

Update

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TEACHER RETIREMENT SYSTEM OF TEXAS

Independent contractor or third-party entity?

NEW TWIST

In 2010, TRS became aware of a new twist in the independent contractor vs. employee debate. The work arrangement involves a Texas Limited Liability Company that sells shares of its own stock to some TRS retirees and then the retiree in his/her capacity as shareholder of the company enters into a contract for services with a TRS-covered employer. The TRS-covered employer pays the company for the services provided by the retiree and the retiree is paid by the company. Retirees who purchased the shares of stock and entered into agreements with TRS-covered employers in their capacity as shareholders expected that they would be considered independent contractors rather than employees of the TRS-covered entities and thereby avoid the limits on employment after retirement. The TRS-covered employers expected to avoid paying the surcharges on the employment of the TRS retirees/shareholders.

TRS reviewed documents provided by the attorney for the limited liability company, including the company agreement with a shareholder, a sample contract between a shareholder and a TRS-covered employer as well as the attorney's responses to direct questions posed by TRS. Based on the documents and responses, TRS concluded that the company was a *third-party entity* for TRS purposes and the retirees were employees of the "third-party" entity, *not* independent contractors.

OLD HISTORY

Since May, 2003 retirees employed by a third-party entity and providing services to a TRS-covered employer are considered employees of the TRS-covered employer for the purposes of administering employment after retirement. A third-party entity is an entity retained by a TRS-covered employer to provide personnel that perform duties or provide services that employees of the TRS-covered employer would otherwise perform. If a TRS retiree is employed by a third-party entity but working at a TRS-covered employer, the retiree must comply with the TRS plan terms regarding employment after retirement and must be reported to TRS on the *Employment of Retired Members Report*. Retirees who were first employed by the third-party entity prior to May 24, 2003 and are working for the third-party entity at a TRS-covered employer are not considered employees of the TRS-covered employer and may work without limit and without jeopardizing any monthly annuity.

RECENT CHANGES

Recent legislative changes opened the door for retirees who retired prior to January 2011 to work without limit for a TRS-covered employer. Retirees who retire January 2011 and after may work without limit for a TRS-covered employer only if they have a 12 full, consecutive-calendar-month-break in service from any type of employment with all TRS-covered employers. Performing services for a TRS-covered employer through a third-party entity is considered employment by the TRS-covered employer and does not count towards this required break in service. Without this 12-month break in service, retirees who retired January 2011 and after may work as substitutes, one-half time, or a combination of substitute work and one-half time employment without forfeiting a monthly annuity payment. The 6-month exception is no longer available.

SO, WHAT'S THE CATCH?

It is true that an independent contractor is not an employee of the TRS-covered employer. As an independent contractor

- any annuity payments are not forfeited by the retiree;
- the months of work are counted toward the required 12 full, consecutive-month-break in service (if the retiree retired January 2011 or after); and

- no surcharges are owed by the TRS-covered employer

However, being an independent contractor involves much more than just purchasing shares of stock in a company that includes the words “independent contractor” in its name. TRS recommends that the reporting entity and the retiree consult with their own attorneys about the requirements for independent contractor status and understand all aspects of the arrangement, including tax consequences, before deciding to contract for the services of the retiree as an independent contractor or shareholder. If you have questions regarding the agreement, contact TRS. State law gives TRS the authority to determine if the retiree is an employee of the TRS-covered employer or an independent contractor. Don't risk the unexpected loss of retirement benefits that the retiree worked so hard to earn.

More information about the standardized school year

House Bill 2561, 82nd Leg., R.S. (2011), amended the definition of a “school year” for TRS purposes to mean a 12-month period beginning September 1 and ending August 31 of the next calendar year. This bill applies beginning with the 2012-13 school year. The change in the definition of school year will impact two factors in the calculation of benefits: compensation and service credit.

The TRS Board of Trustees recently adopted changes in the TRS rules that detail how TRS will apply the new definition of school year in determining the amount of annual compensation credited to a member. The change in the definition of school year will most likely affect 11- and 12-month employees whose contracts begin on July 1st or August 1st of each year. To implement the change in the law, TRS will determine annual compensation for the 2012-13 and earlier school years either according to a 12-month period based on the member's “qualified” contract or work agreement, or on a September 1 through August 31 basis, whichever is most advantageous for a member with either an August through July contract period or a July through June period. In either case, no more than 12 months of compensation will be credited in one school year. Based on this information, **the MD40, Contract and Position Record will be required one more year (the 2012-2013 school year.)**

Annual compensation for the 2013-14 school year and later years will be credited on a September 1 through August 31 basis for all members.

TRS has received a number of inquiries regarding the need for 11- and 12-month employees to change their contracts to a standard year contract. TRS does not require the contracts to be changed. However, members who retire after August, 2013 should consider the most advantageous month for retiring to ensure that in the last school year (September 1st through August 31st) they receive credit for 12 months of compensation if that last year would be included in the final average salary. A member who has a non-standard contract and retires after August 31, 2013, will not have 12 months of compensation in the final year of employment if the member retires at the end of the contract period, i.e., June 30 or July 31.

Please note that the above information applies ONLY to applying annual compensation. For the purpose of determining a year of service credit, the standard school year of September 1 through August 31 will apply beginning with the 2012-2013 school year. This means that one year of service credit will be earned for 90 days of service (in an eligible position) from September 1st through August 31st each year. In the last school year of service before retirement, a member serving in an eligible position who worked or received paid leave for less than 90 days in the school year but worked or received paid leave for a full fall semester in accordance with the employer's calendar will receive a year of service credit.

Using TRS retirees as substitutes

TRS service retirees are allowed to work an unlimited number of days as substitutes without forfeiting any monthly annuities. Disability retirees may work up to 90 days as a substitute without forfeiting any monthly annuities. Surcharges that are owed for the employment of retirees who retired September 1, 2005 and after are also avoided because substitutes are not eligible for membership in TRS.

But the definition of a substitute for TRS purposes does not allow a retiree to serve in a vacant position. For purposes of employment after retirement, a substitute is a person who serves on a temporary basis in the place of a *current* employee. **If the position the retiree is filling is vacant, the retiree cannot be considered a substitute for employment after retirement purposes.**

If the position is vacant and if the retiree retired before January 2011, the retiree is considered a full-time employee and can work without limit. The surcharges will apply if the retiree retired September 2005 or after and if the position the retiree is taking is eligible for membership in TRS. In other words, if the retiree is working one-half

time or more in the vacant position and is expected to work at least 4½ months or more the surcharges will apply. If the retiree retired January 2011 or after, the retiree can work in the vacant position for no more than one-half time without forfeiting any annuity payments. If, however, the retiree has had a 12 full, consecutive-calendar month-break in all employment with any TRS-covered employer, the retiree can work any amount of time in the vacant position without forfeiting any annuity payments. If the retiree has not had a 12 full, consecutive-calendar month-break in all employment with any TRS-covered employer, the retiree can work no more than one-half time without forfeiting any annuity payments. If the retiree exceeds one-half time without having the required 12-month break in service, the retiree will forfeit the annuity payment for each month the retiree exceeds one-half time. Also, applicable surcharges will apply if the retiree is working in the vacant position one-half time or more for a period of 4½ months or more.

The reason the position is vacant does not matter. A retiree cannot be considered a substitute for TRS purposes if the position is vacant.

Unreported compensation or service

TRS reminds all reporting entities that it is extremely important that employers correctly withhold TRS contributions and report all TRS-eligible compensation in a timely manner. Verification, salary reports, or member contributions for additional compensation or service credit are not accepted after the date a member has retired from the system and the first monthly retirement annuity payment has been issued, or after an active member death benefit payment has been issued. All eligible compensation and service should be reported when earned. Failure of an employer to timely report eligible compensation and service can have serious financial consequences for TRS members and their beneficiaries because the cost to establish service or compensation credit is now the actuarial cost to TRS to provide the increased benefit.

Online certification of employee terminations

TRS is excited to announce the launch of Phase I of our Electronic Communications with Reporting Entities project. Implementation of this project means that you – the TRS reporting official – will be able to certify employment terminations for your employees online, via the TRAQS application. In Phase I, you will be able to certify TRS required data for your employees who have terminated employment and applied for a refund of their TRS contributions. You will do this online, without the need to keep track of paper forms and mail documents to TRS.

During the initial implementation period, TRS members who terminate employment and want to withdraw their contributions will complete the current “Notice of Final Deposit and Request for Refund” form (TRS 6). If the employee gives you the form to certify termination data, please complete the form as requested. However, if the employee fails to have you certify the termination and instead mails the form directly to TRS – as many do now – TRS will notify you electronically, rather than sending you a letter requesting the information.

Any time you have employees requesting TRS contribution refunds and those employees fail to have you sign their refund applications, TRS will send you an email notification that you have terminations to complete on TRAQS. Then, all you have to do is sign in to TRAQS and you will be prompted to complete any outstanding termination records. For each employee termination record to be certified, you will see the employee’s identifying information and, once you enter the termination information, all you have to do is select “submit.” The data will be returned to TRS electronically, expediting the member’s refund application and saving you time and paperwork! Once each week, you will receive a reminder email, if you have any outstanding terminations awaiting certification. It’s as simple as that!

An online tutorial will be available soon to guide you in this new process. The next phase of this new process will be to eliminate the written certification from the member’s refund application and have all certifications done online, simply and quickly. In the future, TRS plans to expand electronic certification for terminations to include your retiring employees.

TEAM Program to bring improvements to reporting system

TRS is proud to provide the best possible customer service to our members and annuitants, and we recognize the vital role our reporting entities play in that effort. With a growing population to serve, the effort will only become more challenging for us all in the future. That’s why TRS has initiated the TRS Enterprise Application Modernization Program or TEAM Program. The TEAM Program is a multi-year initiative, which consists of numerous projects that will update non-investment-related business processes and core technologies used by TRS to deliver benefits.

One of these projects involves replacing the TRS Reporting and Query System (TRAQS), which has been in use since January 2001, with a new and improved system. As users of TRAQS, we need *your* suggestions on how a new system could work for you, e.g., what works well now, and what could be improved?

In the next few weeks, each reporting entity will be e-mailed a brief survey in which you'll have the opportunity to provide feedback. The information will be used in outlining the desired outcomes that will be included in a Request for Offers (RFO) to secure a new Pension Administration System. The vendor that is selected will ultimately work with TRS and our reporting entities on developing the new system. Although it won't be possible to accommodate all suggestions received, our goal is to make improvements that will be meaningful to you. We will look forward to hearing from you through our survey!

Nominations now being accepted for seat on TRS Board

Please share the following information with your employees!!

Active member public school employees may now begin requesting petitions to nominate candidates for a seat on the TRS Board of Trustees. An election for one of the active member public school employee positions on the board will take place in spring 2013. Valid petitions **received by TRS on or before January 21, 2013**, will be accepted. To learn more and how to obtain a nominating petition, please visit www.trs.state.tx.us.