



County of Santa Cruz

COUNTY ADMINISTRATIVE OFFICE

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SUSAN A. MAURIELLO, J.D., COUNTY ADMINISTRATIVE OFFICER

January 23, 2002

AGENDA: January 29, 2002

Board of Supervisors
County of Santa Cruz
701 Ocean Street
Santa Cruz, California 95060

Status of County Deferred Compensation Plan

Dear Members of the Board:

At your Board's December 11, 2001 meeting, your Board adopted a resolution modifying the County of Santa Cruz Deferred Compensation program by implementing the changes in compensation limits enacted through the federal Economic Growth and Tax Relief and Reconciliation Act of 2001 (EGTRRA). At that time, you also directed the Commission to return by today's meeting with a revised Deferred Compensation Plan for your consideration.

Status of EGTRRA Implementation

As your Board is aware, EGTRRA implemented a number of changes to both government and private employee programs (457 plans, IRAs and 401(k) plans). The changes which have received the most notice are those which increase the amount of compensation which can be deferred. However, the legislation also made a number of other changes, such as allowing deferred funds to be used to purchase service credits, allowing transfer of funds between 401(k) and 457 and other deferred compensation plans, and simplification of the distribution options at time of separation and for immediate distribution following a divorce.

The December letter mentioned the concern that the increased limits for deferred compensation adopted by the federal government may not be in effect in California for state income tax purposes under the present California Revenue and Tax Code. It has now been determined that California regulations, like those of sixteen other states and the District of Columbia, do not conform with the federal regulations.

At this time, the results of non-conformity between EGTRRA and the California Revenue and Taxation Codes are unclear. The California State Association of Counties has expressed the opinion that the most likely risk for implementing EGTRRA now is that a portion of the compensation amounts deferred in conformance with Federal tax laws could be considered taxable by the California Franchise Tax Board to the extent that they exceed current State law. However, CALPERS has issued the opinion that implementing some of the EGTRRA provisions could potentially jeopardize the tax-qualified status of the entire plan and all of its participants.

In light of these conflicting opinions, it is the recommendation of the Deferred Compensation Advisory Commission that the County not take further action at this time. The Auditor-Controller has established both state and federal maximum limits in the County payroll system for regular deferrals and for catch-up provisions in accordance with the limits approved by your Board on December 11, 2001. Each employee master record contains the annual dollar limit the individuals can defer under the federal law. The dollar limit is determined by whether the employee is taking a regular deferral or exercising one of the catch-up provisions. When an employee's cumulative annual deferrals reach the state limit, the payroll system will compute, deduct and track the state withholding amounts on the amount in excess of the state limit. The result is that the County is able to track and withhold state taxes on the difference between the state and the federal deferral limits. If the state adopts partial or total conformity with the federal law, it will be simple for the County's programmers to change or eliminate the state limits. The Advisory Commission has implemented a procedure in which all employees who request distribution documents are required to meet with the Great West representative to ensure that they are fully informed as to the tax consequences of any actions taken at this time.

On January 10, 2002, the Governor's budget was released, and the summary indicates that the Governor is proposing to bring the State's tax law into closer conformity with Federal law by adopting a number of critical changes made in EGTRRA. At this time, it is unknown which EGTRRA provisions are included in the Governor's budget. In addition, Senate Bill 657 and Assembly Bill 1743 have been introduced to bring California into full conformity with Federal limits. This office and the County's Deferred Compensation administrator are monitoring both of these bills.

The California State Association of Counties, the League of California Cities and other employer groups are taking action to express support of conformity legislation to the Legislature. Letters urging full conformity have been submitted by Mr. Gary Knutson, Santa Cruz County Auditor-Controller in his capacity as the president of the County Auditors Association of California, and by Mr. Richard Bedal, the County Treasurer-Tax Collector. The Deferred Compensation Advisory Commission recommends that your Board join in this effort by sending letters supporting full conformity to our locally elected officials and to the State Committees on Revenue and Taxation.

County Deferred Compensation Plan Document

As mentioned in the December 11, 2001 letter, the County's Deferred Compensation contractor, Great West/BenefitsCorp, offers a service to its contracting jurisdictions in which Great West provides a Model Plan Document which complies with all federal regulations. The Deferred Compensation Advisory Commission has evaluated the Model Plan document and believes that it would be advantageous to the County to utilize this document as the basis for the County's Deferred Compensation plan.

However, it is recommended that this decision be deferred until the issue of federal non-conformance has been resolved.

IT IS THEREFORE RECOMMENDED THAT YOUR BOARD

- 1). Send letters supporting full conformity with EGTRRA to our locally elected officials and to the State Committees on Revenue and Taxation, and
- 2). Direct the County Administrative Officer to return with recommendations regarding the County's Deferred Compensation program when additional information on State conformance is available.

Very truly yours,



Susan A. Mauriello
County Administrative Officer

cc: Members of Deferred Compensation Advisory Commission
Brion Beetz, Great West/BenefitsCorps

SAM/DP