

Rehiring “Retired” TSERS Employees Deal or No Deal?

By Brian D. Barger

In August 2005, the North Carolina General Assembly enacted several changes to statutes governing the requirements and limits on individuals covered under the North Carolina Teachers’ and State Employees’ Retirement System (TSERS) who wish to retire and later return to work for the state.

Background

As referenced in the February 2005 state treasurer’s report to the General Assembly, “North Carolina’s public employee retirement systems have long recognized the right of a public servant to return to work after retirement.” However,

- when and under what circumstances “retired” state workers can return to work without jeopardizing their retirement status/benefits has evolved significantly over time; and
- the changes adopted in 2005 were largely in response to State Treasurer’s Office concerns that prior retirement and return to work statutes were often misapplied in practice and potentially in violation of federal IRS pension plan requirements. The legislation adopted in 2005 was meant to clarify and address these issues.

Specifically, in August 2005 the North Carolina General Assembly adopted Senate Bill 622 and House Bill 320, which revised the definition of *retirement* under TSERS and instituted new, more conservative break-in-service requirements before allowing covered retirees to return to work in certain circumstances.

Unfortunately, because different parts of the retirement/return-to-work (RTW) changes phase in at different times or apply in different circumstances, the resulting legal

morass can quickly give you a headache when attempting to determine which retired employees are entitled to return to work when and get what. The following, however, is a “Cliff Notes” version of the current state of the law (at least until the next legislative go-around).

Where Are We Now?

A. Non-teacher or teacher returns to work with an employer that does not participate in TSERS.¹

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| 1. RTW employer: | Private or otherwise does <i>not</i> participate in TSERS. |
| 2. RTW position: | No restrictions. |
| 3. Break in service: | None required. |
| 4. Salary cap: | No restrictions. |
| 5. Prior agreement: | No restrictions. |
| 6. Compensation result: | Allowed to earn full RTW compensation with employer plus continue to receive full TSERS benefit payments. |
| 7. Contribution: | No TSERS contribution required. |

B. Non-teacher or teacher returns to work with an employer that participates in TSERS in a permanent full-time position that requires TSERS membership.²

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|-------------------------|---|
| 1. RTW employer: | Public employer that participates in TSERS. |
| 2. RTW position: | Permanent full-time positions not otherwise exempted. |
| 3. Break in service: | N/A. |
| 4. Salary cap: | N/A. |
| 5. Prior agreement: | N/A. |
| 6. Compensation result: | TSERS benefits will be stopped on the first day of the month following the month of re-employment.
Employee earns full salary with employer. |
| 7. Contribution: | Employee resumes participation as a contributing member in TSERS the same month that such retirement benefit payments cease. |

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1. See N.C. GEN. STAT. §§ 135-1 (20), 135-3(8)c. and 135-3(8)d. (2006) (hereinafter G.S.).

2. G.S. 135-1 (20) and 135-3(8)d.

C. Non-teacher or teacher retires on or before 10/1/05 (i.e., effective before 11/1/05) and returns to work with an employer that participates in TSERS in a nonpermanent part-time, temporary, interim, fee-for-service or other teacher or non-teacher position that does not require TSERS membership.³

1. RTW employer: Public employer that participates in TSERS.
2. RTW position: Position that does *not* require TSERS membership (e.g., nonpermanent part-time, temporary or interim positions or independent contractor engagements).
3. Break in service: None expressly required, other than the minimum one month required for general retirement.⁴
4. Salary cap: Yes. The greater of: (a) \$26,280,⁵ or (b) 50 percent of the employee's pre-retirement compensation reported to TSERS during the 12-month period preceding retirement (excluding final payments).
5. Prior agreement: No express N.C. statutory prohibition. *But see* federal IRS limitations regarding pre-existing work arrangements.
6. Compensation result: Allowed to earn RTW compensation with employer up to the defined salary cap plus continue to receive full TSERS benefit payments.
If the salary cap is exceeded, (1) TSERS benefit payments cease for the remainder of the calendar year beginning on the first day of the month following the month in which such salary cap amounts are exceeded; and (2) retiree health coverage is suspended until such time that the employee's regular retirement allowance is restored.
Note: TSERS benefits are suspended for 12 months if the salary cap is exceeded during the month of December. Otherwise, potential TSERS benefit payments resume on January 1 of the year following benefit cessation.
7. Contribution: No TSERS contribution required.

D. Non-teacher or teacher retires after 10/1/05 (i.e., effective on or after 11/1/05) and returns to work with an employer that participates in TSERS in a nonpermanent part-time, temporary, interim, fee-for-service or other non-teacher position that does not require TSERS membership.⁶

1. RTW employer: Public employer that participates in TSERS.
2. RTW position: Position that does *not* require TSERS membership (e.g., nonpermanent part-time, temporary, or interim positions or independent contractor engagements).
3. Break in service: Six-month *total* break from service in any capacity (including *no* part-time, temporary, substitute, or contractor service).⁷
4. Salary cap: Yes. The greater of: (a) \$26,280,⁸ or (b) 50 percent of the employee's pre-retirement compensation reported to TSERS during the 12-month period preceding retirement (excluding final payments).
5. Prior agreement: Expressly prohibited (termination plus complete separation from active service "with no intent or agreement, express or implied, to return to service").
6. Compensation result: Allowed to earn RTW compensation with employer up to the defined salary cap plus continue to receive full TSERS benefit payments.
If the salary cap is exceeded, (1) TSERS benefit payments cease for the remainder of the calendar year beginning on the first day of the month following the month in which such salary cap amounts are exceeded; and (2) retiree health coverage is suspended until such time as the employee's regular retirement allowance is restored.
Note: TSERS benefits are suspended for 12 months if the salary cap is exceeded during the month of December. Otherwise, potential TSERS benefit payments resume on January 1 of the year following benefit cessation.
7. Contribution: No TSERS contribution required.

3. G.S. 135-1 (20) and 135-3(8)c. (2005) and (2006).

4. G.S. 135-1 (20) (2005).

5. Note: Per statute, this amount is increased on January 1 of each calendar year by the percentage increase in the Consumer Price Index.

6. G.S. 135-1 (20) and 135-3(8)c. (2006).

7. G.S. 135-1(20) (2006).

8. Note: Per statute, this amount is increased on January 1 of each calendar year by the percentage increase in the Consumer Price Index.

E. Teacher retires *after 7/1/05* (i.e., effective on or after 8/1/05) but on or before 10/1/05 (i.e., effective before 11/1/05) and returns to work with an employer that participates in TSERS to teach on a full-time or part-time basis less than 50 percent of the applicable workweek (i.e., nonpermanent) in a North Carolina public or charter school.⁹

See Section C. above for what postretirement work is permitted in this circumstance (i.e., a position that does *not* require TSERS membership, such as nonpermanent part-time, temporary, or interim positions or independent contractor engagements).

F. Teacher retires *after 10/1/05* (i.e., effective on or after 11/1/05) and returns to work with an employer that participates in TSERS to teach on a full-time or part-time basis less than 50 percent of the applicable workweek (i.e., nonpermanent) in a North Carolina public or charter school.¹⁰

1. RTW employer: Public employer that participates in TSERS.
2. RTW position: Nonpermanent part-time or full-time teaching position with a public or charter school in a capacity that is *less* than 50 percent of the applicable work week (e.g., work on a nonpermanent part-time, substitute, or other temporary or interim basis).
3. Break in service: Six-month *total* break from service in any capacity (including as a substitute teacher or part-time tutor or any other part-time, temporary, substitute, or contractor service).
4. Salary cap: Yes. The greater of: (a) \$26,280,¹¹ or (b) 50 percent of the employee's pre-retirement compensation reported to TSERS during the 12-month period preceding retirement (excluding final payment).
5. Prior agreement: Expressly prohibited (termination plus complete separation from active service "with no intent or agreement, express or implied, to return to service").
6. Compensation result: Allowed to earn RTW compensation with employer up to the defined salary cap plus continue to receive full TSERS benefit payments.
If the salary cap is exceeded, (1) TSERS benefit payments cease for the remainder of the calendar year beginning on the first day of the month following the month

9. G.S. 135-1 (20), 135-3(8)c., and 115-325(a)(5a) (2005) and (2006).

10. G.S. 135-1 (20), 135-3(8)c. and 115-325(a)(5a) (2006).

11. Note: Per statute, this amount is increased on January 1 of each calendar year by the percentage increase in the Consumer Price Index.

in which such salary cap amounts are exceeded; and (2) retiree health coverage is suspended until such time as the employee's regular retirement allowance is restored.

Note: TSERS benefits are suspended for 12 months if the salary cap is exceeded during the month of December. Otherwise, potential TSERS benefit payments resume on January 1 of the year following benefit cessation.

7. Contribution: No TSERS contribution required.
- G. Teacher retires on or before 7/1/05 (i.e., effective before 8/1/05) and returns to work with an employer that participates in TSERS to teach on a substitute, interim, or permanent part-time or full-time basis in a North Carolina public or charter school.¹²**
1. RTW employer: Public employer that participates in TSERS.
 2. RTW position: Teaching position with a public or charter school, including substitute, interim, or permanent assignments.
 3. Break in service: Six-month break from service in any capacity with a public or charter school (*except* for work as a substitute teacher or part-time tutor, which is allowed).
 4. Salary cap: None.
 5. Prior agreement: No express N.C. statutory prohibition. *But see* federal IRS limitations regarding pre-existing work arrangements.
 6. Compensation result: Allowed to earn full RTW compensation with employer plus continue to receive full TSERS benefit payments.
 7. Contribution: 11.70 percent TSERS contribution after 7/1/05.
- H. Teacher retires *after 7/1/05* (i.e., effective on or after 8/1/05) but on or before 10/1/05 (i.e., effective before 11/1/05) and returns to work with an employer that participates in TSERS to teach on a permanent part-time or full-time basis more than 50 percent of the applicable workweek in a North Carolina public or charter school.¹³**
1. RTW employer: Public employer that participates in TSERS.
 2. RTW position: Permanent part-time or full-time teaching position with a public or charter school in a capacity that is *more* than 50 percent of the applicable work week (e.g., no work as a nonpermanent substitute or otherwise on an interim or temporary basis).
 3. Break in service: Six-month *total* break from service in any capacity (*including as a*

12. G.S. 135-1 (20), 135-3(8)c. and 115-325(a)(5a) (2005).

13. G.S. 135-1 (20), 135-3(8)c. and 115-325(a)(5a) (2005) and (2006).

- substitute teacher or part-time tutor or any other part-time temporary, substitute, or contractor service).
4. Salary cap: None.
5. Prior agreement: No express N.C. statutory prohibition. *But see* federal IRS limitations regarding pre-existing work arrangements.
6. Compensation result: Allowed to earn full RTW compensation with employer plus continue to receive full TSERS benefit payments.
7. Contribution: 11.70 percent TSERS contribution after 7/1/05.
- I. Teacher retires after 10/1/05 (i.e., effective on or after 11/1/05) and returns to work with an employer that participates in TSERS to teach on a permanent part-time or full-time basis more than 50 percent of the applicable workweek in a North Carolina public or charter school.¹⁴**
1. RTW employer: Public employer that participates in TSERS.
2. RTW position: Permanent part-time or full-time teaching position with a public or charter school in a capacity that is *more* than 50 percent of the applicable work week (e.g., no work as a nonpermanent substitute or otherwise on an interim or temporary basis).
3. Break in service: Six-month *total* break from service in any capacity (*including as a substitute teacher or part-time tutor or any other part-time, temporary, substitute, or contractor service*).¹⁵
4. Salary cap: None.
5. Prior agreement: Expressly prohibited (termination plus complete separation from active service “with no intent or agreement, express or implied, to return to service”).
6. Compensation result: Allowed to earn full RTW compensation with employer plus continue to receive full TSERS benefit payments.
7. Contribution: 11.70 percent TSERS contribution after 7/1/05.

Why Should I Care?

Because TSERS previously requested and received a favorable determination letter from the IRS, state employees who participate in TSERS receive the benefit of increases in

deferred compensation without paying current income tax (along with other tax benefits that are available to qualified retirement plans). However, failure to comply with applicable IRS pension plan requirements (either on a state or local level) could have a number of consequences, including:

- TSERS disqualification
- IRS action to recover improper payments
- Local school board accountability to the state/TSERS for corrective costs

This last risk is particularly troublesome. Because any sanctions against TSERS would occur at the state level, any IRS requirement that the state recover funds that were impermissibly paid may result in the state seeking assistance (i.e., money) from applicable local authorities who originally made the rehiring arrangements.

Such a request by the state could prove both costly (if, for example, the employee has an employment agreement or otherwise refuses to return the pension payments without litigation) and embarrassing to the school board or other state employer that ultimately may be required to pay “retirement rehire” compensation plus the recaptured cost of improperly-paid pension benefits for a given position.

The state/TSERS also may begin initiating their own audits of postretirement return-to-work payments *independent* of any IRS action to recover improper payments and other related TSERS costs from local districts.

As such, administrators attempting to follow the new rules should consider the following practical tips:

- Beware of “pre-existing arrangements” generally prohibited per IRS Revenue Rulings and other guidance (before or after 11/1/05).
- Beware of “sham”/fraudulent breaks in service or instances involving no break in service (before or after 11/1/05)
- Beware of employer-initiated pressure/deals with employees to retire and be rehired as a local board of education cost-reduction strategy.
- Beware of employee-initiated promises/deals regarding postretirement return to work prior to or as part of an employee’s separation.
- Employees should be advised that given salary cap and other limits, returning to work postretirement for a TSERS employer is at their own risk. ■

14. G.S. 135-1 (20), 135-3(8)c. and 115-325(a)(5a) (2005).

15. G.S. 135-1(20) (2005).