraph is applicable shall, if such individual is ineligible to become a member of such system on the date of enactment of this paragraph or, if later, the day he first occupies such position, be deemed to be covered by the separate retirement system consisting of the positions of members of the division or part who do not desire coverage

under the insurance system established under this title. Services in positions covered by a separate retirement system created pursuant to this subsection (and consisting of the positions of members who desire coverage under an agreement under this section) shall be covered under such agreement on compliance, to the extent practicable, with the same conditions as are applicable to coverage under an agreement under this section of services in positions covered by a separate retirement system created pursuant to subparagraph (C) of subsection (d)(6) or the corresponding provision of prior law (and consisting of the positions of members who desire coverage under such agreement).

(3) Any agreement with any instrumentality of two or more States entered into pursuant to this Act may, notwithstanding the provisions of subsection (d)(5)(A) and the references thereto in subsections (d)(1) and (d)(3), apply to service performed by employees of such instrumentality in any policeman's or fireman's position covered by a retirement system, but only upon compliance, to the extent practicable, with the requirements of subsection (d)(3). For the purpose of the preceding sentence, a retirement system, which covers positions of policemen or firemen or both, and other positions, shall, if the instrumentality concerned so desires, be deemed to be a separate retirement system with respect to the positions of such policemen or firemen, or both, as the case may be.

Delegation of Functions

(h) The Commissioner of Social Security is authorized, pursuant to agreement with the head of any federal agency, to delegate any of the Commissioner's functions under this section to any officer or employee of such agency and otherwise to utilize the services and facilities of such agency in carrying out such functions, and payment therefore shall be in advance or by way of reimbursement, as may be provided in such agreement.

Wisconsin Retirement Fund

(i)(1) Notwithstanding paragraph (1) of subsection (d), the agreement with the State of Wisconsin may, subject to the provisions of this subsection, be modified so as to apply to service performed by employees in positions covered by the Wisconsin retirement fund or any successor system.

(2) All employees in positions covered by the Wisconsin retirement fund at any time on or after January 1, 1951, shall, for the purposes of subsection (c) only, be deemed to be a separate coverage group; except that there shall be excluded from such separate coverage group all employees in positions to which the agreement applies without regard to this subsection.

(3) The modification pursuant to this subsection shall exclude (in the case of employees in the coverage group established by paragraph (2) of this subsection) service performed by any individual during any period before he is included under the Wisconsin retirement fund.

(4) The modification pursuant to this subsection shall, if the State of Wisconsin requests it, exclude (in the case of employees in the coverage group established by paragraph (2) of this subsection) all service performed in policemen's positions, all service performed in firemen's positions, or both.

Certain Positions No Longer Covered By Retirement Systems

(j) Notwithstanding subsection (d), an agreement with any State entered into under this section prior to the date of the enactment of this subsection may, prior to January 1, 1958,

be modified pursuant to subsection (c)(4) so as to apply to services performed by employees, as members of any coverage group to which such agreement already applies (and to which such agreement applied on such date of enactment), in positions (1) to which such agreement does not already apply, (2) which were covered by a retirement system on the date such agreement was made applicable to such coverage group, and (3) which, by reason of action by such State or political subdivision thereof, as may be appropriate, taken prior to the date of the enactment of this subsection, are no longer covered by a retirement system on the date such agreement is made applicable to such services.

Certain Employees of the State of Utah

(k) Notwithstanding the provisions of subsection (d), the agreement with the State of Utah entered into pursuant to this section may be modified pursuant to subsection (c)(4) so as to apply to services performed for any of the following, the employees performing services for each of which shall constitute a separate coverage group: Weber Junior College, Carbon Junior College, Dixie Junior College, Central Utah Vocational School, Salt Lake Area Vocational School, Center for the Adult Blind, Union High School (Roosevelt, Utah), Utah High School Activities Association, State Industrial School, State Training School, State Board of Education, and Utah School Employees Retirement Board. Any modification agreed to prior to January 1, 1955, may be made effective with respect to services performed by employees as members of any of such coverage groups after an effective date specified therein, except that in no case may any such date be earlier than December 31, 1950. Coverage provided for in this subsection shall not be affected by a subsequent change in the name of a group.

Policemen and Firemen in Certain States

(l) Any agreement with a State entered into pursuant to this section may, notwithstanding the provisions of subsection (d)(5)(A) and the references thereto in subsections (d)(1) and (d)(3), be modified pursuant to subsection (c)(4) to apply to service performed by employees of such State or any political subdivision thereof in any policeman's or fireman's position covered by a retirement system in effect on or after the date of the enactment of this subsection, but only upon compliance with the requirements of subsection (d)(3). For the purposes of the preceding sentence, a retirement system which covers positions of policemen or firemen, or both, and other positions shall, if the State concerned so desires, be deemed to be a separate retirement system with respect to the positions of such policemen or firemen, or both, as the case may be.

Positions Compensated Solely on a Fee Basis

(m)(1) Notwithstanding any other provision in this section, an agreement entered into under this section may be made applicable to service performed after 1967 in any class or classes of positions compensated solely on a fee basis to which such agreement did not apply prior to 1968 only if the State specifically requests that its agreement be made applicable to such service in such class or classes of positions.
(2) Notwithstanding any other provision in this section, an agreement entered into under this section may be modified, at the option of the State, at any time after 1967, so as to exclude services performed in any class or classes of positions compensation for which is solely on a fee basis.

(3) Any modification made under this subsection shall be effective with respect to services performed after the last day of the calendar year in which the modification is mailed or delivered by other means to the Commissioner of Social Security.
(4) If any class or classes of positions have been excluded from coverage under the State agreement by a modification agreed to under this subsection, the Commissioner of Social Security and the State may not thereafter modify such agreement so as to again make the agreement applicable with respect to such class or classes of positions.
(n)(1) The Commissioner of Social Security shall, at the request of any State, enter into or modify an agreement with such State under this section for the purpose of extending the provisions of title XVIII, and sections 226 and 226A, to services performed by employees of such State or any political subdivision thereof who are described in paragraph (2).
(2) This subsection shall apply only with respect to employees--

(A) whose services are not treated as employment as that term applies under section 210(p) by reason of paragraph (3) of such section; and

(B) who are not otherwise covered under the State's agreement under this section.

(3) For purposes of sections 226 and 226A of this Act, services covered under an agreement pursuant to this subsection shall be treated as "medicare qualified government employment".
(4) Except as otherwise provided in this subsection, the provisions of this section shall apply with respect to services covered under the agreement pursuant to this subsection.

Amended Section 530 of the Revenue Act of 1978

(a) Termination of Certain Employment Tax Liability.

(1) In general.

- If -

(A) for purposes of employment taxes, the taxpayer did not treat an individual as an employee for any period, and

(B) in the case of periods after December 31, 1978, all federal tax returns (including information returns) required to be filed by the taxpayer with respect to such individual for such period are filed on a basis consistent with the taxpayer's treatment of such individual as not being an employee,

then, for purposes of applying such taxes for such period with respect to the taxpayer, the individual shall be deemed not to be an employee unless the taxpayer had no reasonable basis for not treating such individual as an employee.

(2) Statutory standards providing one method of satisfying the requirements of paragraph (1).

- For purposes of paragraph (1), a taxpayer shall in any case be treated as having a reasonable basis for not treating an individual as an employee for a period if the taxpayer's treatment of such individual for such period was in reasonable reliance on any of the following:

(A) judicial precedent, published rulings, technical advice with respect to the taxpayer, or a letter ruling to the taxpayer;

(B) a past Internal Revenue Service audit of the taxpayer in which there was no assessment attributable to the treatment (for employment tax purposes) of the individuals holding positions substantially similar to the position held by this individual; or

(C) long-standing recognized practice of a significant segment of the industry in which such individual was engaged.

(3) Consistency required in the case of prior tax treatment.

- Paragraph (1) shall not apply with respect to the treatment of any individual for employment tax purposes for any period ending after December 31, 1978, if the taxpayer (or a predecessor) has treated any individual holding a substantially similar position as an employee for purposes of the employment taxes for any period beginning after December 31, 1977.

(4) Refund or credit of overpayment.

- If refund or credit of any overpayment of an employment tax resulting from the application of paragraph (1) is not barred on the date of the enactment of this Act (Nov. 6, 1978) by any law or rule of law, the period for filing a claim for refund or credit of such overpayment (to the extent attributable to the application of paragraph (1)) shall not expire before the date 1 year after the date of the enactment of this Act (Nov. 6, 1978).

(b) Prohibition Against Regulations and Rulings on Employment Status.

- No regulation or Revenue Ruling shall be published on or after the date of the enactment of this Act (Nov. 6, 1978) and before the effective date of any law hereafter enacted clarifying the employment status of individuals for purposes of the employment taxes by the Department of the Treasury (including the Internal Revenue Service) with respect to the employment status of any individual for purposes of the employment taxes.

(c) Definitions.

- For purposes of this section -

(1) Employment tax. - The term 'employment tax' means any tax imposed by subtitle C of the Internal Revenue Code of 1986 (formerly I.R.C. 1954, section 3101 et seq. of this title).

(2) Employment status. - The term 'employment status' means the status of an individual, under the usual common law rules applicable in determining the employer-employee

relationship, as an employee or as an independent contractor (or other individual who is not an employee).

(d) Exception.

- This section shall not apply in the case of an individual who, pursuant to an arrangement between the taxpayer and another person, provides services for such other person as an engineer, designer, drafter, computer programmer, systems analyst, or other similarly skilled worker engaged in a similar line of work.

(e) Special Rules For Application of Section.

(1) NOTICE OF AVAILABILITY OF SECTION

- An officer or employee of the Internal Revenue Service shall, before or at the commencement of any audit inquiry relating to the employment status of one or more individuals who perform services for the taxpayer, provide the taxpayer with a written notice of the provisions of this section.

(2) RULES RELATING TO STATUTORY STANDARDS

- For purposes of subsection (a)(2) -

(A) a taxpayer may not rely on an audit commenced after December 31, 1996, for purposes of subparagraph (B) thereof unless such audit included an examination for employment tax purposes of whether the individual involved (or any individual holding a position substantially similar to the position held by the individual involved) should be treated as an employee of the taxpayer,

(B) in no event shall the significant segment requirement of subparagraph (C) thereof be construed to require a reasonable showing of the practice of more than 25 percent of the industry (determined by not taking into account the taxpayer), and

(C) in applying the long-standing recognized practice requirement of subparagraph (C) thereof-

(i) such requirement shall not be construed as requiring the practice to have continued for more than 10 years, and

(ii) a practice shall not fail to be treated as long-standing merely because such practice began after 1978.

(3) AVAILABILITY OF SAFE HARBORS

- Nothing in this section shall be construed to provide that subsection (a) only applies where the individual involved is otherwise an employee of the taxpayer.

(4) BURDEN OF PROOF-

(A) IN GENERAL

- If-

(i) a taxpayer establishes a prima facie case that it was reasonable not to treat an individual as an employee for purposes of this section, and

(ii) the taxpayer has fully cooperated with reasonable requests from the Secretary of the Treasury or his delegate,

then the burden of proof with respect to such treatment shall be on the Secretary.

(B) EXCEPTION FOR OTHER REASONABLE BASIS

- In the case of any issue involving whether the taxpayer had a reasonable basis not to treat an individual as an employee for purposes of this section, subparagraph (A) shall only apply for purposes of determining whether the taxpayer meets the requirements

of subparagraph (A), (B), or (C) of subsection (a)(2).

(5) PRESERVATION OF PRIOR PERIOD SAFE HARBOR

- If -

(A) an individual would (but for the treatment referred to in subparagraph (B)) be deemed not to be an employee of the taxpayer under subsection (a) for any prior period, and

(B) such individual is treated by the taxpayer as an employee for employment tax purposes for any subsequent period,

then, for purposes of applying such taxes for such prior period with respect to the taxpayer, the individual shall be deemed not to be an employee.

(6) SUBSTANTIALLY SIMILAR POSITION

- For purposes of this section, the determination as to whether an individual holds a position substantially similar to a position held by another individual shall include consideration of the relationship between the taxpayer and such individuals.

Revenue Procedure 85-18

SECTION 1. PURPOSE

The purpose of this revenue procedure is to amplify and supersede Rev. Proc. 81-43, 1981-2 C.B. 616, which provides instructions for implementing the provisions of section 530 of the Revenue Act of 1978, 1978-3 (Vol. 1) C.B. xi, 119 (the Act), relating to the employment tax status of independent contractors and employees.

SEC. 2. BACKGROUND

.01 Rev. Proc. 81-43 is superseded to reflect changes made to section 530 of the Act by section 269(c) of the Tax Equity and Fiscal Responsibility Act of 1982, 1982-2 C.B. 462, 536, which extends the provisions of section 530 indefinitely.

Section 530(a)(1) of the Act, as amended, provides that if, for purposes of the employment taxes under subtitle C of the Internal Revenue Code, a taxpayer did not treat an individual as an employee for any period, then the individual will be deemed not to be an employee for that period, unless the taxpayer had no reasonable basis for not treating the individual as an employee. For any period after December 31, 1978, the relief applies only if (1) all federal tax returns (including information returns) required to be filed by the taxpayer with respect to the individual for the period are filed on a basis consistent with the taxpayer's treatment of the individual as not being an employee, and (2) the treatment is consistent with the treatment for periods beginning after December 31, 1977.

.02 A new section 3.02 titled "Filing of Returns" has been added stating that relief under section 530(a)(1) of the Act will not be granted if a Form 1099 has not been timely filed for each worker for any period after December 31, 1978.

.03 Section 3.05 (relating to refunds, credits, and abatements) is clarified to state that it does not apply to periods in which a taxpayer "treated" an individual as an employee.

SEC. 3. APPLICATION

.01 "Safe Haven" Rules

There are several alternative standards that constitute "safe havens" in determining whether a taxpayer has a "reasonable basis" for not treating an individual as an employee. Reasonable reliance on any one of the following "safe havens" is sufficient:

(A) judicial precedent or published rulings, whether or not relating to the particular industry or business in which the taxpayer is engaged, or technical advice, a letter ruling, or a determination letter pertaining to the taxpayer; or

(B) a past Internal Revenue Service audit (not necessarily for employment tax purposes) of the taxpayer, if the audit entailed to assessment attributable to the taxpayer's employment tax treatment of individuals holding positions substantially similar to the position held by the individual whose status is at issue (a taxpayer does not meet this test if, in the conduct of a prior audit, an assessment attributable to the taxpayer's treatment of the individual was offset by other claims asserted by the taxpayer); or

(C) long-standing recognized practice of a significant segment of the industry in which the individual was engaged (the practice need not be uniform throughout an entire industry).

A taxpayer who fails to meet any of the three "safe havens" may nevertheless be entitled to relief if the taxpayer can demonstrate, in some other manner, a reasonable basis for not treating the individual as an employee. In H.R. Rep. No. 95-1748, 95th

Cong., 2d Sess. 5 (1978), 1978-3 (Vol. 1) C.B. 629, 633, it is indicated that "reasonable basis" should be construed liberally in favor of the taxpayer.

.02 Filing of Returns.

For any period after December 31, 1978, the relief under section 530(a)(1) will not apply, even if the taxpayer has met the "safe haven" rules of paragraph 3.01 of this revenue procedure, if the appropriate Form 1099 has not been timely filed with respect to the workers involved. See Rev. Rul. 81-224, 1981-2 C.B. 197.

.03 Interpreting the Word "Treat"

In determining whether a taxpayer did not "treat" an individual as an employee for any period within the meaning of section 530(a)(1) of the Act, the following guidelines should be followed:

(A) The withholding of income tax or the Federal Insurance Contributions Act (FICA) tax from an individual's wages is "treatment" of the individual as an employee, whether or not the tax is paid over to the Government.

(B) Except as provided in paragraph (C) and (E) below, the filing of an employment tax return (including Forms 940 (*Employer's Annual Federal Unemployment Tax Return*), 941 (*Employer's Quarterly Federal Tax Return*), 942 (*Employer's Quarterly Tax Return for Household Employees*), 943 (*Employer's Annual Tax Return for Agricultural Employees*), and W-2 (*Wage and Tax Statement*)) for a period with respect to an individual, whether or not tax was withheld from the individual, is "treatment" of the individual as an employee for that period.

(C) The filing of a delinquent or amended employment tax return for a particular tax period with respect to an individual as a result of Service compliance procedures is not "treatment" of the individual as an employee for that period. For this purpose, Collection or Examination activities constitute compliance procedures. For example, if the Service determines as a result of an audit that a taxpayer's workers are common law employees, that determination is not "treatment" of the workers as employees for the period under audit. However, if the taxpayer withholds employment taxes or files employment tax returns with respect to those workers for the periods following the period under audit, the action is "treatment" of the workers as employees for those later periods.

(D) Internal Revenue Service Center notices that merely advise the taxpayer that no return has been filed and request information from the taxpayer are not compliance procedures.

(E) A return prepared by the Service under section 6020(b) of the Code is not "treatment" of an individual as an employee; nor is the signing of an audit Form 2504 (Agreement to Assessment and Collection of Additional Tax and Acceptance of Overassessment).

.04 Consistency in prior periods

The relief under section 530(a)(1) of the Act, as amended, does not apply to the employment tax treatment of any individual for any period ending after December 31, 1978, if the taxpayer (or a predecessor) treated any individual holding a substantially similar position as an employee for employment tax purposes for any period beginning after December 31, 1977. However, relief will not be denied under the consistency provision for any periods prior to the period in which the individuals were treated as employees. For example, a taxpayer did not treat an individual as an employee in 1978 and 1979. In 1980, the taxpayer began treating individuals holding substantially similar

positions as employees. This subsequent treatment does not prevent the taxpayer from receiving relief under section 530(a)(1) for 1978 and 1979. The application of the consistency rule prevents taxpayers from changing the way they treat workers solely to take advantage of the relief provisions. The application of this provision to predecessors is intended to prevent evasion of this rule, for example, by reincorporations.

.05 Refunds, Credits, and Abatements

Relief under section 530(a)(1) of the Act is available to taxpayers who are under audit by the Service or who are involved in administrative (including Appellate) or judicial processes with respect to assessments based on employment status reclassifications. Relief also is extended to any claim for a refund or credit of any overpayment of an employment tax resulting from the termination of liability under section 530(a)(1), provided the claim is not barred on the date of enactment of this provision (November 6, 1978) by any law or rule of law.

Taxpayers who have entered into final closing agreements under section 7121 of the Code or compromises under section 7122 with respect to employment status controversies are ineligible for relief under the Act, unless they have not completely paid their liability. Thus, for example, a taxpayer who has agreed to or compromised a liability for an amount which is to be paid in installments, but who still has one or more installments to pay, is relieved of liability for such outstanding installments. Taxpayers who settled employment status controversies administratively with the Service on any basis other than section 7121 or 7122 of the Code or who unsuccessfully litigated such cases also are eligible for relief, provided their claims are not barred by the statute of limitations or by the application of the doctrine of *res judicata*. However, unpaid judgments will be abated if section 530(a)(1) of the Act applies. Thus, an unsuccessful litigant in an employment status case who fulfills the Act's requirements can avoid collection of any unpaid employment tax liabilities, regardless of the doctrine of *res judicata.*

The application of the doctrine of *res judicata* will prevent a refund based on section 530(a)(1) of the Act if a taxpayer paid a judgment in an action relating to the same issue as to the same taxpayer. Thus, if the specific matter was judicially decided and the judgment paid, relief under section 530(a)(1) is not available.

This subsection will not apply to those periods in which a taxpayer "treated" an individual as an employee within the meaning of subsection .03 of this section.

.06 Handling of Claims

Relief under section 530(a)(1) of the Act applies to the taxes imposed on an employer by sections 3111 or 3301 of the Code. It also applies to an employer's liability under section 3102 and 3403 to withhold and pay the taxes imposed by sections 3101 and 3402. Therefore, an unpaid assessment of those taxes against an employer who qualifies for relief under section 530(a)(1) of the Act should be abated. Timely claims for refund of such taxes paid by a taxpayer who qualifies for relief will be honored.

.07 Interest and Penalties

If a taxpayer is relieved of liability under section 530(a)(1) of the Act, any liability for interest or penalties attributable to that liability is forgiven automatically. This relief from interest and penalties applies whether charged directly against the taxpayer or personally against a corporate taxpayer's officers.

.08 Status of Workers

Section 530 of the Act does not change in any way the status, liabilities, and rights of the worker whose status is at issue. Section 530(a)(1) terminates the liability of the employer for the employment taxes but has no effect on the workers. It does not convert individuals from the status of employee to the status of self-employed.

Section 31.3102-1(c) of the regulations provides, with respect to the collection and payment of the employee's share of the FICA tax, that "until collected from him [by [*10] the employer] the employee is also liable for the employee tax with respect to all wages received by him." Therefore, if an employer's liability under section 3102 of the Code for the employee's share of the tax imposed by section 3101 is terminated under section 530(a)(1) of the Act, the employee remains liable for that tax. Employees who incorrectly paid the self-employment tax (section 1401 of the Code) may file a claim for refund; however, the amount of the self-employment tax refund will be offset by the amount of the employee's share of the tax imposed on the employee as a result of the application of section 31.3102-1(c) of the regulations.

.09 Definition of Employee

For purposes of section 530(a) of the Act, the term employee means employees under sections 3121(d), 3306(i), and 3401(c) of the Code.

SEC. 4.EFFECT ON OTHER DOCUMENTS

Rev. Proc. 81-43 is amplified and superseded.

Internal Revenue Service
Revenue Ruling 86-88

FICA; HOSPITAL INSURANCE; EXTENSION TO STATE AND POLITICAL SUBDIVISION EMPLOYEES

This revenue ruling provides guidelines concerning the applicability of the Medicare tax to employees of states and political subdivisions.

For purposes of this revenue ruling, the term 'state' includes the Commonwealth of Puerto Rico, the Virgin Islands, and the District of Columbia.

For purposes of this revenue ruling, the term 'political subdivision' has the same meaning that it has under section 218(b)(2) of the Social Security Act, 42 U.S.C. section 418(b)(2). Thus, 'political subdivision' ordinarily includes a county, city, town, village, or school district. In many states, depending upon the manner in which such entities are created under state law, 'political subdivision' includes a sanitation, utility, reclamation, improvement, drainage, irrigation, flood control, or similar district.

For purposes of this revenue ruling, the term 'state employer' of a state includes the state and any agency or instrumentality of that state that is a separate employer for purposes of withholding, paying, and reporting the federal income taxes of employees. The term 'political subdivision employer' of a political subdivision includes the political subdivision and any agency or instrumentality of that political subdivision that is a separate employer for purposes of withholding, reporting, and paying the federal income taxes of employees.

SERVICES SUBJECT TO THE MEDICARE TAX

Q1. What services are subject to the Medicare tax under the Act?

A1. As a general rule, services performed for a state employer or political subdivision employer by an employee hired by the state employer or political

subdivision employer after March 31, 1986, are subject to the Medicare tax. The following services, however, are NOT subject to the Medicare tax even though the services are performed by an employee hired after March 31, 1986:

(1) services covered by an agreement between the state and the Secretary of Health and Human Services entered into pursuant to section 218 of the Social Security Act, 42 U.S.C. section 418 (218 agreement) providing for social security coverage including Medicare,

(2) services excluded from the definition of employment under any provision of section 3121(b) of the Code other than section 3121(b)(7),

(3) services performed by an individual who is employed by a state employer

(except for a District of Columbia employer) or a political subdivision employer to relieve the individual of unemployment,

(4) services performed in a hospital, home, or other institution by a patient or inmate thereof as an employee of a state employer or a political subdivision employer,

(5) services performed by an individual as an employee of a state employer or a political subdivision employer serving on a temporary basis in case of fire, storm, snow, earthquake, flood, or other similar emergency, or

(6) services performed by any individual as an employee included under section 5351(2) of title 5, United States Code (relating to certain interns, student nurses, and other student employees of the District of Columbia government), other than as a medical or dental intern or a medical or dental resident in training.

THE CONTINUING EMPLOYMENT EXCEPTION

Q2. If an employee was hired before April 1, 1986, by a state employer or a political subdivision employer and services are performed for the state employer or political subdivision employer by that employee after March 31,

1986, are those services subject to the Medicare tax?

A2. Services are not subject to the tax if they are performed after March 31,

1986, for a state employer or political subdivision employer by an employee who was hired by the state employer or the political subdivision employer before April 1, 1986, and if the employee meets the following requirements:

(i) the employee was performing regular and substantial services for remuneration for the state employer or political subdivision employer before April 1, 1986,

(ii) the employee was a bona fide employee of that employer on March 31, 1986,

(iii) the employment relationship with that employer was not entered into for purposes of avoiding the Medicare tax, and

(iv) the employment relationship of the employee with that employer has not been terminated after March 31, 1986 (other than as provided in the rules described in Q&A8 below, which concern employees who transfer from one state employer, or one political subdivision employer, to another).

Section 3121(u)(2)(C) of the Code.

For purposes of this revenue ruling, this exception to the Medicare tax is called the 'continuing employment exception.'

Q3. An employee signed an employment contract before April 1, 1986, but did not begin to perform services until after March 31, 1986. Does the employee qualify for the continuing employment exception?

A3. No. The employee does not qualify for the continuing employment exception because the employee was not performing regular and substantial services for remuneration before April 1, 1986. Section 3121(u)(2)(C)(ii)(I) of the Code.

Q4. Before April 1, 1986, an individual was performing services for remuneration as a substitute teacher on an 'as needed' basis for a state employer or a political subdivision employer, and the individual continued performing those services on that basis after March 31, 1986. Does the individual qualify for the continuing employment exception?

A4. No. The individual does not qualify for the continuing employment exception. Even though the services performed may have been substantial, the services were not regular because they were performed on an 'as needed' basis. Section 3121(u)(2)(C)(ii)(I) of the Code.

Q5. A was a state employee performing regular and substantial services for remuneration prior to April 1, 1986. A's employment relationship with the state employer was terminated after March 31, 1986. but A was later rehired by the state employer. Does the continuing employment exception apply to A?

A5. No. Section 3121(u)(2)(C)(iii) of the Code.

Q6. How is termination of employment defined for purposes of determining whether the Medicare tax is applicable?

A6. The question of whether an employment relationship has terminated is a question of fact that must be determined on the basis of all the relevant facts and circumstances. Great weight, however, will be given to the personnel rules of the state employer or political subdivision employer to determine whether an employment relationship has been terminated.

Q7. An employee who was hired before April 1, 1986, by a state employer transferred after March 31, 1986, to another state employer of that state. The transfer was made without a termination of the employee's overall employment relationship with that state. Does the employee qualify for the continuing employment exception?

A7. Yes. An employee hired before April 1, 1986, by a state employer who transfers after March 31, 1986, to another state employer of that state may qualify for the continuing employment exception, provided the transfer was made without a termination of the employee's overall employment relationship with that state. The same rule applies

to an employee hired before April 1, 1986, by a political subdivision employer, who transfers after March 31, 1986, to another political subdivision employer of that political subdivision.

On the other hand, an employee hired before April 1, 1986, does not qualify for the continuing employment exception if after March 31, 1986, the employee transfers from a state employer to a political subdivision employer or from a political subdivision employer to a state employer. Likewise, an employee does not qualify for the exception if the employee transfers from a political subdivision employer in one political subdivision to a political subdivision employer in a different political subdivision, or from a state employer in one state to a state employer in a different state. Section 3121(u)(2)(D) of the Code.

Different rules, however, control whether a transfer affects an employee's status for purposes of the Medicare tax wage base. In the case of an employee who is subject to the Medicare tax, even if the employee transfers from one state employer to another state employer of that state or from one political subdivision employer to another political subdivision employer of that political subdivision, a new Medicare tax wage base applies to wages received from the second employer. Thus, the rules that determine whether there is a new Medicare tax wage base are the same as those applicable to employees of private employers.

SERVICES EXCLUDED FROM EMPLOYMENT

Q8. What services are excluded from the definition of employment?

A8. See sections 3121(b)(1)-(6), (8)-(20) of the Code for a list of services that are excluded from the definition of employment for purposes of the social security taxes, including the Medicare portion of the taxes.

Q9. A 218 agreement may contain terms optionally excluding from social security coverage certain types of employment. 42 U.S.C. section 418(c)(3). If employment is optionally excluded from coverage under the terms of a 218 agreement, is that employment subject to the Medicare tax if services are performed by an individual otherwise subject to the Medicare tax under the rules of Q&A1 and Q&A2?

A9. Yes. The optionally excluded services are subject to the Medicare tax if they are performed by an individual otherwise subject to the tax under the rules of Q&A1 and Q&A2 above.

Q10. A student is hired by a school, college, or university after March 31,

1986, to perform services for the school, college, or university. The student is in a group optionally excluded from coverage under the terms of an applicable 218 agreement. Are the services performed by the student subject to the Medicare tax?

A10. Services performed by a student employed by a school, college, or university are not subject to the Medicare tax if the student is enrolled and regularly attending classes at the school, college, or university. Section

3121(b)(10) of the Code. Services of a student that are subject to contributions under a 218 agreement continue to be subject to such contributions.

DEFINITION OF WAGES

Q11. Is the definition of wages for Medicare tax purposes the same as the definition of wages for making social security contributions under 218 agreements?

A11. No, not in all cases. The term 'wages' for purposes of paying Medicare tax is defined by section 3121(a) of the Code. The term 'wages' for purposes of making contributions under a 218 agreement is defined by section 209 of the Social Security Act. 42 U.S.C. section 409. Questions concerning the definition of wages (and employment) for purposes of paying Medicare tax should be directed to the Service. Questions concerning the definition of wages (and employment) for purposes of making 218 contributions should be directed to the Social Security Administration (SSA).

RULES FOR REPORTING AND PAYMENT OF MEDICARE TAX

Q12. Is the Medicare tax reported and paid to the Internal Revenue Service or to the SSA?

A12. The Medicare tax is reported and paid to the Service (1) by a state employer of a state if on April 7, 1986, NO employee of any state employer of that state was covered under a 218 agreement, and (2) by a political subdivision employer of a political subdivision if on April 7, 1986, NO employee of any political subdivision employer of that political subdivision was covered under a 218 agreement.

The Medicare tax is reported to the State Social Security Administrator (1) by a state employer of a state if on April 7, 1986, ANY employee of any state employer of that state was covered under a 218 agreement, and (2) by a political subdivision employer of a political subdivision if on April 7, 1986, ANY employee of any political subdivision employer of that political subdivision was covered under a 218 agreement.

Q13. A 218 agreement was in effect with state X on or before April 7, 1986. The agreement provided for coverage of employees of a political subdivision employer of political subdivision A but not for coverage of any employee of any political subdivision employer of political subdivision B. After April 7, 1986, a modification of the 218 agreement was executed providing for coverage of some, but not all, employees of a

political subdivision employer of political subdivision B. The effective date of the new coverage was April 1, 1986. When that political subdivision employer of political subdivision B reports and pays the Medicare tax on wages for services performed by those of its employees who are not subject to the modification, is the tax reported and paid to the State Social Security Administrator or to the Internal Revenue Service?

A13. The tax is reported and paid to the Internal Revenue Service. Modifying a 218 agreement after April 7, 1986, to extend coverage on a retroactive basis does not change the agency to which the employer must report and pay the Medicare tax for services performed by employees who are subject to the Medicare tax.

Q14. How is the Medicare tax reported and paid to the Internal Revenue Service?

A14. Taxable wages must be reported on line 6 of Form 941E, Quarterly Return of Withheld Federal Income Tax and Hospital Insurance (Medicare) Tax. The reporting, depositing, and paying of the Medicare tax are subject to the same rules applicable to private employers. These rules are similar to those applicable to income tax withholding.

Q15. How is the Medicare tax reported and paid to the SSA?

A15. The Medicare tax is reported and paid to the SSA just as contributions under a 218 agreement are reported and paid to the SSA.

Q16. Will all penalties for failure to pay the Medicare tax and failure to make timely deposits of that tax be assessed against state and political subdivision employers?

A16. The Service will waive penalties for failure to pay and for failure to make timely deposits of the Medicare tax with respect to services performed through the fourth quarter of 1986, so long as all payments due for April through December of 1986 are paid by February 2, 1987. If all payments due for April through December 1986 are not paid by February 2, 1987, this automatic waiver of penalties is not applicable, even with respect to amounts paid by February 2, 1987. Penalties may be waived, however, if the employer shows reasonable cause for failure to pay and failure to make timely deposits of the tax. See sections 6651 and 6656 of the Code. A state employer or political subdivision employer should not report any Medicare tax wages on line 6 of Form 941E for the second or third quarter unless appropriate deposits and/or payments are made for that quarter.

Q17. If a state employer or a political subdivision employer has federal employees on the state or political subdivision payroll, how should that employer report the full social security tax or the Medicare portion of the social security tax, whichever is applicable?

A17. The state employer or political subdivision employer should use Form

941E to report the full social security taxes and or the Medicare portion of the taxes. For those federal employees subject to the FULL social security taxes, the tax must be

included with the withheld federal income tax on line 3 of Form 941E, with an attached supporting statement showing the amount of wages subject to the social security taxes, the amount of the taxes withheld, and the employer's share of the taxes. For those federal employees subject ONLY to the Medicare portion of the social security taxes, the Medicare tax must be reported on line 6 of Form 941E.

Q18. If a state employer or a political subdivision employer must report and pay the Medicare tax to the Service as explained in Q&A12, how should the employer transmit Copy A of Forms W-2 for newly hired employees who are subject to the Medicare tax?

A18. For newly hired employees subject to the Medicare tax. the employer should transmit Copy A of Forms W-2 with a Form W-3, Transmittal of Income and Tax Statements, and should check the 'Medicare Fed. emp.' checkbox in Box 2 on the Form W-3. This checkbox will be changed to 'Medicare government employee' on the 1987 Form W-3 to reflect the extension of the Medicare tax to state and political subdivision employees. For employees not subject to the Medicare tax, the employers should follow the current practice of transmitting Copy A of Forms W-2 with a Form W-3, checking the ' 941/941r ' checkbox in Box 2 on the Form W-3.

Q19. If a state employer or a political subdivision employer must report and pay the Medicare tax to the State Social Security Administrator as explained in Q&A12, how should the employer transmit Copy A of Forms W-2 for newly hired employees subject to the Medicare tax?

A19. For newly hired employees subject to the Medicare tax, the employer should transmit Copy A of Forms W-2 with a Form W-3 S&L, Transmittal of Income and Tax Statements for State and Local Governmental Employers, and should check the 'Medicare Government Employee' checkbox on the Form W-3 S&L IN ADDITION TO the 'Section 218' checkbox. For those employees covered under a 218 agreement, the state employer or the political subdivision employer should follow the current practice of transmitting the Forms W-2 with a Form W-3 S&L, checking the 'Section 218' checkbox in Box 2 on the Form W- 3 S&L. If the employer also has employees who are not covered under the 218 agreement and who were hired before April 1, 1986, then for those employees, the employer should transmit Forms W-2 with a Form W-3 and should check the ' 941/941u ' box on the Form W-3.

Internal Revenue Service

Revenue Ruling 88-36

FICA, HOSPITAL INSURANCE; STATE AND POLITICAL SUBDIVISION EMPLOYEES

SECTION 3121. - DEFINITIONS

FICA, hospital insurance; state and political subdivision employees. Guidance is provided, in question and answer form, concerning the application of the hospital insurance (medicare) tax portion of the Federal Insurance Contributions Act (FICA) by section 3121(u) of the Code, to wages for services performed by state and political subdivision employees hired after March 31, 1986. Rev. Rul. 86-88 supplemented.

The Service has issued Rev. Rul. 88-36, supplementing Rev. Rul. 86-88, 1986-2 C.B. 172, in question and answer format, which provides guidelines concerning the 1985 amendment to section 3121(u), which extended Medicare (the hospital portion of FICA) to wages for services rendered by state and political subdivision employees hired after March 31, 1986. The ruling addresses such areas as the types of services which are subject to the medicare tax and the continuing employment exception. In general, an individual, who was employed by a state or political subdivision before March 31, 1986 and who was performing regular and substantial services for remuneration, will not be subject to the tax on services performed after that date. This rule applies only if the employment was not terminated after April 1.

This revenue ruling supplements Rev. Rul. 86-88, 1986-2 C.B. 172, which provides guidelines, in question and answer form, concerning the 1985 amendment of section 3121(u) of the Internal Revenue Code. In general, the amendment extends the hospital insurance (medicare) tax portion of the Federal Insurance Contributions Act (FICA) to wages for services rendered by state and political subdivision employees hired after March 31, 1986.

In this revenue ruling, the terms 'state,' 'political subdivision,' 'state employer,' 'political subdivision employer,' and 'continuing employment exception' have the same meanings as in Rev. Rul. 86-88.

SERVICES SUBJECT TO THE MEDICARE TAX

Q1. If an individual receiving social security retirement insurance benefits was hired as an employee of a state or political subdivision after March 31, 1986, are the services performed by the individual for the state or political subdivision subject to the medicare tax?

A1. Yes. The fact that an employee is receiving social security retirement insurance benefits does not affect the employee's liability for the medicare tax.

Q2. Are services performed by an election official or election worker for a state employer or political subdivision employer subject to the medicare tax?

A2. Yes, unless the remuneration paid in a calendar year for such service is less than $100. Section 3121(u)(2)(B)(ii)(V) of the Code, added by section 1895(b)(18)(A) of the Tax Reform Act of 1986, 1986-3 (Vol. 1) C.B. 852. This amendment is effective for services rendered after March 31, 1986.

Q3. A township has a small number of regularly employed fire fighters. To assist these fire fighters, certain residents of the township have volunteered their services in cases of emergency. The township alerts these residents to emergencies by sounding a siren. The township keeps a record of the residents who respond to the emergency calls and periodically pays each such resident a nominal amount for each emergency for which the resident performed services. Are the payments made to the residents by the township subject to the medicare tax?

A3. No. The services are considered to be performed by an employee of a state or political subdivision on a temporary basis in case of fire, storm, snow, earthquake, flood, or other similar emergency and thus are not subject to the medicare tax. See Section 3121(u)(2)(B)(ii)(III) of the Code.

THE CONTINUING EMPLOYMENT EXCEPTION

Q4. An individual was hired in September 1984 as a part-time cook by a state hospital to perform two hours of paid service each Sunday preparing the evening meal. The individual is not a patient or inmate of the hospital and has worked two hours each week as an employee of the hospital continuously since September 1984. Are the individual's services performed after March 31, 1986, subject to the medicare tax?

A4. No. The continuing employment exception applies here if the individual was performing regular and substantial services for remuneration for the state employer or political subdivision employer before April 1, 1986. Whether this requirement is met is a question of fact. On these facts, the individual's services are determined to be regular and substantial, and the exception applies.

Q5. In November 1982, an individual was elected to a state public office for a four-year term beginning in January 1983, making the individual an employee of the state. In November 1986, the individual was re-elected. Are the individual's services performed in the second term that begins in January 1987 subject to the medicare tax?

A5. No. The continuing employment exception applies here if the employment relationship has not been terminated after March 31, 1986. The individual was re-elected before the first term expired, so there was no break in the employment relationship.

Q6. B, a school district employee, performed regular and substantial services for remuneration for a political subdivision employer during the school year beginning in

September 1985 and ending in May 1986. In May 1986, the school district notified B that B's employment would be terminated as of the end of May 1986 because the school district might not receive sufficient funding. B continued to be covered under the school district's health insurance program through August 1986 on the same basis as before May

1986. Sufficient funding was provided, and in September 1986 B began working on the same basis as before. Are B's services performed after August 31, 1986, subject to the medicare tax?

A6. No. In fact, B's employment with the school district was continuous because the school district received sufficient funding. The school district's personnel policies indicate that the employment relationship continued because B retained health insurance coverage. See Q&A6 of Rev. Rul. 86-88.

Q7. C, a professor at a state university, performed regular and substantial services for remuneration for the university from September 1985 to June 1986. C was granted a leave of absence for the 1986-1987 school year, with the right to return to the same position at the end of the leave. In September 1987, C returned from the leave and resumed the same position with the university. Are C's services performed after returning from the leave of absence subject to the medicare tax?

A7. No. The leave of absence was granted by the university and did not terminate the employment relationship. The university's personnel policies indicate that the employment relationship continued because C was given the right to return to the same position. See Q&A6 of Rev. Rul. 86-88.

Q8. D taught a two-hour photography course twice a week at a local community college in the spring semester, which began on March 1, 1986. D then signed a three-year agreement with the college that he would teach the same course every spring. When D returned in the spring of 1987, were his services subject to the medicare tax?

A8. No. D was performing regular and substantial services for remuneration prior to April 1, 1986. The employment relationship was not terminated, as D had a commitment to return to the same position each spring.

Q9. Each summer, a Township Parks Department advertises for workers to cut grass. E was hired by the township in May 1985 to cut grass during that summer. E stopped performing services for the township at the end of that summer. In May 1986, E was again hired by the township to cut grass. Are E's services performed when E returned in

A9. Yes. E's employment relationship was terminated after April 1, 1986, as E had no commitment to perform services for the township each summer.

Q10. A part-time police officer has been paid on a weekly basis since March 10, 1986, to be 'on call' for a set schedule of hours each week. When the officer is 'on call,' he must stay at his residence and be available to provide assistance in the case of an emergency or

to handle any police business that may arise. Are the services performed by the officer after April 1, 1986 subject to the medicare tax?

A10. No. Although the officer responds to calls on an 'as needed' basis, he has a set schedule of hours during which he is performing the service of being available to respond to such calls. Based on the above facts, the officer was performing regular and substantial services for remuneration prior to April 1, 1986 and thus, qualifies for the continuing employment exception to the medicare tax.

Revenue Procedure 91-40

SECTION 1. PURPOSE
This revenue procedure sets forth rules relating to the minimum retirement benefit requirement prescribed under section 31.3121(b)(7)-2 of the Employment Tax Regulations.

SECTION 2. BACKGROUND
Section 3121(b)(7)(F), added to the Internal Revenue Code by section 11332(b) of the Omnibus Budget
Reconciliation Act of 1990, Public Law No. 101-508, 104 Stat. 1388, generally expands the definition of employment, for purposes of the Federal Insurance Contributions Act (FICA), to include service as an employee for a state or local government entity unless the employee is a “member of a retirement system” of such entity. Section 3121(b)(7)(F) is effective with respect to service performed after July 1, 1991. Thus, wages for services performed after July 1, 1991, received by an employee of a state or local government entity who is not a member of a retirement system of such entity will generally be subject to FICA taxes, and will also be taken into account in determining the employee’s eligibility for Social Security and Medicare benefits. Under section 31.3121(b)(7)-2(e) of the regulations, a retirement system generally includes any pension, annuity, retirement or similar fund or system within the meaning of section 218 of the Social Security Act that is maintained by a state, political subdivision or instrumentality thereof to provide retirement benefits to its employees who are participants. However, the definition of retirement system is limited in order to carry out the purposes of section 3121(b)(7)(F) of the Code and the corresponding provisions of the Social Security Act. Under the regulations, in order for service in the employ of a state or local government entity to qualify for the exception from employment
under section 3121(b)(7), the employee must be a member of a retirement system that provides certain minimum retirement benefits to that employee. To meet this minimum retirement benefit requirement with respect to an employee, section 31.3121(b)(7)-2(e)(2)(i) of the regulations generally requires that a retirement system provide benefits to the employee that are comparable to those provided in the Old-Age portion of the Old-Age, Survivor, Disability Insurance program under Social Security. Section 31.3121(b)(7)-2(e)(2)(vi) of the regulations provides that the Commissioner may, through guidance of general applicability, promulgate additional testing methods to determine whether, a retirement system meets the minimum retirement benefit requirement. This revenue procedure is an exercise of this authority. It outlines a set of safe harbor formulas for defined benefit retirement systems. Benefits calculated under one of these formulas

are deemed to meet the minimum retirement benefit requirement. In addition, procedures are set out by which an employer may determine whether retirement benefits calculated under other formulas meet the minimum retirement benefit requirement of the regulations with respect to an employee.

SECTION 3. DEFINED BENEFIT RETIREMENT SYSTEM SAFE HARBOR FORMULAS

.01 Final and highest average pay formulas.

(1) Periods of 36 months or less. A defined benefit retirement system that calculates benefits by reference to a participant's average compensation meets the minimum retirement benefit requirement with respect to an employee if it makes available to the employee a single life annuity payable beginning no later than age 65 that is at least 1.5 percent of average compensation for each year (or fraction thereof) of credited service. For this purpose, average compensation may be defined as the average of the employee's compensation over the 36 (or fewer) consecutive or non-consecutive months that provides the highest such average, the average of the employee's compensation for his or her last 36 (or fewer) months of service with the employer, or the average of the employee's compensation for his or her high consecutive or nonconsecutive or final 3 (or fewer) calendar or plan years of service.

(2) Periods of more than 36 months. A defined benefit retirement system that calculates benefits by reference to a participant's average compensation over a period of more than 36 months meets the minimum benefit requirement in the same manner as a retirement system described in section 3.01(l) except that the 1.5 percent factor is replaced with a higher factor in accordance with the following table:

Averaging period	Factor
37-48 months	1.55 percent
49-60 months	1.60 percent
61-120 months	1.75 percent
Over 120 months	2.00 percent

.02 Formulas using fractional accrual rule.

A defined benefit retirement system that calculates benefits based on a pro rata accrual towards a projected normal retirement benefit may meet the minimum retirement benefit requirement in the same manner as provided in section 3.01(l) provided the projected normal retirement benefit under the plan formula is greater than or equal to the benefit described in such section.

.03 Additional requirements for defined benefit plan formulas to meet safe harbors.

(1) Calculation of compensation.

(a) To meet the requirements of any of the defined benefit safe harbor formulas for plan years beginning after July 1, 1991, a retirement system must calculate benefits based on a definition of compensation that meets the requirements of section 31.3121(b)(7)-2(e)(2)(iii)(B) of the regulations.

(b) In the event that the definition of compensation under the retirement system is less inclusive than the definition otherwise permitted under this section, the applicable benefit

percentage in the safe harbor formula of section 3.01 must be increased to account for the lower compensation base. The benefit percentage for employees in a retirement system whose benefits are computed using this definition must be multiplied by the ratio of (i) aggregate compensation (defined as under section 3.03(l)(a) and assuming that compensation considered in determining retirement benefits is limited to the contribution base described in section 3121(x)(1)) of these employees to (ii) aggregate compensation (as defined under the plan) of these employees. This ratio may be determined based upon the compensation during the immediately preceding plan year. In the case of a retirement system sponsored by more than one employer, this ratio must be calculated separately with respect to the employees of each employer whose benefits are computed using this definition. The rule in this section 3.03(l)(b) is illustrated by the following example:
Example. A defined benefit retirement system maintained by a political subdivision provides a retirement benefit equal to 2.5 percent of a participant's average compensation during his or her last calendar year of service. The compensation used for this purpose satisfies section 3.03(l)(a), except that it caps the compensation taken into account at $30,000. Assume that the ratio under section 3.03(t)(b) is 150 percent. This figure is derived by comparing the total compensation of employees in the plan (using the plan definition but capping compensation at the FICA contribution base (rather than at $30,000)) to the total compensation (using only the plan definition of compensation) of employees in the plan. The retirement system meets the requirements of 3.03(l) because the plan benefit percentage of 2.5 percent is more than 150 percent of the applicable safe harbor benefit percentage of 1.5 percent.

(2) Credited service.
(a) In order to meet the requirements of any of the defined benefit safe harbor formulas, a formula must generally include in credited service the employee's entire period of actual service with the employer since commencing participation in the retirement system, plus any past service credited under the retirement system. A formula may, however, exclude any periods of actual service for the employer that are treated as employment under section 3121(b) of the Code, provided that during such periods the employee did not participate in the retirement system. A retirement system subject to paragraph (f)(2)(i)(B) of section 31.3121(b)(7)-2 of the regulations (relating to the treatment of benefits accrued in plan years beginning prior to January 1, 1993) may also limit service consistent with the rules contained in that paragraph.
(b) A formula may limit the maximum period of service that is credited for accrual purposes under this rule. If this limit is less than 30 years in the case of formulas described in section 3.01(l) or (2), or 35 years in the case of formulas described in section 3.02, however, the benefit formula must be increased by the ratio of 30 (or 35) years to such lower limit.
(c) Except as provided in section 3.03(4) with respect to part-time and other classes of employees, a formula may limit the periods of actual service actually credited for accrual purposes under this rule to whole years or similar periods, provided the periods are reasonable.
(d) The rules in this subsection are illustrated by the following example:
Example. In 1995, an employee is a participant in a retirement system with 5 years of credited service. Assume that the retirement system provides benefits under a formula

described in section 3.01. In January 1996, the employee moves to a position that is not covered by the retirement system. Assume that service in the new position constitutes covered employment under section 3121(b) of the Code for purposes of the FICA (e.g., because a section 218 voluntary agreement is in effect with regard to such position). In January 1998, the employee returns to the old position and recommences participation under the retirement system. The employee must be treated as being in the employee's sixth year of credited service in determining whether the benefit under the retirement system meets the minimum retirement benefit requirement. This is because the retirement system may generally disregard the service of an employee that constitutes employment under section 3121(b) for purposes of the FICA.

(3) Treatment of prior distributions from the retirement system.

In determining whether the requirements of any of the defined benefit safe harbor formulas are met, prior distributions may continue to be considered as part of the benefit accrued under the retirement system unless they were distributed by the employer without any election by the employee. In addition, if a retirement system gives a former employee credit for benefit determination purposes for periods of prior service with respect to which a prior distribution was made only if the employee contributes to the system an amount equal to all or a portion of the prior distribution (with or without interest), and this option is provided on reasonable terms, such prior service is not required to be taken into account in determining whether the requirements of any of the defined benefit safe harbors are met until the required contribution is actually made. If prior service is not taken into account under this rule, the prior distribution may not be taken into account either. The rules of this paragraph is illustrated by the following example:

Example. An employee retires under the early retirement option under a retirement system maintained by a state government. The employee elects to receive a single sum distribution representing the entire accrued benefit under the plan. Subsequently, the employee is rehired by the same employer. The plan does not provide for any recontribution of the prior distribution. Whether the employee is a member of the retirement system from which the employee received the distribution is determined without regard to the single sum distribution. That is, a single life annuity that is the actuarial equivalent of the single sum may be treated as part of the accrued benefit under the plan. Similarly, all periods of service credited under the plan during the employee's previous service must be considered.

(4) Credited service for part-time, seasonal, and temporary employees.

To meet the requirements of any of the defined benefit safe harbor formulas with respect to a part-time, seasonal or temporary employee for plan years beginning after December 31, 1992, a safe harbor formula may not permit double proration of the employee's benefits under the retirement system. See 29 CFR §2530.204-2(d) for a description of double proration of benefit accruals. Under this rule, the benefit under the retirement system may be prorated either on the basis of full-time service or on the basis of full-time compensation, but may not be prorated based on both service and compensation. In addition, a safe harbor formula may not subject the crediting of service used in calculating the benefit of any part-time, seasonal or temporary employee to any conditions, such as a requirement that the employee attain a minimum age, perform a minimum period of service, be credited with a minimum number of hours of service, make an election in order to participate, or be present at the end of the plan year. The

requirements of this section 3.03(4) will be deemed met with respect to an employee, however, if the requirements of section 31.3121(b)(7)-2(d)(2)(ii) of the regulations relating to amounts distributable upon certain events are met with respect to such employee. See section 31.3121(b)(7)-2(d)(2)(iii) of the regulations for the definitions of part-time, seasonal, and temporary employee for this purpose.

.04 Examples of application of safe harbor formulas.

The application of the defined benefit safe harbors are illustrated in the following examples:

Example 1. An employee has been a participant in a state retirement system for 9 years and several months at the beginning of a plan year of the system. The employee has only 9 years of credited service under the system at the beginning of the plan year, however, because the retirement system calculates service for accrual purposes on the basis of whole years of actual service. Under the retirement system, each participant is credited with a retirement benefit based upon the participant's highest average compensation over 36 consecutive months times his or her years of service (as so determined). Assume the retirement system imposes no other conditions on the accrual of benefits and meets the service crediting requirements of section 3.03(2). If at all times during the plan year prior to being credited with a tenth year of service the employee has a total accrued benefit of at least 13.5 percent of his or her highest average compensation (1.5 percent times 9 years), and at all times during the plan year after being credited with the tenth year of service the employee has a total accrued benefit of at least 15 percent of his or her highest average compensation (1.5 percent times 10 years), and the retirement otherwise meets the requirements of this revenue procedure and the regulations, the employee will be treated as a qualified participant throughout the plan year. This analysis applies without regard to whether the participant actually accrues a benefit in the plan year or is credited with an additional year of service for accrual purposes (e.g., if future accruals under the plan have been frozen or if the participant has obtained the maximum level of benefits under the plan).

Example 2. Assume the same facts as in Example 1, except that the plan grants 1 month of credited service for every whole month of actual service, and that the employee had 111 months of service (9 years and 3 months) at the beginning of the plan year. If at all times during the first month of the plan year prior to being credited with the 112th month of service the employee has a total accrued benefit of at least 13.875 percent of his highest average compensation (1.5 percent times 111 months, divided by 12), and at all times during the first month of the plan year after being credited with the 112th month of service the employee has a total accrued benefit of at least 14 percent of his highest average compensation (1.5 percent times 112 months, divided by 12), and the retirement system otherwise meets the requirements of this revenue procedure and section 31.3121(b)(7)-2(e) of the regulations, the participant is a qualified participant in the plan within the meaning of section 31.3121(b)(7)-2(d)(1) for the entire first month of the plan year.

Example 3. Assume the same facts as in Example 1, except that, instead of crediting only whole years of participation for accrual purposes, the retirement system credits only service during plan years in which a participant has at least 1,000 hours of service. Thus, as in Example 1, the participant has 9 years of credited service at the beginning of the plan year. If at all times during the plan year prior to meeting the 1,000-hour requirement

the employee has a total accrued benefit of at least 13.5 percent of his or her highest average compensation (1.5 percent times 9 years), and at all times during the plan year after meeting the 1,000-hour requirement the employee has a total accrued benefit of at least 15 percent of his or her highest average compensation (1.5 percent times 10 years), the employee will be treated as a qualified participant in the retirement system within the meaning of section 31.3121(b)(7)-2(d)(1) of the regulations throughout the plan year.

SECTION 4. DEFINED BENEFIT RETIREMENT SYSTEMS WITH BENEFIT FORMULAS NOT DESCRIBED IN THE SAFE HARBORS OF SECTION 3

.01 In general.

A defined benefit retirement system that calculates benefits under a formula that does not meet one of the safe harbor formulas described in section 3 of this revenue procedure meets the minimum retirement benefit requirement with respect to an employee if the employee's accrued benefit as of the date of the determination is at least as great as the accrued benefit the employee would have if his or her accrued benefit had been calculated under the safe harbor formula in section 3.01(l). In determining whether this requirement is satisfied, the additional requirements set forth in section 3.03 must be taken into account. The rules in this paragraph are illustrated by the following example:

Example. A defined benefit plan maintained by a political subdivision and described in section 457(b) of the Code provides only for single sum distributions and thus does not meet the requirements of any of the defined benefit safe harbor formulas. The plan may still meet the minimum retirement benefit requirement with respect to an employee if it provides a single sum with respect to such employee that is the actuarial equivalent (using reasonable actuarial assumptions) of a single life annuity meeting the requirements of section 3.01(1).

.02 Treatment of past service credit.

In determining whether an employee's accrued benefit under a defined benefit retirement system that calculates benefits under a formula that does not meet one of the defined benefit safe harbor formulas is at least as great as the accrued benefit the employee would have if his or her accrued benefit had been calculated under the safe harbor formula in section 3.01(1), a retirement system may ignore periods of service by an employee with the employer prior to his or her commencement of participation in the retirement system, notwithstanding the additional rules relating to credited service in section 3.03(2). If such periods of service are ignored, however, any accrued benefits attributable to such period of service must also be ignored. The rule in this paragraph is illustrated by the following example:

Example: An employee begins to participate in a retirement system in the employee's fifth year of service. The retirement system provides credit for all past service with the employer. Assume the retirement system does not provide benefits under a formula that meets the requirements of any of the safe harbors. The employee must be treated as being in the employee's fifth year of credited service if benefits attributable to the past service are to be taken into account in comparing the benefit under the retirement system to the benefit the employee would have under the safe harbor formula of section 3.01(1) to determine whether the minimum retirement benefit requirement is met.

SECTION 5. EMPLOYEES WITH MULTIPLE POSITIONS OR WHO PARTICPATE IN CERTAIN

RETIREMENT SYSTEMS

See section 31.3121(b)(7)-2(e)(2)(iv) and (v) of the regulations for rules to be used in determining the service, compensation and benefits taken into account for purposes of this revenue procedure in the case of employees who are employed in more than one position with the employer, and employees who are participants in retirement systems maintained by more than one employer, respectively.

SECTION 6. EFFECTIVE DATE

This revenue procedure is effective with respect to service performed after July 1, 1991.

Guide to the Citations in this Publication

Citation Source	Example	Purpose
Internal Revenue Code	IRC §132(a)(1)	Title 26 of the United States Code, the primary statutory authority for laws dealing with federal tax.
Treasury Regulation	Reg. §1.162-2(a)(2)	Provides guidance for new legislation or to address issues that arise with respect to existing Internal Revenue Code sections. Regulations interpret and give directions on complying with the law.
Treasury Proposed Regulation	Prop. Reg. 106897-08	Generally, regulations are first published in proposed form in a Notice of Proposed Rulemaking (NPRM).
Treasury Decision	TD 9696	Document that contains the text of a final or temporary regulation
Revenue Procedure	RP 2014-1	An official statement of a procedure that affects the rights or duties of taxpayers or other members of the public under the Internal Revenue Code, related statutes, tax treaties and regulations and that should be a matter of public knowledge.
Revenue Ruling	RR 2012-25	An official interpretation by the IRS of the Internal Revenue Code, related statutes, tax treaties and regulations. It is the conclusion of the IRS on how the law is applied to a specific set of facts.
Notice	Notice 98-03	A public pronouncement that may contain guidance that involves substantive interpretations of the Internal Revenue Code or other provisions of the law.
Announcements	Ann. 85-113	A public pronouncement that has only immediate or short-term value.
Private Letter Ruling	PLR 200437030	A private letter ruling, or PLR, is a written statement issued to a taxpayer that interprets and applies tax laws to the taxpayer's specific set of facts. A PLR may not be relied on as precedent by other taxpayers or IRS personnel.
Technical Advice Memorandum	TAM 200222003	Guidance furnished by the Office of Chief Counsel to IRS personnel in response to an internal request, concerning technical or procedural questions that develop during a proceeding.
Supreme Court Decision	269 U.S. 514 (1926)	Final decision on tax matter presented to Supreme Court from lower courts.
Social Security Act	42 U.S.C. section 418	Original 1935 legislation establishing social security; now Title 42 of the United States Code.

Statutory Citations for State Enabling Laws As of July 2014	
State or U.S. Territory	**Citation**
Alabama	Code of Alabama, Title 36. Public Officers and Employees, Chapter 28, Social Security for State, Municipal, Etc., Employees, § 36-28-1, et seq.
Alaska	Alaska Statutes Annotated, Title 39, Public Officers and Employees, Chapter 30. Insurance and Supplemental Employee Benefits, Article 1, Old Age and Survivors Insurance, § 39.30.010, et seq.
Arizona	Arizona Revised Statutes Annotated, Title 38. Public Officers and Employees, Chapter 5. Social Security and Retirement, Article 1, Social Security for Public Officers and Employees, § 38-701 et seq.
Arkansas	Arkansas Code Annotated, Title 24. Retirement and Pensions, Chapter 1. General Provisions, Subchapter 2. Public Employees' Social Security, § 24-1-201, et seq.
California	Annotated California Codes, Government Code, Title 2. Government of the State of California, Division 5. Personnel, Part 4. Federal Old Age and Survivors' Insurance, Chapter 1. General Provisions, Definitions, Designation of Special Groups, Article 1. General Provisions and Definitions, § 22000, et seq.
Colorado	Colorado Revised Statutes Annotated, Title 24. Government—State Public Employees' Retirement Systems, Article 53. Public Employees' Social Security, § 24-53-101, et seq.
Connecticut	Connecticut General Statutes Annotated, Title 5. State Employees, Chapter 66. State Employees Retirement Act, Part I. General Provisions, § 5-152 et seq.
Delaware	Delaware Code Annotated, Title 29. State Government, Part V. Public Officers and Employees, Chapter 57. Social Security, § 5701, et seq.
Florida	Florida Statutes Annotated, Title XXXVII. Insurance (Chapters 624-651), Chapter 650. Social Security for Public Employees 650.01, et seq.
Georgia	Code of Georgia Annotated, Title 47. Retirement and Pensions, Chapter 18. Social Security Coverage for Employees of the State and Political Subdivisions of the State, Article 1. General Provisions § 47-18-1, et seq.
Hawaii	Hawai‘i Revised Statutes Annotated, Division 1. Government, Title 7. Public Officers and Employees, Chapter 88. Pension and Retirement Systems, Part VI. Federal Social Security for Public Employees, § 88-211, et seq.
Idaho	Idaho Code Annotated, Title 59. Public Officers in General, Chapter 11. Social Security Benefits, § 59-1101, et seq.
Illinois	Smith-Hurd Illinois Compiled Statutes Annotated, Chapter 40. Pensions, Act 5. Illinois Pension Code, Article 21, Social Security Enabling Act 5/21-101, et seq.
Indiana	Annotated Indiana Code, Title 5. State and Local Administration, Article 10.1. Social Security Coverage for Public Employees, Chapter 1. Definitions, 5-10.1-1-1, et seq.
Iowa	Iowa Code Annotated, Title III. Public Services and Regulation [Chs. 80-122C], Subtitle 3. Retirement Systems [Chs. 97-98A], Chapter 97C. Federal Social Security Enabling Act, 97C.1, et seq.
Kansas	Kansas Statutes Annotated, Chapter 40. Insurance, Article 23. Old-Age and

Statutory Citations for State Enabling Laws As of July 2014	
State or U.S. Territory	**Citation**
	Survivors Insurance for Public Employees, 40-2301.
Kentucky	Baldwin's Kentucky Revised Statutes Annotated, Title VIII. Offices and Officers, Chapter 61, General Provisions as to Offices and Officers; Social Security for Public Employees; Employees Retirement System, General Provisions, Social Security for Public Employees, 61.410 , et seq.
Louisiana	Louisiana Statutes Annotated, Louisiana Revised Statutes, Title 42. Public Officers and Employees, Chapter 13. Old Age, Survivors, Disability, and Health Insurance, § 1001, et seq.
Maine	Maine Revised Statutes Annotated, Title 5. Administrative Procedures and Services, Part 21. Social Security for State and Municipal Employees, Chapter 431. Social Security for State and Municipal Employees, § 19001, et seq.
Maryland	Annotated Code of Maryland, State Personnel and Pensions, Division III. Other Retirement and Pension Provisions [Titles 35-End], Title 36. Social Security Benefits, § 36-101, et seq.
Massachusetts	Massachusetts General Laws Annotated, Part I. Administration of the Government (Ch. 1-182), Title XVII. Public Welfare (Ch. 115-123B), Chapter 118C. Coverage of Certain Employees Under the Federal Social Security Act, § 1, et seq.
Michigan	Michigan Compiled Laws Annotated, Chapter 38. Civil Service and Retirement, Social Security for Public Employees, 38.851, et seq.
Minnesota	Minnesota Statutes Annotated, Retirement (Ch. 352-356B), Chapter 355. Social Security Coverage, State and Local Government Employees, § 355.01, et seq.
Mississippi	West's Annotated Mississippi Code, Title 25. Public Officers and Employees; Public Records, Chapter 11. Social Security and Public Employees' Retirement and Disability Benefits, Article 1. Social Security Benefits, § 25-11-1, et seq.
Missouri	Vernon's Annotated Missouri Statutes, Title VIII. Public Officers and Employees, Bonds and Records, Chapter 105. Public Officers and Employees--Miscellaneous Provisions Generally, § 105.005, et seq.
Montana	Montana Code Annotated, Title 19. Public Retirement Systems, Chapter 1. Social Security, Part 1. General Provisions, § 19-1-101, et seq.
Nebraska	Revised Statutes of Nebraska Annotated, Chapter 68. Public Assistance, Article 6. Social Security, §68-601, et seq.
Nevada	Nevada Revised Statutes Annotated , Title 23. Public Officers and Employees (Chapters 281-289), Chapter 287. Programs for Public Employees, Participation of Employees of State and Its Political Subdivisions in Federal Old-Age and Survivors' Insurance, §287.050, et seq.
New Hampshire	Revised Statutes Annotated of the State of New Hampshire, Title VI. Public Officers and Employees (Ch. 91 to 103), Chapter 101. Old Age and Survivors' Insurance, §101:1, et seq.
New Jersey	New Jersey Statutes, TITLE 43. Pensions and Retirement and Unemployment Compensation, Subtitle 9 Social Security, Chapter 22, Old Age and Survivors

Statutory Citations for State Enabling Laws As of July 2014	
State or U.S. Territory	**Citation**
	Insurance for Public Employees, § 43:22-1, et seq.
New Mexico	New Mexico Statutes Annotated, Chapter 10. Public Officers and Employees, Article 14. Social Security Coverage § 10-14-1, et seq.
New York	McKinney's Consolidated Laws of New York Annotated, Retirement and Social Security Law, Chapter 51-A of the Consolidated Laws, Article 1. Short Title § 1. Short title of chapter, Article 3. Federal Old-Age and Survivors Insurance Coverage for Certain Public Employees § 130, et seq.
North Carolina	North Carolina General Statutes Annotated, Chapter 135. Retirement System for Teachers and State Employees; Social Security; State Health Plan for Teachers and State Employees, Article 2. Coverage of Governmental Employees Under Title II of the Social Security Act § 135-19, et seq.
North Dakota	North Dakota Century Code Annotated, Title 52. Social Security, Chapter 52-10. Public Employees Under Federal Social Security § 52-10-01, et seq.
Ohio	Baldwin's Ohio Revised Code Annotated, Title I. State Government, Chapter 144. Old Age and Survivors Insurance--Municipal Employees 144.01, et seq.
Oklahoma	Oklahoma Statutes Annotated, Title 51. Officers, Chapter 4. Old Age and Survivors Insurance Under Federal Act, § 121, et seq.
Oregon	Oregon Revised Statutes Annotated, Title 22. Public Officers and Employees, Chapter 237. Public Employee Retirement Generally, Social Security Act Coverage, 237.410, et seq.
Pennsylvania	Purdon's Pennsylvania Statutes and Consolidated Statutes, Title 65 P.S. Public Officers, Chapter 10. Public Officer and Employee Social Security Contribution Law § 201, et seq.
Puerto Rico	Laws of Puerto Rico Annotated, Title Three. Executive, Chapter 33. Retirement of Government Personnel Federal social security for Puerto Rico § 813, et seq.
Rhode Island	General Laws of Rhode Island Annotated, Title 36. Public Officers and Employees, Chapter 7. Federal Old-Age and Survivors' Insurance, § 36-7-1, et seq.
South Carolina	Code of Laws of South Carolina 1976 Annotated, Title 9. Retirement Systems, Chapter 3. Coverage of Public Officers and Employees, Under Federal Social Security Act, Article 1. General Provisions § 9-3-10, et seq.
South Dakota	South Dakota Codified Laws, Title 3. Public Officers and Employees, Chapter 3-11. Social Security Coverage 3-11-1, et seq.
Tennessee	West's Tennessee Code Annotated, Title 8. Public Officers and Employees, Chapter 38. Social Security § 8-38-101, et seq.
Texas	Vernon's Texas Statutes and Codes Annotated, Government Code, Title 6. Public Officers and Employees, Subtitle A. Provisions Generally Applicable to Public Officers and Employees, Chapter 606. Social Security, Subchapter A. General Provisions § 606.001, et seq.
Utah	Utah Code Annotated, Title 67. State Officers and Employees, Chapter 11. Federal Social Security § 67-11-1, et seq.

Statutory Citations for State Enabling Laws As of July 2014	
State or U.S. Territory	**Citation**
Vermont	Vermont Statutes Annotated, Title Three. Executive, Part 1. Generally, Chapter 19. Social Security for State and Municipal Employees § 571, et seq.
Virginia	Annotated Code of Virginia, Title 51.1. Pensions, Benefits, and Retirement, Chapter 7. Federal Social Security for State and Local Employees § 51.1-700, et seq.
Virgin Islands	Bill Number 10, Sixteenth Session, 1951.
Washington	Revised Code of Washington Annotated, Title 41. Public Employment, Civil Service, and Pensions, Chapter 41.48. Federal Social Security for Public Employees 41.48.010, et seq.
West Virginia	Annotated Code of West Virginia, Chapter 5. General Powers and Authority of the Governor, Secretary of State and Attorney General; Board of Public Works; Miscellaneous Agencies, Commissions, Offices, Programs, Etc., Article 7. Social Security Agency, § 5-7-1, et seq.
Wisconsin	Wisconsin Statutes Annotated, Public Employee Trust Fund (Ch. 40), Chapter 40. Public Employee Trust Fund, Subchapter III. Social Security for Public Employees 40.40, et seq.
Wyoming	Wyoming Statutes Annotated, Title 9. Administration of the Government, Chapter 3. Compensation and Benefits, Article 3. Social Security § 9-3-301, et seq.

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Legal Aspects of Handling Employee Overpayments

Eastern Section Payroll R&D Committee

2008 CASBO Annual Conference
Anaheim, California

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Legal Aspects of Handling Employee Overpayments

CASBO

April 27, 2008

CASBO Annual Conference

SMART BUSINESS. SMART SCHOOLS. TM

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Presented By

Jan Hobson, Payroll Manager
Orange Unified School District

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Orange County Department of Education

Government Code

Background

When dealing with employee overpayments in a School District we must, for the most part, depend on the laws of the Government Code. In a School District atmosphere where we rely so heavily on a set of laws that are exclusive to our business, it is difficult to grasp the thought that our California Education Code is silent and the Government Code takes over as the final ruling on the matter of employee overpayments.

Therefore in 1988 the case of California State Employees' Association vs. the State of California was heard. In summary the case was as follows:

In August 1986 an audit report of the California Medical Facility at Vacaville reported 731 outstanding erroneous salary advances totaling $463,113. In mid-October 1986 respondents began notifying affected employees by form letter of the amount of and reason for the individual overpayments. The letter set out a repayment plan to deduct up to $400 from the net salary and 40% of the net overtime wages beginning with the October pay period. Employees were given 7 days within which to negotiate a modification of the repayment scheduling due to undue hardship. Any employee questions were directed to the Business Office. At least one employee received a memorandum from the personnel office in mid-October entitled "Accounts Receivable", which specified the amount of and reason for the overpayment and gave the name of a contact person to call if there were questions.

Respondents contended that Government Code Section 17051 authorized the salary withholding method utilized herein, and relied on Gefakys vs. State Personnel Board (1982) as authority for their position.

Appellate court contended that the general provisions of Government Code Section 17051 must give way to the specific statutory scheme of the attachment law and the wage garnishment and that respondents' recoupment procedure constitutes an unlawful attachment of garnishments in violation thereof, or an unlawful setoff in contravention of policies underlying the attachment and wage garnishment statutes.

The county counsel of the San Diego County Office of Education offered this opinion in regards to the case:

"Other than as provided in Education Code Section 45197(g)/88197(g) we find no authority for school districts to withhold amounts from an employee's current wages due to overpayments. In the absence of such explicit authority it appears that the decision in California State Employees Association vs. State of California would govern. This means that in the absence of employee consent, the district must obtain a court judgment against the employee for the amount due and execute thereon by the means legally available which may include wage garnishment."

Education Code

Background

Education Code Section 45197(g) and 88197(g) refers to annual vacations and says:

(g) If an employee is terminated and had been granted vacation which was not yet earned at the time of termination of his/her services, the employer shall deduct from the employee's severance check the full amount of salary which was paid for such unearned days of vacation taken.

This appears to be the only situation that overpayments can be automatically recovered without employee consent.

District Policy

The district should have a written administrative policy in place outlining the procedure for recovery of overpayments.

Examples of procedures to include in the policy are:

- ☑ **Notification of Overpayment** – *Employee will be notified in writing within a specific time frame from date of discovery.*
- ☑ **Overpayment Schedules** - *Overpayments must be repaid by the employee in the calendar year in which the overpayment occurred.*
- ☑ **Repayment Restrictions** – *Repayment amount deducted from employee's wages can not be more than XX% of employee's net wages.*
- ☑ **Agreement to Terms** – *Employee may request to meet with the Payroll Supervisor. Employee agreement to terms of overpayment must be in writing.*
- ☑ **No Agreement** – *Legal action that will be taken by the district to recover overpayment.*

REMEMBER:

Written Policy does not give the district the legal right to collect an overpayment without the employee's approval.

Contract Language

The district policy for recovery of overpayments should also be included in the contract language of the district.

District Contract Language Examples:

- *Whenever it is determined that an error has been made in the calculation of reporting any classified employee's payroll or in the payment of any classified employee's salary, the District shall, within five (5) workdays following such determination, provide the employee with a statement of the correction. However, the District, after standard payroll deductions, shall withhold $25.00 as a calculation adjustment. In the case of an underpayment, a supplemental payment will be paid to the employee by the District. A repayment schedule for salary overpayment shall be agreed to between the employee and the District.*

- *Proper salary class and step placement is a joint responsibility of the employee and the District. All employees are to review their salary placement at least annually and should they believe that they are improperly placed on the salary schedule, they are to immediately bring this information to the attention of the District. Any payroll error resulting in insufficient payment for an employee in the bargaining unit shall be corrected, and a special payroll revolving fund check issued no later than 5 working days after the Payroll Department has received both a written request from the employee and verification of the error. Should the incorrect salary placement result in an overpayment, the employee shall upon realizing the fact or upon notification from the District, repay the full amount of such overpayment, based upon a repayment schedule developed by the Accounting Director and the employee. The repayment period should not be longer than the period during which the employee was overpaid except that such repayment schedule shall not result in more than twenty-five (25%) of the employee's take home pay, being withheld from any single pay check. In the event of any payroll error, such error shall be corrected retroactively for a period of up to three (3) years from the date the error was discovered.*

- *Any adjustment to an employee's paycheck due to an error in payment which constitutes a reduction of the normal paycheck shall be limited to no more than 25% from any pay period provided an employee has not indicated intent to resign. Such adjustments shall be accompanied by an oral or written explanation prior to such issuance of the check.*

Employee Notifications

In the case of an overpayment, employees should be notified as soon as possible. Initial notification to the employee may be verbal. However, if the employee can not be reached directly, do not leave any details on an answering machine. The most information to leave on an answering machine is your name, title, and brief message to the employee to please contact the Payroll Department regarding their last pay check.

Follow up with written notification to the employee. It is recommended notifications to the employee be sent via Certified Mail / Return Receipt Requested.

The notification should include:

- ☑ Period of Overpayment
- ☑ Reason for Overpayment
- ☑ Amount of Overpayment
- ☑ A referral to the person who will arrange a repayment schedule.

When meeting with the employee:

- ☑ Have documentation showing the amount that was paid in comparison to the amount that should have been paid to the employee.
- ☑ Know the parameters of repayment plans allowed by the district policy and contract language.
- ☑ Have various repayment plans ready to discuss with the employee.
- ☑ Remain calm and avoid accusatory statements.
- ☑ Obtain written authorization from the employee for the repayment agreement.

Sample Notifications

Date

Name
Address
City

Re: Salary Overpayment

Dear

This letter is to advise you that you have been overpaid on your salary. On _____, 2008, you received a salary overpayment of $_____ in error.

Please contact the Payroll Department to discuss a repayment agreement at (714) 123-XXXX.

Sincerely,

Name
Title

Payroll Department
The District

SECOND REQUEST

Date

Name
Address
City

Re: Salary Overpayment

Dear

On _____, 2008, this office sent you a letter notifying you that you had been overpaid on your salary. As indicated in the letter, on _____, 2008, you received a salary overpayment in error in the amount of $_____. As of the date of this letter, this amount is still outstanding.

Please issue a personal check for the salary overpayment payable to the "The District", attach the check to a copy of this notice, and return to the address indicated below. Thank you for your prompt attention to this matter.

If you have any questions, please call me at (714) 123-XXXX.

Sincerely,

Name
Title

Payroll Department
The District

FINAL REQUEST

Date

Name
Address
City

Re: Salary Overpayment

Dear

On _____ and _____, 2008, this office notified you that you had been overpaid on your salary. As indicated in the letters, on _____, 2008, you received a salary overpayment in error in the amount of $_____. As of the date of this letter, this amount is still outstanding.

This office is legally obligated to recoup the full amount of overpaid compensation made to an employee. Failure to collect overpaid compensation would be a gift of public funds in violation of Article XVI, section 6 of the California Constitution.

Please contact this office immediately at (714) 123-XXXX to make payment arrangements. If you do not contact this office by _____, 2008, we will have no alternative but to begin collection proceedings.

Your prompt attention to this matter would be greatly appreciated.

Sincerely,

Name
Title
The District

Payroll Procedures

The district should establish payroll procedures to avoid overpayments.

Examples of Payroll Procedures to follow are:

- ☑ Establish a committee to include Payroll, Human Resources, Benefits, and Risk Management.
  - o Meet once a month to review status of employees on long term leaves such as Maternity Leave or Worker's Compensation.
  - o Review possible procedure changes that may be required as to how information is distributed between Payroll and other departments.
- ☑ Meet quarterly with site timekeepers.
  - o Review district policy and contract language required for tracking employee leaves.
  - o Receive feedback from the sites which may help in detecting communication problems between sites and district office.
- ☑ Pay off excess vacation on the next payroll cycle after an employee terminates.
- ☑ Remove employees from direct deposit when paying the final wages due after termination.
- ☑ Review preliminary edit reports prior to final payroll.
  - o Duplicate or Multiple Assignment Edit
  - o Paying Employee in Terminated Status Edit
  - o Net Amount Issued Over District Cap Edit
  - o Employees in Sick Differential Edit

Small Claims Court

Should You Go?

Before a district decides to go to small claims court to recover an overpayment, there are a few questions that may need to be reviewed.

- What is the dollar amount of the claim? If it is more than $5000, will the district waive the excess amount of the overpayment and still go to court?
- Has the district made a reasonable effort to contact the employee to offer a compromise? Does the Payroll Department have records of the attempts made to contact the employee and copies of the correspondence?
- Assuming the district will win, is there reasonable assurance that it will be able to collect on the judgment?

In order to garnish an employee's wages, the party to whom the money is owed must obtain a money judgment award from the court which has jurisdiction over the matter.

If the amount sought to be recovered is less than $5,000, such judgment can be sought through a small claims award. If the amount is greater than $5,000, the District has the option of waiving any monies in excess of $5,000 or seeking an award in municipal court.

Should the District decide to obtain a judgment for money in small claims court, counsel is not necessary or allowed in the court room. However, the proceeding to obtain a writ of execution and subsequently an Earnings Withholding Order would necessitate counsel.

Once a money judgment has been obtained, the district should record an abstract of the judgment in the county and in any other county where the district believes the employee owns any real property. This ensures that the district may recover the judgment should the employee leave prior to satisfying the judgment. The district will then be paid in the event that the real property is sold or refinanced. The judgment is good for ten years and may be renewed when it expires.

Small Claims Court

Information, Forms and Claims

There are many forms that must be completed to file a Small Claims case. This procedure varies from County to County through out California and depending on the case; the district may need to file it at a particular court house in its County.

The good news is that all of this is outlined very well on the State of California web site at http://www.dca.ca.gov/publications/small_claims.

In addition to a court locater which is done by zip code, there is a question and answer section “The Small Claims Court-A Guide to its Practical Use”.

Sampling of Information on Site:

Basic Considerations and Questions

What Is Small Claims Court?

Small claims court is a special court where disputes are resolved quickly and inexpensively. In small claims court, the rules are simplified and the hearing is informal. Attorneys are generally not allowed. The person who files the claim is called the **plaintiff**. The person against whom the claim is filed against is called the **defendant**. They are also called **claimants or parties**. You don't need to be a United States citizen to file or defend a case in small claims court. If you are a non-English speaker, see Making the Best of Your Day in Court section for information on an interpreter.

In general, claims are limited to disputes up to $5,000. However, **natural persons** (individuals) can claim up to $7,500. Corporations, partnerships, unincorporated associations, governmental bodies, and other legal entities cannot claim more than $5,000. Also, no claimant (natural person or legal entity) may file *more than two* small claims court actions for more than $2,500 anywhere in the state during any calendar year. For example, if you file an action for $4,000 in February 2007 and another action for $4,000 in March 2007, you may not file any more actions for more than $2,500 until January 1, 2008. You may file as many as you wish for $2,500 or less.

The fee for filing in small claims court depends on the amount of the claim: 30 if the claim is for $1,500 or less, $50 if the claim is for more than $1,500 but less than or equal to $5,000, or $75 if the claim is for more than $5,000. However, if a plaintiff has filed more than 12 small claims in California within the previous 12 months, the filing fee for each subsequent case is $100. The filing fee is paid by the plaintiff to the clerk of the small claims court.

Since the limits on amounts of claims and filing fees may be changed by legislative action, you should check with your local small claims adviser or small claims clerk to determine the current limits on claims and filing fees. You may also consult with your own attorney if you wish.

Small claims courts can order a defendant to do something, as long as a claim for money is also part of the lawsuit. If you are suing to get back the lawn mower you loaned to a neighbor, for instance, the court can order the return of the mower, or payment for the mower if it is not returned.

Examples of other disputes that might be resolved in small claims court are:

- Your former landlord refuses to return the security deposit you paid.
- Someone dents your car's fender and refuses to pay for its repair.
- Your new TV will not work, and the store refuses to fix it or replace it.
- Your tenant caused damage to the apartment in an amount that exceeded the security deposit. (Note: You can't file an eviction action in small claims court.)
- You were defrauded in the purchase of a car, and desire to cancel the purchase and get back the amount of your down payment from the seller.
- You lent money to a friend, and he or she refuses to re-pay it.

In most small claims courts, cases are heard within 30-40 days after filing the plaintiff's claim, but they are never set for earlier than 20 days or more than 70 days after the claim is filed. Most cases are heard on weekdays, but some courts also schedule evening and Saturday sessions.

Is Small Claims Court Your Best Option?

Before filing a case in small claims court, it's important to decide whether going to small claims court is the best way to resolve your dispute. Many disputes can be resolved by using other dispute resolution methods, such as **mediation**. Many counties help resolve disputes informally through their local consumer affairs offices, or through local public or private dispute resolution or mediation programs.

You need to consider whether the defendant is legally responsible for the claim. Is the law on your side? If there is a law that applies to your case, the small claims judge must follow that law, interpreting it in a spirit of reasonableness and fairness to both parties. If the law isn't on your side, but you feel that justice is, you may get a more favorable result through voluntary mediation.

If you decide to file a small claims court case, be prepared to devote some time and effort to it. This includes preparing for the hearing, gathering evidence, meeting with witnesses, and attending the hearing in person.

You also may need to take action and spend money to enforce any **judgment**. While a small claims court judgment carries legal weight, it may be difficult or even impossible to **enforce** the judgment. Collecting a court judgment is one of the most challenging and frustrating aspects of any lawsuit. The person who is obligated to pay the judgment may not have the money to pay it, or may simply refuse to pay it. Enforcement procedures are available, but these require extra effort and also money on your part. It's possible that you will never collect anything.

In deciding whether to file a small claims case, remember that you may not **appeal**. By choosing small claims court to resolve your dispute, you give up the right to have a different judge re-hear the case. So if you should lose, that's probably the end of the case for you. If you win, the person or entity against whom you filed your claim (the defendant) may appeal the judge's ruling. In that situation, the entire dispute will be heard again, before a different judge.

Have You Tried to Settle the Dispute Yourself?

Have you and the defendant tried to resolve the dispute on a friendly basis? If you haven't done so before suing, why not try? At the very least, you should ask the defendant for the legal remedy that you hope the judge will award you.

Are you able to give the other person some incentive to perform? If he or she owes you money, you might consider offering to accept less than the full amount, if it's paid right away. If you owe money, it may be worth paying a bit more than you feel you owe, just to end the dispute. If the dispute goes to court and results in a judgment against you, the amount you owe may be increased by **court costs** and **interest**, and the judgment will be noted in your credit record.

If there's no dispute about the amount you owe, but you simply can't pay the entire debt at one time, consider offering to make monthly or weekly payments until the debt is paid. (Even after the case is decided, the judge can authorize you to pay the judgment by weekly or monthly payments.)

Have You Considered Mediation?

Mediation is a process for resolving disputes informally. A third party —a *mediator*—helps the parties arrive at their own solution. Unlike a judge, a mediator doesn't issue a decision. The best quality of the mediation process is that it attempts to restore the relationship between the parties. While only some disputes can be resolved by mediation (since both parties must agree to the results), consider whether your dispute can be resolved in that way. Disputes involving neighbors and family members are particularly well suited for mediation because of the importance of the relationships between the parties.

If you decide that mediation (rather than small claims court) might resolve the dispute, ask the clerk if the small claims court offers a mediation program. If not, the clerk may know of a publicly funded program in your county. You can also locate a mediation program by looking in the business section of your telephone directory, or by calling the California Department of Consumer Affairs at 1-800-952-5210. Hearing-impaired persons may call 1-800-322-1700 (TDD) or 916-322-1700 (TTY).

Where Can You Obtain More Information and Advice?

- **Small Claims Adviser -** Small claims advisers provide free individual personal advisory services to small claims **disputants**. The law requires each county to provide a small claims advisory service. Some advisers are available only by phone, while others may be visited in an office setting. Some advisory services provide recorded advice by phone. All small claims advisers provide information regarding the procedural rules, and some will also assist you in preparing your case. To locate your local small claims adviser, contact the local small claims clerk or look in your telephone directory. The small claims advisory services of all counties are listed in the websites of the Department of Consumer Affairs at www.dca.ca.gov, and of the Judicial Council at www.courtinfo.ca.gov/selfhelp/smallclaims/scbycounty.htm.

- **Publications -** Small claims court procedural rules are summarized and explained in a Department of Consumer Affairs publication entitled *Consumer Law Sourcebook: Small Claims Court Laws & Procedures.* Consumer laws are summarized in Consumer Law Sourcebook: Consumer Law (forthcoming). While the Consumer Law Sourcebooks are written principally for judges and small claims advisers, some disputants find them useful. Most county law libraries make reference copies available to the public. Your county law library may also have books on the subject of your claim. Materials published by the Department of Consumer Affairs can be ordered from its Consumer Information Center at 800-952-5210, or its Policy and Publications Development Office at 866-320-8652 or 916-574-7378. If you have access to a computer, you can print a copy of The Small Claims Court: A Guide to Its Practical Use (this handbook) by visiting the website of the Department of Consumer Affairs at www.dca.ca.gov.

- **Internet Resources -** The internet offers countless sources of information. If you don't have access to the internet at home, visit your public library. The Judicial Council's self-help websites offer assistance in both English and Spanish: English — www.courtinfo.ca.gov/selfhelp/smallclaims/ (California Courts Self Help Center) Spanish — www.courtinfo.ca.gov/selfhelp/espanol/ (Centro de Ayuda de las Cortes de California)

- Court forms can be viewed and printed at the Judicial Council's self-help websites listed above. The websites also include a list of certified interpreters. If you are the plaintiff, reviewing the following court forms is likely to provide useful information: ***Information for the Small Claims Plaintiff*** (Form SC-150), and ***Plaintiff's Claim and Order to Go to Small Claims Court*** (Form SC-100).

- If you are the defendant, reviewing the following court forms is likely to provide information useful to you: ***Information for the Defendant*** (Form SC-100 (page 4)), and ***Defendant's Claim and Order to Go to Small Claims Court*** (Form SC-120).

- The following websites provide access to federal and California statutes and regulations: federal statutes — www.gpoaccess.gov/uscode/search.htmlCalifornia statutes — www.leginfo.ca.gov federal regulations — www.regulations.govCalifornia regulations — www.calregs.com

- The Department of Consumer Affairs provides fact sheets and information on landlord-tenant issues, auto repairs, contractor hiring, and the professions and occupations regulated by the department on its website at www.dca.ca.gov.

- Links to websites designed to help persons who represent themselves in court actions are listed at www.publiclawlibrary.org/help.html. Links to other information resources are provided in the website of *Consumer Reports* magazine.

- **Attorneys -** An attorney may be able to advise and assist you before or after filing your claim. You should consult an attorney if you feel it would be cost-effective to do so, considering the size of the claim and the kinds of issues involved. You can't have the attorney represent you in court. Except in rare instances, fees charged by the attorney for private assistance are not recoverable as *court costs or damages*. For a list of lawyer referral services, go to the website of the State Bar of California. If you can't afford an attorney, a legal services program might be able to help. Legal services programs for low-income persons are listed at www.Lawhelpcalifornia.org/CA/.

Who Can File or Defend a Claim?

With certain exceptions, anyone can sue or be sued in small claims court. Generally, all parties must represent themselves. A person or an entity (for example, a corporation) that files a small claims action is called the plaintiff. The party who is sued is called the defendant.

An individual can sue another individual or a business, but may not file a claim against a federal agency. A business, in turn, can sue an individual or another business. However, an **assignee** (a person or business that sues on behalf of another, such as a collection agency) can't sue in small claims court.

To file or defend a case in small claims court, you must be (a) at least 18 years old or legally emancipated, and (b) mentally competent. A person must be represented by a **guardian ad litem** if he or she is under 18 and not legally emancipated, or has been declared mentally incompetent by a court. For a minor, the representative is ordinarily one of his or her parents. A small claims clerk or small claims adviser can explain how to have a guardian ad litem appointed.

If the court determines that a party is unable to properly present his or her claim or defense for any reason, the court may allow another individual to assist that party. The individual who helps you can only provide assistance — the individual's participation in court cannot amount to legal representation, and the person can't be an attorney.

Can Someone Else Represent You?

In most situations, parties to a small claims action must represent themselves. As a general rule, attorneys or non-attorney representatives (such as debt collection agencies or insurance companies) may not represent you in small claims court. Self-representation is usually required. There are, however, several exceptions to this general rule:

- **Corporation or other legal entity** — A corporation or other legal entity (but not a natural person) can be represented by a regular employee, an officer, or a director, and a partnership can be represented by a partner or regular employee of the partnership, but the representative may not be an attorney or person whose only job is to represent the party in small claims court.

- **Property agent** — A property agent may represent the owner of rental property if the property agent was hired principally to manage the rental of that property and not principally to represent the property owner in small claims court and the claim relates to the rental property. At the hearing, the agent should tell the judge that he or she was hired and is employed principally to manage the property, or this statement may be in a written declaration. A common interest development also may appear and participate in a small claims action through an agent.

- **Sole proprietorship** — In a case in which a claim can be proved or disputed by evidence of an account that constitutes a business record, and there is no other issue in the case, a sole proprietorship (such as a physician) can be represented by a regular employee who is employed for purposes other than solely representing the proprietor in small claims court actions, and who is qualified to testify to the identity and mode of preparation of the business record. In that situation, the employee must be able to testify that (1) the evidence of the account was made in the regular course of business, (2) the evidence of the account was made at or near the time of the transaction, and (3) the sources of the information about the account and its time and method of preparation are such as to indicate their trustworthiness.

- For example, this exception to the general rule of self-representation might permit a dentist's bookkeeper to represent the dentist in an action to collect a patient's account. However, if the patient alleged that the dentist's services were unnecessary or performed poorly, the case would involve another issue of fact, and the dentist would need to appear at the hearing in person. As in all actions to collect debts and accounts, the plaintiff's claim form must include an itemization of all fees and charges that have been added to the original loan amount or agreed price.

- In the following kinds of situations, a party need not appear in court, and may either send a representative or submit written declarations to prove his or her claim or **defense**. However, the representative can't be compensated, and is disqualified if he or she has appeared in small claims actions as a representative of others four or more times during the calendar year.

- **Non-resident real property owner -** A non-resident owner of real property located in California may defend a small claims case related to the property by submitting a declaration or sending a representative.

- **Military service -** A person who is on active duty in the military service outside California, or who while on active duty is transferred out of state for more than six months after the claim arose, may be represented by a non-attorney, and may submit declarations in support of his or her claim or defense. For instance, a tenant who is on active duty, and is transferred out of state for more than six months, can ask a qualified person to file a small claims action on behalf of the tenant to recover a security deposit from a landlord, and to represent the tenant at the hearing.

- **Jail or prison -** A person who is in jail or prison may be represented by someone who isn't an attorney, and may file written declarations in support of his or her claim or defense.

- **Non-resident driver involved in an in-state auto accident -** Some courts will allow a non-resident driver involved in an in-state auto accident to send a representative (but never an attorney), submit evidence by declaration, and appear in court by telephone. Contact a small claims adviser in the county where you're sued to learn about the procedures used in that county.

An individual who represents a party to a small claims court action must complete and sign an Authorization to Appear on Behalf of Party (Form SC-109) — a form provided by the clerk of the small claims court or printed at the Judicial Council's self-help website. The representative must state that he or she is actually authorized to represent the party, and he or she also must describe the basis for that authorization, such as a letter from the represented party. If the represented party is a corporation or other legal entity or an owner of real property, the representative also must state that the representative isn't employed solely to represent the corporation or entity in small claims court. In the other situations listed above, the representative must state that the representative is acting without compensation, and hasn't appeared as a representative in small claims actions more than four times during the calendar year.

Can Your Spouse Represent You?

Spouses may represent each other in small claims court if they have a joint interest in the claim or defense and the represented spouse has given his or her consent. However, one spouse may not represent the other spouse if the court decides that justice would not be served — such as where their interests are not the same and may conflict. The represented spouse need not come to court if the judge allows representation.

STATE OF CALIFORNIA
dca
DEPARTMENT OF CONSUMER AFFAIRS

I Need To:

- Read the California Tenants Book
- Locate the Small Claims Court Guide
- Find a Press Release
- Search for Publications

Small Claims Court Checklist

Before the Hearing -
For the Plaintiff

1. Contact the other party to discuss the issues and try to resolve the problem.
2. Offer to resolve the problem by mediation or other informal dispute resolution methods.
3. Familiarize yourself with small claims court procedures. Read this handbook. Talk to a small claims adviser. Attend a court session.
4. Determine the exact amount in dispute, and how it's calculated.
5. Identify a court where venue is proper.
6. File a Plaintiff's Claim and Order to Go to Small Claims Court (Form SC-100), and pay the filing fee. If you're a business, also file a Fictitious Business Name [Declaration] (Form SC-103) if appropriate.
7. Arrange for service of process on each defendant sufficiently in advance of the hearing as required. Make sure that the Proof of Service (Small Claims) (Form SC-104) is completed and returned to the court the required number of days before the hearing.
8. Prepare for the court hearing. Organize your thoughts. Collect evidence. Talk to witnesses.

9. Keep communication open. Try to resolve the dispute with the other party before the hearing.
10. Attend the hearing and present your case.

Before the Hearing -
For the Defendant

1. Determine whether you may be legally obligated to pay the claim, and, if so, why. Consult a small claims adviser or an attorney to determine how much, if anything, you owe.
2. Contact the plaintiff to discuss the issues and try to resolve the dispute.
3. Suggest or agree to try mediation or some other informal dispute resolution method.
4. Familiarize yourself with small claims court procedures. Read this handbook. Talk to a small claims adviser. Attend a court session.
5. If you have a claim against the plaintiff, consider asking the court to resolve it at same hearing. (Complete and file a Defendant's Claim and Order to Go to Small Claims Court (Form SC-120).)
6. Prepare for the court hearing. Organize your thoughts. Collect evidence. Consult witnesses.
7. Keep communication open. Try to resolve the dispute before the hearing.
8. If you and the other party haven't met and discussed the claim, ask the court to postpone the hearing to let you and the other party meet and resolve the dispute informally if you can.
9. If you owe something, try to pay it, or to work out a payment plan before the hearing.
10. Try to avoid having a court judgment entered against you, since it probably will appear on your credit record for a long time, even after you've paid it.
11. Attend the hearing and present your defense.

After the Hearing -
Plaintiff and Defendant

1. Read the Notice of Entry of Judgment (Form SC-130) that you have received from the small claims court. It tells you and the other party how the judge ruled. If you discover an error in the judgment, you may file a Request to Correct or Vacate Judgment (Form SC-108). Either a plaintiff or a defendant may file such a request.
2. If either of the parties was unable to attend the hearing for good cause, the party who did not appear may file a Notice of Motion to Vacate Judgment (Form SC-135) to request a new hearing in the small claims court.
3. Judgment debtor - If the other party asserted a claim asserted against you, and you appeared at the hearing, and the judge decided against you, and there is good reason for you to believe that the judge made a mistake, you may file a Notice of Appeal (Form SC-140) to obtain a new hearing before a different judge.
4. Judgment debtor - You may comply with the judgment (for instance, by payment to the judgment creditor or the court). If you can only make weekly or monthly payments, the court probably will issue an installment payment order if you request it by filing a Request to Pay Judgment in Installments (Form SC-106).
5. Judgment debtor - If you haven't paid the judgment in full within 30 days after receipt of the Notice of Entry of Judgment (Form SC-130), complete the Judgment Debtor's Statement of Assets (Form SC-133) that accompanied the Notice of Entry of Judgment (Form SC-130) and send it to the judgment creditor.
6. Judgment debtor - After the judgment creditor has received full payment, make sure that the judgment creditor files an Acknowledgment of Satisfaction of Judgment (Form EJ-100) with the small claims court.

Judgment creditor - File an Acknowledgment of Satisfaction of Judgment (Form EJ-100) with the court when the judgment debt is paid or take steps to collect the judgment.

Collection Agencies

Are They For Your District?

If your letter writing, personal meetings, and phone calls have all failed to resolve the overpayment issue, perhaps it's time to use a professional.

The district can contract with a collection agency and use their services to collect its overpayments.

The cost to the district will vary depending on the volume of business and the amount of debt that is to be collected.

How Do Agencies Make Money?

Collection agencies often work on commission, where they receive a percentage of the amount they collect. Individual collectors are often paid a low base wage plus commissions based on their personal performance.

How Do Agencies Work?

A collection agency will take many of the same actions as the district such as letter writing and phone calls. However, collectors are aided by specialized phone systems, computers, and software designed to automate the process and make it more effective and cost efficient in retrieving payments.

Agencies try to create a sense of urgency, in order to collect within the shortest amount of time, and to encourage the employee to prioritize this particular obligation.

Of particular interest to the district, a collection agency will always encourage the employee to contact them directly to resolve the overpayment issue.

How Will the Employee be Affected?

Many times by the simple act of receiving a letter or a phone call from a third party collection agency, the employee will be motivated to repay the overpayment.

Of concern to the employee should be:

- ☹ A collection agency can report the overpayment (debt) to one or more of the credit bureaus as a "collection account", including the amount owed and whether or not it was paid.
- ☹ Paying off the debt will not result in the item being removed from the employee's credit reports. It will simply be marked as "paid".
- ☹ A collection agency can request the employee's credit report in order to obtain information of the employee's financial situation and to get an updated address and phone number.
- ☹ Collection accounts are subject to the normal 7 year time limit for appearing on credit reports. As specified in Section 605 of the Fair Credit Reporting Act, this time limit is based on the date of the original delinquency.

How is the Employee Protected?

- ⃠ Collection agencies can not legally seize the employee's assets, bank accounts, or paycheck unless there has been a successful lawsuit with an awarded judgement.
- ⃠ Collection agencies can not legally get an employee terminated from their employment.
- ⃠ Collection agencies can not legally make any kind of public announcements or disclosures concerning the debt, except to the credit bureaus.

Reporting Requirements

The district should always try and recover an overpayment of wages in the same tax year in which they were overpaid as a W-2c will not be required.

If the overpayment is recovered in the same tax year in which it was overpaid, treat as an abatement of wages.

☑ Adjust employee's reported wages and taxes withheld (if applicable) for:

- o Federal
- o State
- o Social Security
- o Medicare

☑ Report the adjustments on Form 941 for the quarter during which the repayment occurred.

Special rules apply when overpayments are collected for prior calendar years.

☑ File a form W-2c to adjust Social Security & Medicare wages if the overpayment is repaid within 3 years of April 15th following the year of the original payment date.

- o Complete the W-2c with the tax year in which the overpayment was made to the employee.
- o The employee will file Form W-2c in the year in which the overpayment is repaid.

☑ Refund the employee the overpayment of Social Security & Medicare taxes as calculated.

- o Obtain an affidavit from the employee stating receipt of the monies and that no further claim for such monies will be requested from the IRS on the employee's tax returns.

- ☑ Complete form W-3c to accompany form W-2c for filing with Social Security Administration.

- ☑ Complete form 941c to reconcile Forms W-2, W-2c, W-3, and W-3c amounts.

If the overpaid wages are not paid back in the same year issued, an adjustment on form W-2c is not allowed for boxes 1 and 2.

This is because the employee received and had use of those funds during that year. The employee is not entitled to file an amended return (form 1040X) to recover the income tax of these wages.

Instead, the employee is entitled to a deduction (or credit in some cases) for the repaid wages on their income tax return for the year of repayment.

Form 843, Claim for Refund and Request for Abatement, may be used to apply for a refund when the district has paid more federal income taxes than what was withheld from the employee.

- ☑ Attach form 843 to the 941c where the adjustment was reported in part 2.

- ☑ The district cannot adjust the amounts reported as income tax after the calendar year it was reported unless it was not withheld from the employee and the correction is just and administrative adjustment.

For more information, please visit websites:

- www.irs.gov

- www.edd.ca.gov

Print Form | Submit by Email

PAYROLL COMMITTEE **2008 CASBO ANNUAL CONFERENCE**

WORKSHOP EVALUATION FORM ANAHEIM, CALIFORNIA

Workshop Session Date & Time 04/27/08 2:30 - 3:30

Pay14 Legal Aspects of Handling Employee Overpayments

Yes, I am interested in becoming a member of a committee. Please contact me at:

Name: District County

Phone# Email Address:

Please rate this workshop on each of the following:

		Select only one					
		N/A	Poor	Fair	Good	Average	Excellent
1	Were session objectives clearly communicated?	0	1	2	3	4	5
2	Was the session interesting?	0	1	2	3	4	5
3	Was the presentation easy to follow?	0	1	2	3	4	5
4	Was there adequate opportunity for audience participation?	0	1	2	3	4	5
5	Were handouts available or offered electronically?	0	1	2	3	4	5
6	What was your overall rating of this session?	0	1	2	3	4	5
7	What was your overall evaluation of the presenter(s)?	0	1	2	3	4	5
8	Were the visual aids effective?	0	1	2	3	4	5
9	Should this topic be presented again at future conference?	0	1	2	3	4	5

We welcome your comments on this workshop. Place any comments regarding this workshop in the space provided and check the box for comments. If you have any suggestions for a topic to be presented at a future conference place a check under suggestions along with your topic idea in the space provided.

Comment ☐ Suggestion ☐

_____
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