

House Bill 59 TRS Housekeeping

Sponsor: Representative Robin Hamilton

By request of the Teachers' Retirement Board
David L. Senn, Executive Director
406 444-3376

DESCRIPTION

House Bill 59 is a housekeeping, general revision bill, making administrative changes to the Teachers' Retirement System (TRS) laws. HB 59 was reviewed by the State Administration and Veterans' Affairs Interim Committee. Many of the amendments are necessary to comply with the Pension Protection Act of 2006 and/or are required to comply with the Internal Revenue Service's regulations governing qualified plans.

The changes clarify the definitions of employer, full-time and part-time service, normal retirement age, and adds a definition for normal form or normal form benefit. More substantive amendments will help clarify laws governing who must be a member of the Teachers' Retirement System, division of benefits under a family law order in the case of a divorce, joint and survivor optional benefits available at the time of retirement, and verification of termination of employment as required by the Internal Revenue Code.

SECTION-BY-SECTION DESCRIPTION

Section 1. §19-20-101, Definitions

- *Employer* – Clarify and more specifically identify public agencies that are eligible to participate in TRS. The amendments do not add to or eliminate any employers currently participating in TRS.
- *Full-time service* – Amendments are intended to clarify that an alternative school calendar of less than 180 days, which meets accreditation standards for a full-time school year, would also qualify as full-time service under the TRS.

The 2005 legislature eliminated the requirement that districts have at least 180 days of pupil instruction and replace it with an hourly requirement. Since then we have seen a number of school calendars of less than 180 days, some as few as 160. Under current law, the TRS defines full-time service as 180 days, or 140 hours per month over at least 9 months during the fiscal year. Therefore, if the proposed amendments are not adopted, TRS members could end up receiving less than 1 year's service credit for having worked the full school year. This amendment has a proposed effective date retroactive to July 1, 2005.

- *Normal form or normal form benefit (new)* – the term is used in statute but not defined in the act. It simply means a monthly benefit paid for the life of the retiree.
- *Normal Retirement Age* – Amendment is required by changes in the Pension Protection Act of 2006. The IRS rules define “normal retirement age” as being age 62 or:

“not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry....”

The regulations provide two safe harbors that the IRS will presume to be the “typical” earliest normal retirement ages, depending on facts and circumstances: (1) age 55 for non-public safety employees, and (2) age 50 for public safety employees. Earlier ages are not deemed to be typical; however, the IRS Commissioner has the authority to review this based on facts and circumstances.

The proposed amendments will define normal retirement age under TRS as age 55 and eligible for an unreduced retirement benefit. We believe this amendment will qualify as “normal retirement age” under the IRS regulations and will **not** change the benefit any member of the TRS is eligible to receive under current law. Changing the definition also resulted in several changes throughout HB 59.

What might change is the option to return to work for the same employer if there is a prearranged agreement to return to work. If there is a prearranged agreement and the retired member is not age 55 or older and eligible for unreduced benefits, they would not be able to return to work, even in a part-time position, and draw their TRS benefits.

- *Part-time service* – Changes are necessary to maintain the same historical calculation of part time service credit.
- *Prior Service* – Definition is no longer applicable as no current member has service prior to September 1, 1937. Eliminating this definition resulted in several changes throughout HB 59.

Section 2. § 19-20-302, Active membership.

One of the most often asked questions is who must be a member of the TRS. The proposed amendments clarify and more specifically identify positions that are eligible to participate in TRS. To the best of our knowledge, the following positions are all currently members of the TRS, and these amendments will not change who must be a member of TRS. The clarifying terminology includes:

- Professionally qualified persons as defined in 20-4-901, MCA, such as, counselors, curriculum specialists, artists, musicians, and others with special training who are qualified to appraise pupils' special competencies
- Dean of students
- Administrative officers and instructional staff of a community college; or,
- Anyone reported on the district's Annual Data Collection Report to OPI employed in a nonclerical position.

Section 3. § 19-20-305. Alternate payees – family law orders.

Several changes were enacted in 2007 to allow for the separation of the TRS benefit in the case of divorce. The amendments include the following changes.

- Clarify the terms “actuarially equivalent amount” and “fixed amount”. When benefits are divided in the case of divorce, benefits can be paid to the alternate payee for their life (actuarially equivalent amount) or in a fixed monthly amount over a certain period of time (fixed amount).
- Clarify the TRS member’s benefit will be reduced at the time of retirement by the amount payable to the alternate payee, thus creating a separate benefit payable for the life of the alternate payee.

Section 4. § 19-20-401 Creditable service.

- Strike language referencing creditable service earned prior to September 1, 1937

Section 5. § 19-20-409. Transfer of service credits and contributions from public employees' retirement system.

- Clarify and clean-up language and revise statutory construction in subsection 8

Section 6. § 19-20-603. Withdrawal of accumulated contributions -- options.

- The proposed amendment will provide members withdrawing their account the options to roll over the payment to a ROTH IRA.

Section 7. § 19-20-605. Pension accumulation account -- employer's contribution.

- Delete language that is no longer relevant, and clarify that the state general fund is also paying the supplemental contribution for special education cooperatives, and counties. This does not change the current payment of supplemental contributions by these entities or the general fund.

Section 8. § 19-20-701. Benefits.

- Require TRS members and their employers certify if there is any prearranged agreement prior to termination for the member to return to work.

TRS Tax Counsel, Ice Miller, noted that as of 2009 plan year, the IRS will treat a return to part-time work in the same manner as a return to full-time work. That is, if the member has not attained "normal retirement age", there must be a bona fide separation from service in order for benefits to begin prior to a return to part-time employment with the same employer. Therefore, in a reemployment situation the IRS is interested in whether there was a bona fide separation from service prior to the reemployment. We believe that this procedure is very important in furthering tax qualification of TRS. In addition, this is a very important step in protecting members from early distribution taxes.

Section 9. § 19-20-702. Optional and period certain allowances.

- Clarify what constitutes an optional retirement allowance, and the different options available in case of death or divorce of the beneficiary when a Family Law Order has not been issued and the TRS member is awarded their full benefit under a property settlement agreement.

The amendments are intended to clarify the two types of benefits, and simplify the language regarding death of the beneficiary, or divorce where the property settlement awards the entire TRS benefit to our member.

Section 10. § 19-20-703. Payments to be monthly.

- Clarify that distributions of benefits to members who are age 70 ½ will be made only to inactive members. Active members age 70 ½ do not qualify for benefits and therefore would not be eligible to receive a monthly benefit.

Section 11. § 19-20-718. Maximum contribution limitation.

- Clarify definition of compensation for purpose of complying with § 415 of the Internal Revenue Code. This definition of compensation will **NOT** be used for calculation benefits or for determining employee and employer contributions. This definition is more inclusive of fringe benefits and allows for the broadest definition in order to assist any member in complying with the 415 limits. The annual limit on compensation for 2009 is \$245,000. The IRS requires this language be included in the plan documents for a public plan, but practically speaking, we cannot envision this limit will ever impact any Montana TRS member.

- Amendments are necessary to comply with the Pension Protection Act of 2006 and requirements to remain a tax-favored qualified plan.

Section 12. § 19-20-731. Postretirement employment limitations -- cancellation and recalculation of benefits.

- Change language to comply with the amendments to the definition of normal retirement age in Section 1. This change will not impact any TRS member's retirement benefit.

Section 13. § 19-20-804. Allowance for service retirement.

- Correct language to comply with the amendments to the definition of normal retirement age in Section 1. This change will not impact any TRS member's retirement benefit.

Section 14. § 19-20-905. Cancellation of allowance and restoration of membership.

- Strike language referencing service earned prior to September 1, 1937

Section 15. § 19-20-1001. Allowances for death of member.

- Changes required to comply with amendments to family law orders, see section 3

Section 16. § 19-20-1003. Payment of death benefits.

- Updating reference to section 19-20-702 to capture amendments in §19-20-702, see section 9

Section 17. § 20-15-106. Retirement systems for employees and teachers.

- Add reference to TRS and PERS statutes

Section 18. § 20-15-403. Applications of other school district provisions.

- Add the TRS membership statute to the list of laws outside of Title 20 that apply to community college districts.

Section 19. Repeal § 19-20-406. Creditable service for prior service

- Strike statute governing creditable service earned prior to September 1, 1937

Section 20. Effective date.

- This act is effective July 1, 2009.

Section 21. Retroactive applicability.

- The definition of full-time service, section 1, must be made retro active to 2005 when the legislature changed the law governing what constituted a full school year. If this amendment is not approved, service credit will be recalculated and reduced for all teachers employed in districts with fewer than 180 days in the school year.
- The Internal Revenue Service requires that these provisions be included as provisions in the "plan documents" of a public pension plan in order for the public pension plan to maintain its status with the Internal Revenue Service as a qualified plan. All of the standards set forth in section 11 are standards that the Teachers' Retirement System has been required to and has complied with up to this time, but are promulgated as amendments now to meet new Internal Revenue Service requirements that certain standards be set forth in a pension plan's plan documents.

By virtue of the fact that public pension plans are established by legislative mandate, public pension systems do not typically generate and distribute "plan documents" that describe the benefits and obligations of the plan and its members. Rather, the plan documents of a public pension plan are comprised of the applicable statutes, administrative rules, and other standards that legally govern the public pension plan, so modification of the TRS's plan documents means modification of the statutes and/or administrative rules governing the retirement system and because the Montana legislature only meets every other year, these amendments must sometimes be made retroactive.

Summary

Many of the changes proposed in HB 59 are required to comply with the Internal Revenue Service's regulations governing qualified plans. Failure to comply with the IRS's plan document requirements could result in the Teachers' Retirement System losing its status as a qualified plan. Loss of status as a qualified plan would mean that the plan and contributing employers and employees would lose the favorable tax treatments applicable to contributions and benefits from a qualified plan, including but not limited to pretax treatment of contributions. If the plan were required to pay federal taxes on its investment income, the legislature could be asked to make up the losses through additional contributions.

Additionally, HB 59 will help clarify several definitions, TRS membership eligibility, family law orders, optional retirement benefits, and eligibility for retirement benefits. These amendments are not intended to change and current benefits, rights or features available to members, or to enhance or diminish benefits in any way.

AMENDMENTS TO HB 59

1. Compliance with the Federal Heroes Earnings Assistance and Relief Tax act.

New Section. Compliance with Federal HEART Act. (1) **[Mandatory Provision]** Effective with respect to deaths occurring on or after January 1, 2007, while a member is performing qualified military service (as defined in chapter 43 of title 38, United State Code), to the extent required by § 401(a)(37) of the Internal Revenue Code, the designated beneficiaries are entitled to benefits that the system would provide if the member had resumed employment and then died, that are contingent on the member's death while employed.

- The Heroes Earnings Assistance and Relief (HEART) Tax Act Creates new requirements for treatment of survivor benefits of those killed while performing qualified military service. Under this act, the designated beneficiary of a member killed while performing qualified military service, will be entitled to survivor benefits as if the member died while an active member of the TRS.
- This benefit is largely available under current law. This provision would make available a one-time \$500 death benefit paid to members who die within one year of termination, and a \$200 minor child benefit paid to the minor children of any member who dies within one year of termination. These benefits are a very immaterial and therefore there is no way to estimate the impact of this change.