

# 10. Tax Information and Legal Matters

## Income Tax Withholding

Federal and California law requires income tax withholding on distributions from pension plans, annuities and deferred compensation plans. We will withhold income tax from the taxable portion of your benefit unless you take action not to have taxes withheld. To do that, you must file an *Income Tax Withholding Preference Certificate* with us. One is included as part of the *Service Retirement Application*. You can also download the certificate at [www.CalSTRS.com](http://www.CalSTRS.com) or order it by calling 800-228-5453.

If you do not have taxes withheld or if you do not have enough taxes withheld, you may need to make estimated tax payments. Generally, your withholding or estimated tax payments or the total of both must cover at least 90 percent of your total tax liability for the current year. Failure to meet the 90 percent limit could subject you to penalties.

You can view your current tax withholding elections on *myCalSTRS* at [www.CalSTRS.com](http://www.CalSTRS.com).

A portion of your benefit may not be taxable if you made previously taxed contributions to CalSTRS during your career. CalSTRS uses the Simplified Method established by the IRS to determine the taxable portion of your benefit. You may use any acceptable method when reporting to the IRS. For details on the Simplified Method, see *Pension and Annuity Income*, IRS publication 575, available at [www.irs.gov](http://www.irs.gov) or refer to *Pension and Annuity Guidelines*, FTB publication 1005, from the California Franchise Tax Board at [www.ftb.ca.gov](http://www.ftb.ca.gov).

## Periodic Payments

Unless you tell us otherwise, we will withhold income tax on your periodic payments—payments received in installments at regular intervals—as if you were married and claiming three dependents. To change this withholding, see the information on how to file an *Income Tax Withholding Preference Certificate* on page 86.

## Nonperiodic Payments

CalSTRS withholds income tax from nonperiodic payments such as a partial lump sum, one-time death benefit or the benefit accrued



and unpaid on the date of death of a CalSTRS benefit recipient. Withholdings from nonperiodic payments are set at a flat rate of 20 percent for federal and 6 percent for state. Your beneficiary can elect not to have state taxes withheld from a nonperiodic payment unless he or she resides outside of the United States or its possessions, in which case tax withholding is required. Federal taxes must be withheld unless the payment is a rollover.

### **Income Tax Withholding Preference Certificate**

To request a change to your income tax withholding status, you must complete the CalSTRS *Income Tax Withholding Preference Certificate* form. CalSTRS must receive this form no later than the first day of the month preceding the month you wish the change to take effect. You can download or order the form at [www.CalSTRS.com](http://www.CalSTRS.com) or request a copy by calling 800-228-5453.

### **Lump-Sum Distributions**

If you receive a lump-sum distribution, including a refund of your contributions, you should be aware that the Internal Revenue Code includes several complex rules regarding tax and penalties on distributions. You may be eligible to defer tax liability on the taxable amount of the distribution by rolling over that amount into another qualified retirement plan or IRA.

To take advantage of these rollover provisions, the distribution must be made by a trustee-to-trustee transfer. For more information on rollovers, see the CalSTRS *Tax Considerations for Rollovers* brochure. You can download or order the brochure at [www.CalSTRS.com](http://www.CalSTRS.com) or order it by calling 800-228-5453.

### **Tax Withholding for Out-of-State Residents**

Under federal law, if you are not a resident of California, you are not subject to California state tax. However, CalSTRS benefits may be subject to taxation in the state where you live. CalSTRS cannot withhold taxes for another state.

CalSTRS will not withhold California state income taxes for benefit payees who live outside California unless the payee files the *Income Tax Withholding Preference Certificate*.

You should consult a qualified tax professional for specific tax advice. You should contact the IRS, the California Franchise Tax Board or a qualified tax advisor for information relevant to your individual situation. For general information on withholding tax from CalSTRS benefits, go to [www.CalSTRS.com](http://www.CalSTRS.com) or call 800-228-5453.

### **Internal Revenue Codes Affecting Benefits**

#### **Section 401(a)(9)**

Internal Revenue Code section 401(a)(9) and the California Education Code both require CalSTRS to begin a distribution of your benefits no later than April 1 of the calendar year following the year you reach age 70½.

CalSTRS will not be required to begin distribution of your account if:

- You are currently employed in a position subject to coverage under CalSTRS.
- Your current employment is covered by, or you are retired from, another public retirement system. For a listing of other public retirement systems, see [Retiring From More Than One Public Retirement System in Section 6](#).

Annually, CalSTRS attempts to notify members who may be affected by these statutory provisions. Therefore, it is important we have your current mailing address at all times.

#### **NOTE**

The IRS may impose an excise tax equal to 50 percent of the minimum required distribution if you receive less than the minimum-required distribution for a taxable year. Refer to the IRS or your tax professional for details.

#### **Section 401(a)(17)**

Internal Revenue Code section 401(a)(17) limits the compensation that can be used to provide a benefit by a governmental plan such as CalSTRS. The compensation limit applies to everyone who became a member or participant of CalSTRS on or after July 1, 1996.

The compensation limit is \$230,000 for the 2008-2009 plan year and \$245,000 for the 2009-2010 plan year. Any compensation in excess of this limit is not creditable compensation, and neither employer nor member contributions to the Defined Benefit Program, the Defined Benefit Supplement Program or the Cash Balance Benefit Program should be paid to CalSTRS on the excess amount.

### **Section 415**

Internal Revenue Code section 415 limits the benefits that can be paid by a state or local government defined benefit plan such as that administered by CalSTRS. Benefits are limited to an absolute dollar amount that is indexed for inflation. If you choose to receive a lump-sum payment, your service retirement will no longer qualify as a joint and survivor annuity under Internal Revenue Code section 415, and it may therefore exceed the section 415 benefit limit. For calendar year 2009, the dollar limit is \$195,000 at ages 62 through 65. The limit is lower below these ages and higher above these ages.

Currently, few CalSTRS members have been, or are likely to be, affected by the limits of section 415. Once we receive your *Service Retirement Application*, we will notify you if your benefit will be affected by the section 415 benefit limit. Consistent with federal law, CalSTRS has established the Replacement Benefits Program from which benefits in excess of the section 415 limits can be paid. If your benefit is limited by section 415, you will receive a separate payment from the Replacement Benefits Program in addition to the limited benefit.

## **Legal Matters**

### **CalSTRS Right to Recover Costs**

When a third party causes the injury or death of a CalSTRS member before retirement and the member or family pursues civil litigation, CalSTRS must be informed. We have a right to recover an amount equal to the actuarial equivalent of benefits paid under the plan because of the injury or death of the member. The process that permits this participation is called subrogation.

### **Power of Attorney**

You can arrange to have your assets managed by a third party through a power of attorney. We can provide you with some of the necessary forms.

When a CalSTRS benefit payee becomes incapacitated and can no longer manage his or her financial affairs, we may need to determine who has the legal authority to act on the payee's behalf regarding the payee's CalSTRS account and benefits. That authority could extend to changing the recipient's address, instituting or changing direct deposit authorizations and changing tax withholding preferences.

A durable power of attorney is the most common method used by a benefit payee to delegate authority to act for the payee. This document permits a benefit payee to act as a principal and appoint an agent. The document also identifies the extent of authority granted to the agent.

A durable power of attorney can be drafted by an attorney or purchased as a commercially available fill-in-the-blank form. CalSTRS has a *Special Power of Attorney* form available. This form enables your named agent to handle all matters pertaining to a CalSTRS account, unless barred by law.

In addition, we require an agent to execute an affidavit affirming the agent's authority under the durable power of attorney. For the agent's convenience, the CalSTRS form, *Declaration of Attorney in Fact*, can be completed by the agent each time he or she makes a request.

You can download a *Special Power of Attorney* or a *Declaration of Attorney in Fact* form at [www.CalSTRS.com](http://www.CalSTRS.com) or call 800-228-5453 to request a copy.

### **Your Rights— The Appeal Process**

Any party who disagrees with a decision by CalSTRS staff at any level may request review of that decision by higher authority. These rights and the procedure will be provided early in the written correspondence and may be found at [www.CalSTRS.com](http://www.CalSTRS.com) (select FAQ under *Tools*). The following is a brief

description of the appeal process. It is not intended to take the place of the law or the detailed written procedures.

### **Requesting an Executive Review**

If you disagree with the initial decision from CalSTRS, you may request an Executive Review to review this decision. The Executive Review Committee, which is typically the final level of review within CalSTRS, is made up of members of the executive staff, program managers and staff, the Ombudsman and general counsel staff. The committee reviews the situation based upon any additional information you provide, the law and facts and prepares a written analysis and decision.

### **Requesting a Hearing**

To appeal the Executive Review Committee's decision, you may request an administrative hearing, which will be held before an independent administrative law judge employed by the Office of Administrative Hearings. The request for a hearing must be made within 90 days from the date of the committee's response.

The Office of Administrative Hearings schedules the hearing and notifies all parties regarding the time, date and location. The hearing is a full evidentiary hearing, meaning witnesses may be called. CalSTRS may be represented by the state attorney general or may use in-house counsel. You may be represented by an attorney or you may represent yourself. Following the hearing, the administrative law judge will submit a Proposed Decision to CalSTRS. Within 30 days CalSTRS will provide all parties with a copy of the Proposed Decision.

### **Proposed Decision and Further Action**

The Proposed Decision of the administrative law judge is not the final decision. The Teachers' Retirement Board must decide whether or not to adopt the Proposed Decision within 100 days of receiving it. The Teachers' Retirement Board's Appeals Committee has the final authority to act on behalf of the board in these matters. When you receive your copy of the Proposed

Decision, you will be given the date that the Appeals Committee will act on your case, what the staff is recommending and how you may submit further written argument.

Sometimes the Appeals Committee does not adopt the Proposed Decision and orders that the matter be returned to the administrative law judge for further hearing or brought back before the Appeals Committee for hearing at a later meeting based upon the record, including the transcript, with or without taking additional evidence. If heard by the Appeals Committee, it will make its own independent decision after hearing arguments from both sides.

If you are dissatisfied with the Appeals Committee's decision, you may ask the committee to reconsider its decision or you may appeal to Superior Court. You will be notified of this right when you receive your copy of the Appeal Committee's decision shortly after the hearing takes place.

### **Community Property Information**

If you have been divorced or have terminated your registered domestic partnership, or you are presently going through a divorce or termination, your spouse or partner may have a community property interest in your CalSTRS benefits. You may need to refer to your settlement agreement or contact an attorney for legal advice on how your benefits may be affected.

The designation of any additional beneficiaries named on your *One-Time Death Benefit Recipient* form remains valid. However, a court order may specify that a former spouse or partner has an entitlement to certain death benefits.

If you choose to have your former spouse as your one-time death benefit recipient, you must submit a new *One-Time Death Benefit Recipient* form after your final dissolution judgment. For information about how CalSTRS benefits are affected by divorce or legal separation, refer to the CalSTRS *Community Property Information* brochure. To order or view this brochure, visit [www.CalSTRS.com](http://www.CalSTRS.com) or call 800-228-5453.