

2013 Legislative Session – HB 315 – Act Authorizing Public Charter Schools  
Testimony of the Montana Teachers' Retirement System/Board (TRS)

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New Section 14(7)(c) – page 23 – provides that employees in a public charter school are eligible for participation in retirement and other benefit programs of the state pursuant to Title 19, chapter 20 (the TRS provisions), if the governing board of the public charter school elects to participate.

New Section 22 – page 32 - provides for a process for the public charter school to exercise its election option by contracting with the TRS Board, and to revoke its participation in TRS at any time by submission of a termination resolution to the TRS Board. The TRS Board is authorized to approve, or not, a proposed contract for participation in the system if, in its sole discretion, the contract adversely affects the interests of the retirement system. The TRS Board is also authorized to "withhold approval of the termination of contract until satisfactory arrangements are made to provide funding for any excess accrued liabilities not previously funded by the terminating public charter school."

The potential participation by public charter schools and their employees in TRS, as set forth in the bill, raises issues related to plan administration, funding, and even tax-qualification, as well as questions regarding plan participant rights to continue to accrue pension benefits and participation in social security if a public charter school does not participate in or provide a pension plan that provides sufficient replacement benefits.

**Tax Qualification Issue**

On November 7, 2011, the IRS and the Dept. of Treasury issued an advance notice of proposed rulemaking (ANPRM) regarding determination of governmental plan status. Substantively, the proposed rules pertain primarily to definitions that will be employed in determining whether an entity is eligible to participate in a tax-qualified state pension plan. An entity must be: a state government; a political subdivision of the state government; or an agency or instrumentality of the state government or a political subdivision. Other entities may not participate in a state public pension plan, and a public pension plan that allows participation by non-eligible employers/members may lose its tax-qualified plan status.

As originally presented, the proposed rules as set forth in the ANPRM are fairly clearly understood to exclude public charter schools as participants in public pension plans. As stated in an article by Michael Podgursky, Stuart Buck, and Renita Thukral:

"Unfortunately, the proposed Treasury Department regulations, if adopted as currently written, would make it very difficult for state and local teacher plans to admit charter schools and retain their governmental plan status. Indeed, if these regulations are implemented as written, the prudent course of action for any state or local plan administrator, faced with possibility of losing governmental status, would be to throw charter schools out of the plan." See *"Charter school teachers would be hit hard by new Treasury Department ruling on pensions,"* Education Gadfly Daily, 2012, at <http://www.edexcellence.net/commentary/education-gadfly-daily/flypaper/2012/charter-schools>

At this time, a final notice of proposed rulemaking has not been issued. However, because the IRS and Treasury represent the proposed definitions as interpretation of current law, allowing participation of public charter school employees before finalization of the anticipated rules could be problematic. As well, implementation of participation election/contracting and administrative processes for TRS participation by public charter schools would be time consuming and costly, and may be for naught.

**Plan Administration Issues**

HB 315, as currently drafted, would require TRS to establish administrative processes for contracting with public charter schools, for assessing whether a proposed contract for participation is adverse to the interests of the retirement system, and for making an actuarial valuation of the liabilities of a terminating public charter school and to provide for any excess accrued liabilities not previously funded by the terminating charter school. While administrative processes can be established, detail regarding appropriate administrative processes is not provided, nor is rulemaking authority specifically granted to TRS to address those missing details. Some administrative points that may need to be addressed are as follows:

- A participation election contract should be a uniform document prescribed by TRS to ensure uniform application of participation eligibility criteria and standards to all applying/participating charter schools.
- Costs for an actuarial valuation for a terminating charter school should be the responsibility of the terminating charter school.
- Information from other states has indicated that consistent receipt of employer and employee contributions from public charter schools – particularly from those that are authorized and or governed by entities not already participating in the retirement system – may become a problem. A requirement that contributions from participating public charter schools be required to be withheld from funding transferred by OPI and remitted directly to TRS would ensure proper funding and administration of charter school participation in TRS at a lower administrative cost.
- Since a charter school may cease to do business at any time for any number of reasons, or may elect to terminate participation in TRS, and the state is expressly not liable for the debts of a public charter school, some protections should be considered for other TRS participating employers to prevent shifting of unpaid contributions and/or unfunded liabilities of terminating public charter schools to other employers and members in the system. For example, a provision expressly stating that the state will assume responsibility for the unpaid contributions or unfunded liabilities of a terminated public charter school would ensure appropriate funding of benefits attributable to the creditable service of charter school employees without undue administrative burden on the retirement system or cost shifting to other employers.

### **Plan Funding Issues**

- For every public charter school that elects not to participate in TRS, or is prohibited from participating based on the outcome of IRS/Treasury rulemaking, public educator positions will be removed from TRS participation, and the salary base from which contributions to TRS are determined will shrink. While TRS has no basis to determine what the actuarial/funding impact of such outcomes will be, it anticipates there will be an impact.
- A retired member of TRS who went to work for a non-participating public charter school would appear not to be subject to the post-retirement earnings limitations under current TRS law. TRS participants who are eligible to retire would be encouraged to retire when first eligible and to return to work in a non-participating charter school. While TRS has no basis to determine what the incidence or actuarial/funding impact of such adverse selection would be, it anticipates there will be an impact.
- The apparent ability for public charter schools to opt in and out of the retirement system at will would provide the opportunity for charter schools to make those determinations specifically based on the pool of available educators, and whether participation impacts their ability to hire TRS retirees, thereby exacerbating the potential for adverse selection against the retirement system.
- As discussed in the Plan Administration Issues section above, a number of issues unaddressed in HB 315 may result in unnecessarily greater administrative expenses or inability to recover unpaid contributions or contributions for the unfunded liabilities of terminated public charter schools.
- Providing an opportunity for one segment of eligible employers to discontinue participation in the retirement system would raise questions and may provide a legal basis for arguments by other employers that they should have the same right to opt out of the retirement system. TRS would strongly prefer that even if participation by charter schools remains optional, once an election is made, that election should be irrevocable.

### **TRS Member Rights Terminated, No Requirement for Replacement Benefits, and Social Security Participation**

Under HB 315, an existing public school could convert to a public charter school, elect not to participate in TRS, and current TRS participants could be required to find employment in another TRS-reportable position or have their right to continue to accrue retirement benefits terminated. As well, nothing in the bill indicates that a public charter school that elects not to participate in TRS is required to provide another pension or retirement savings plan for its employees. Finally, there may be employers in TRS currently that were not required and did not elect to participate in Social Security, for which employers TRS constitutes a qualified social security replacement plan. If such employers convert to charter school status and elect not to participate in TRS, there may be social security participation issues to be addressed.