



ADMINISTRATIVE SERVICES DEPARTMENT

CITY HALL
10300 TORRE AVENUE • CUPERTINO, CA 95014-3255
TELEPHONE: (408) 777-3220 • FAX: (408) 777-3109
CUPERTINO.ORG

CITY COUNCIL STAFF REPORT

Meeting: January 18, 2022

Subject

Consider approving the attached addendum to the Memoranda of Understanding between the City of Cupertino and the Cupertino Employees Association (CEA)/IFPTE Local 21 and Operating Engineers Union Local No. 3 (OE3) AFL-CIO, for the period of July 16, 2019 to June 30, 2022 adding a City-sponsored Section 125 Premium Only (POP) Plan and modifying existing leave sell-back provisions in compliance with IRS “constructive receipt” doctrine.

Recommended Action

Approve the attached addendums to adopt a City-sponsored Section 125 Premium Only (POP) Plan and modify existing leave sell-back provisions in compliance with IRS “constructive receipt” doctrine.

Description

As part of a review of the City’s labor agreements by the City’s former contract City Attorney, both the need for a POP plan and compliance with constructive receipts was brought to staff’s attention. Staff has met and conferred with the City’s bargaining units since that time to reach agreement on the attached side letters.

As a result of these meetings, language was added and/or revised to the existing MOU’s and side letter agreements were reached. Staff requests Council’s approval to include these side letters as an amendment to the current MOU’s.

City-Sponsored Section 125 POP Plan:

As part of the most recently negotiated labor contracts, the City began to offer a cash-in-lieu benefit to CEA/IFPTE Local 21 and Unrepresented employees. This allowed employees with proof of other healthcare coverage to be paid cash in lieu of \$350 per month for waiving healthcare coverage with the City. The additional in lieu dollars were offset by savings the City achieved due to lower healthcare expenses. In order to comply with IRS rules related to in lieu health benefits, as well as to maintain pre-tax treatment for both City premiums and employee out-of-pocket contributions, the City needed to enroll in Section 125 Premium Only Plan. In part, Section 125 of the IRS revenue code states that to the extent any City premium contributions or employee out-of-pocket costs

for premiums are eligible for pre-tax treatment under Section 125 of the Internal Revenue Code, the City and all participating employees shall pay their respective share of the cost of medical, dental, vision, and short and long term disability insurance through a City-sponsored Section 125 Premium Only Plan (POP).

Leave sell-back provisions:

The IRS considers income to be received for tax purposes if the individual actually receives it or has an option to receive it during each tax year. This is known as the constructive receipt doctrine. Application of the constructive receipt doctrine to the City's sell back of leave provisions would mean that any annual leave subject to sell-back would have to be taxed as it is earned because the City's program allows the employee an unimpeded option to take this leave as cash rather than take the time off. Leaves impacted by this doctrine include vacation, administrative leave, and compensatory time off.

However, IRS Regulations also provide that the constructive receipt doctrine will not apply if an individual's control over the receipt of income is subject to substantial limitations or restrictions. Several private letter rulings have held that income is not constructively received as annual leave accrues if an individual has made an irrevocable election before the tax year in which it accrues to receive only a designated portion of this annual leave as cash.

Relying on these private letter rulings as an indication of how the IRS would view the City's sell-back of leave provisions, the City has proposed, and the bargaining units have agreed to modify the program prospectively to comply with IRS Regulations.

The side letter agreements will be incorporated into the next Memoranda of Understanding between the City and CEA/Local 21 and OE3.

Sustainability Impact

No sustainability impact.

Fiscal Impact

Fiscal impact for the POP Plan is a onetime set up fee of \$284 and annual maintenance fee of \$99. These costs can be absorbed into the existing Human Resources budget this fiscal year and will be added as ongoing costs to the program budget. (100-44-400) page 329 of the final budget document as part of the Fiscal Year 2022-23 Proposed Budget. There is no fiscal impact to modify the existing sell back provisions.

Prepared by: Vanessa Guerra, HR Manager

Reviewed by: Kristina Alfaro, Director of Administrative Services

Approved for Submission by: Dianne Thompson, Assistant City Manager

Attachments:

A – CEA-OE3 POP Plan Side Letter Agreement

B – CEA Side Letter Agreement

C – OE3 Side Letter Agreement (Desk Item)