



MAILING ADDRESS:
PO Box 295
TRENTON, NJ 08625-0295

LOCATION:
50 WEST STATE STREET
TRENTON, NEW JERSEY

CHRIS CHRISTIE
Governor

KIM GUADAGNO
Lt. Governor


State of New Jersey
DEPARTMENT OF THE TREASURY
DIVISION OF PENSIONS AND BENEFITS
(609) 292-7524 TDD (609) 292-7718
www.state.nj.us/treasury/pensions

ANDREW P. SIDAMON-ERISTOFF
State Treasurer

FLORENCE J. SHEPPARD
Acting Director

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TO: Certifying Officers of the Public Employees' Retirement System (PERS), Teachers' Pension and Annuity Fund (TPAF), Police and Firemen's Retirement System (PFRS), State Police Retirement System (SPRS), and Judicial Retirement System (JRS)

FROM: Florence Sheppard, Acting Director
Division of Pensions and Benefits 

SUBJECT: **Compliance with US Internal Revenue Code — Bona Fide Severance of Employment — Post-Retirement Employment Restrictions for Individuals Covered by any New Jersey State-administered Retirement System**

New Jersey State-administered retirement systems do not permit the payment of retirement benefits without a severance from public employment. This memorandum addresses restrictions pertaining to the re-employment of retired members from any of New Jersey's State-administered retirement systems. It also discusses a new form for all employers called the *Notification of Employment after Retirement*. This form must be completed whenever you, the employer, engage the services of any retired New Jersey public employee. This requirement pertains to your former employees as well as those who retired from another New Jersey public employer.

INTERNAL REVENUE CODE

The PERS, TPAF, PFRS, SPRS, and JRS are established as qualified governmental defined benefit plans in accordance with Internal Revenue Code (IRC) Sections 401(a) and 414(d). In order to preserve the qualified status of these plans and to protect retirees from a 10% excise tax penalty on their monthly retirement payments, the Division of Pensions and Benefits was required to adopt and to enforce regulations to ensure compliance with the IRC requirements.

"Compliance with Internal Revenue Code" was adopted as a special new rule, effective March 9, 2012, under Title 17, Chapter 1, Subchapter 17, of the New Jersey Administrative Code. The provisions of N.J.A.C. 17:1-17.14, were needed to clarify criteria regarding retiree re-employment.

N.J.A.C. 17:1-17.14.2(a) states:

"Bona fide severance from employment' means a complete termination of the employee's employment relationship with the employer for a period of at least 180 days.¹ The following does not constitute a complete termination of the employee's relationship with the employer:

- i. Employment or re-employment in a part-time position;
- ii. Employment or re-employment in a position that is not covered by the Defined Benefit Plan;

¹ Employees who work a 10-month school year and retire on July 1 or August 1, must count the 180-day severance of employment from the start of the following normal school year in September.

- iii. A change in title;
- iv. Employment or re-employment as a contract employee, a leased employee,² or an independent contractor; or
- v. Termination of employment with a pre-arranged agreement for re-employment.

Federal Internal Revenue Service factors shall be used as guidance in determining whether an employment relationship exists. A mandatory retirement shall be treated as a 'bona fide severance from employment.'"

The above 180-day requirement does not apply to individuals who were required to retire under the mandatory retirement provisions of the PFRS, SPRS, or JRS.

Re-employment by a different unit of the same public entity, whether in a position covered by the same retirement system or a different retirement system, is considered to be employment by the same employer.

- Example 1 – a State employee who retires from one State agency and returns to work as a full- or part-time employee or independent contractor at the same or any other State agency, including a State university, within 180 days following retirement is considered to be returning to work for the same employer. A bona fide severance from employment has not occurred and the individual does not qualify for the receipt of retirement benefits.
- Example 2 – a TPAF member who retires from a school district and returns as a part-time teacher in the same district within 180 days following retirement is considered to be returning to work for the same employer. A bona fide severance from employment has not occurred and the individual does not qualify for the receipt of retirement benefits.

Further, if an employee holds more than one position with the employer, he or she must separate from all employment in order to retire, even if the positions are covered by different retirement systems, or the second position is not subject to pension contributions.

- Example 3 – A municipal fireman, enrolled in PFRS, also works in a PERS position for the same municipality. In order to retire from the PFRS, the member must terminate from both positions in order to qualify for retirement benefits from the PFRS. Further, the individual must be terminated from each position for at least 180 days prior to any consideration of return to employment in the non-PFRS position.
- Example 4 – A State employee in the executive branch is also an adjunct faculty member at a State college. The executive branch position is covered by the PERS; the adjunct faculty position is covered by the Alternate Benefits Program (a defined contribution plan). In order to retire from the executive branch position and collect PERS benefits the individual must also separate from the second State position, even though the position is covered by a different retirement system. Further, the individual must be terminated from each position for at least 180 days prior to any consideration of return to employment in the non-PERS position.

² This includes services provided to all employers who are party to a shared service agreement with your former employer.

Consequences of Invalid Re-employment

If an individual returns to public employment with the former employer prior to satisfying the requirements of a bona fide severance from employment, the employee will be required to repay all retirement benefits received from the date of retirement and may be required to re-enroll in the same or a different retirement system. For example, a former employee of a county returns to county employment 135 days after retirement in a position that is not covered by his former retirement system. The former employee has not met the requirement for a bona fide severance from employment and will be required to repay all retirement benefits and be enrolled in the appropriate retirement system. All employee/employer pension remittances related to the new enrollment will be retroactive to the date of re-employment. This individual will also not qualify for the receipt of retirement benefits from his former retirement system until he separates from all county employment.

The IRS does not consider a pre-arranged return to public employment to be a bona fide severance from employment no matter how long the break in employment. If the employer and employee make an arrangement prior to the employee's retirement to return to the same employer in any capacity, including as a volunteer — at any future time, regardless whether the position is covered by the former retirement system — the employer/employee relationship is not completely severed and the retirement will be invalid. Should this occur, the employee will be required to repay all retirement benefits received from the date of retirement and may be required to re-enroll in the same or a different retirement system. All employee/employer pension remittances related to the new enrollment will be retroactive to the date of the employment. This would apply even if he or she waited 180 days before returning to the public employment.

Education Employees - Special Provisions for Critical Need Employees

N.J.S.A. 43:15A-57.2(c) and 18A:66-53.2(b) provide an exemption from pension re-enrollment for certain retirees of the PERS or TPAF who are certificated superintendents or certificated administrators and who are hired in a position of critical need. Termination of employment for 120 days with a pre-arranged agreement to return to that employer will not be considered a bona fide severance from employment. While New Jersey law permits these retirees to return to employment with the same employer after 120 days without re-enrollment into the retirement system, the 180-day requirement still applies for tax purposes when considering the pension as an early distribution. A retiree who is under the age of 59½ and returns to employment with the same employer prior to a 180-day break in service may therefore be responsible for excise tax penalties under IRS regulations. (The retiree must report the early distribution tax on IRS *Form* 5329). The Division of Pensions is required to report the premature distribution on the retiree's *Form* 1099-R.

Education Employees - Special Provisions for Coaches

Chapter 21, P.L. 2014, enacted July 30, 2014, permits a former member of the TPAF, who has been granted a retirement allowance for any cause other than disability, to become employed again with the former employer as a coach of an athletics activity if the following conditions are met: (1) the re-employment commences after the retirement allowance becomes due and payable³; (2) the former member had attained normal retirement age as of the date of retirement⁴; and (3) the compensation for the employment is less than \$10,000 per year.

³ Either more than 30 days after the date of retirement, or more than 30 days after the retirement has been approved by the Board of Trustees of the TPAF, whichever date is the later of the two.

⁴ Normal retirement age for members of the TPAF means age 60 for persons who became members before November 2, 2008 (Tiers 1 and 2); age 62 for persons who became members on or after November 2, 2008 (Tiers 3 and 4); age 65 for persons who became member on or after June 28, 2011 (Tier 5).

EMPLOYER RESPONSIBILITIES

If you retain the services of any individual who is retired from one of the New Jersey State-administered retirement systems, you are required to complete the *Notification of Employment after Retirement* form and submit it to the Division of Pensions and Benefits within 15 calendar days of the date of hire. The notification form will be reviewed by the Division to determine if the returning retiree can continue to receive retirement benefits while re-employed, or if the retirement must be canceled and the employee enrolled in the same or another retirement system. The employer must also notify the Division when the employee's services to the employer have been terminated. Completed notification forms should be submitted to: External Audit Unit, Division of Pensions and Benefits, P.O. Box 295, Trenton, NJ, 08625-0295.

ADDITIONAL INFORMATION

Additional information regarding the taxability of pension benefits can be found in Fact Sheet #12, *Taxation of Retirement Benefits*. For specific questions regarding the tax implications of returning to employment after retirement, current or former employees should consult with a professional tax advisor or contact the IRS at 1-800-TAX-1040.

If you have general questions regarding any of the information provided in this letter, contact the Division's Office of Client Services at (609) 292-7524, or e-mail the Division at: <https://www.state.nj.us/treas/pensions/pensionmail.shtml>

Enclosure

Employer Form: *Notification of Employment after Retirement*