



**Ohio
Retirement
Study
Council**

88 East Broad Street, Suite 1175
Columbus, Ohio 43215
PHONE: 614-228-1346
FAX: 614-228-0118

To: Bethany Rhodes, ORSC Director
From: Jeffery A. Bernard, Senior Research Associate *JAB*
Date: November 3, 2015
Subject: Conference Committee Amendments to H.B. 2

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During the Conference Committee on H.B. 2 (community schools), an amendment was added regarding the membership of certain community school employees in the State Teachers Retirement System (STRS) and School Employees Retirement System (SERS). The H.B.2 amendments may need further adjustment depending on anticipated Internal Revenue Service (IRS) regulations regarding community school employees and whether the IRS determines those employees are private or government employees.

Background

National Heritage Academy (NHA), a community school management company operating schools in Ohio, required its Ohio employees to make contributions to STRS or SERS, as required by Ohio law,¹ but additionally withheld Social Security tax for the same employment. NHA's actions raise two issues: 1) whether STRS' and SERS' qualified tax status is endangered by including potentially private employees in a government plan, and 2) the public policy of having Ohio retirement system government employee members dually contributing to Social Security and a state retirement system. While the amendments to H.B. 2 potentially resolve the issue for future community school employees, both of these issues remain for existing community school employees until final regulations are issued by the IRS.

Amendments to H.B. 2

The amendments to H.B. 2 provide that any *new* employees of Ohio's community schools contributing to Social Security will not be eligible for membership in either STRS or SERS. *Existing* employees dually paying Social Security and STRS or SERS contributions will continue to dually contribute. The amendments include provisions that maintain membership of existing STRS or SERS members even if they cease employment for a

¹ R.C. 3307.01 and 3309.01.

period of time. Because the precise membership determinations of H.B. 2 are fairly complex, the attached appendices provide a flow chart of membership determinations for STRS and SERS community school employees.

H.B. 2 Amendments and Pending IRS Regulations

Ohio's retirement systems, including STRS and SERS, are government plans under Internal Revenue Code 414(d). That section describes a government plan as "a plan established and maintained for its employees...by the government of any State or political subdivision." Maintaining this status is essential. Unfortunately, there has been little guidance from the IRS on whether a government plan could maintain its 414(d) status if it includes employees of a community school management company. The central question is if such employees are properly classified as "private" or "government." Recently, the IRS has moved to develop specific regulations on the classification of these employees and whether a state or local retirement system that covers them is a governmental plan under 414(d). On November 8, 2011, the IRS published an Advance Notice of Proposed Rulemaking (REG-157714-06)² and further revised those proposed rules on February 9, 2015, with IRS Notice 2015-07. ORSC staff cannot anticipate the standards the IRS will develop to determine if a community school employee is a private or government employee. A decision in either direction will likely necessitate adjustments to the H.B. 2 amendments.

Community School Employees as Private Employees

If the IRS determines that community school employees that are specifically included in STRS and SERS in H.B. 2 are actually private, then either the amendments to H.B. 2 will need to be amended to exclude such individuals, or the systems will need explicit notification from the IRS that such participation is *de minimus* and will not jeopardize the plans 414(d) status.

Existing Department of Labor Advisory Opinion practices permit a limited number of private employees to participate in a government plan (*de minimus* participation of private employees).³ Regrettably, there is little firm guidance on what constitutes *de minimus* participation.⁴ While the current anticipated dual contributors under H.B. 2 is small (.4% of total STRS active members and .2% SERS active members), ORSC staff believes it would be imprudent to rely on the little guidance currently available to anticipate a *de minimus* ruling.⁵ Instead, ORSC would recommend that, should the IRS deem the dual contributors under H.B. 2 are actually private, that STRS and SERS immediately seek official notification from the IRS that such participation is *de minimus*. If this is not granted, legislation should be advanced to exclude these

² A useful summary of the notice, and reason for its drafting, is available from BNA Daily Tax Report, "New IRS Regulation Project Tackles Definition of 'Governmental Plan' (December 5, 2011).

³ United States Department of Labor, Advisory Opinion 2012-01A.

⁴ United States Department of Labor, Advisory Opinion 99-07A.

⁵ Email correspondence from Marla Bump, STRS Director of Government Relations, and Laurel Johnson, SERS Government Relations Officer on October 27, 2015.

individuals from STRS and SERS to ensure that the systems maintain their governmental plan status.

Community School Employees as Government Employees

Alternatively, *if* the forthcoming regulations determine that community school employees are government employees, the H.B. 2 amendments will need an opposite adjustment.

Ohio has a long and successful history of resisting attempts to include government employees in Social Security. In fact, Ohio has the largest percent of government employees not covered by Social Security in the nation (99%).⁶ One main reason for this is that Ohio's Section 218 Agreement, the mechanism under which a state can elect to cover its employees under Social Security, has virtually no provisions for such coverage.⁷ NHA required its employees to participate in both STRS or SERS and Social Security, creating a dual contribution situation not anticipated under state law. Under the H.B. 2 amendments, this dual contribution continues for certain existing community school members. Should these employees be deemed government employees under forthcoming IRS regulations, the H.B. 2 amendments would need to be amended to ensure that no government employee contributes to Social Security.

ORSC staff summary

The status of community school employees is an unresolved issue at the IRS. The fundamental issue, are these individuals private or government employees, will depend on final IRS regulations. ORSC staff comments on the amendments to H.B. 2 are therefore conditional. It is likely that, no matter which direction the IRS goes, the H.B. 2 amendments will need refinement in one of the following ways:

1) *IF* these community school employees are deemed government employees, then none should participate in Social Security, for the state has no mechanism to permit Social Security coverage of government employees. If the state wishes to provide Social Security coverage to government employees, then an amendment to the state's Section 218 Agreement would be advised.

2) *IF*, on the other hand, these community school employees are deemed private employees, then none should be permitted to participate in the state retirement systems, unless the systems gain official notification from the IRS that such participation is *de minimus* and will not affect their status as a government plan.

⁶ Government Accountability Office, "Social Security Administration: Management Oversight Needed to Ensure Accurate Treatment of State and Local Government Employees" (GAO-10-938, September 29, 2010), Appendix II, pages 40-41.

⁷ Ohio's Section 218 Agreement provides Social Security coverage for only three groups of local employees: certain City of Cincinnati employees who are members of the Teachers Insurance and Annuity Association, Lucas County Recreation, Inc., and Toledo Mud Hens Baseball Club, Inc.

agreement with a community school located within the district's territory whereby the district and the community school endorse each other's programs, may exercise either or both of the following elections:

(a) To have data regarding the academic performance of students enrolled in that community school combined with comparable data from the schools of the district for the purpose of determining the performance of the district as a whole on the district's report card;

(b) To have the number of students attending that community school noted separately on the district's report card.

The election authorized under division (I)(3)(a) of this section is subject to approval by the governing authority of the community school.

Any municipal school district that exercises an election to combine or include data under division (I)(3) of this section, by the first day of October of each year, shall file with the department documentation indicating eligibility for that election, as required by the department.

(J) The department shall include on each report card the percentage of teachers in the district or building who are highly qualified, as defined by the No Child Left Behind Act of 2001, and a comparison of that percentage with the percentages of such teachers in similar districts and buildings.

(K)(1) In calculating English language arts, mathematics, social studies, or science assessment passage rates used to determine school district or building performance under this section, the department shall include all students taking an assessment with accommodation or to whom an alternate assessment is administered pursuant to division (C)(1) or (3) of section 3301.0711 of the Revised Code.

(2) In calculating performance index scores, rates of achievement on the performance indicators established by the state board under section 3302.02 of the Revised Code, and annual measurable objectives for determining adequate yearly progress for school districts and buildings under this section, the department shall do all of the following:

(a) Include for each district or building only those students who are included in the ADM certified for the first full school week of October and are continuously enrolled in the district or building through the time of the spring administration of any assessment prescribed by division (A)(1) or (B)(1) of section 3301.0710 or division (B) of section 3301.0712 of the Revised Code that is administered to the student's grade level;

(b) Include cumulative totals from both the fall and spring administrations of the third grade English language arts achievement assessment;

(c) Except as required by the No Child Left Behind Act of 2001, exclude for each district or building any limited English proficient student who has been enrolled in United States schools for less than one full school year.

(L) Beginning with the 2015-2016 school year and at least once every three years thereafter, the state board of education shall review and may adjust the benchmarks for assigning letter grades to the performance measures and components prescribed under divisions (C)(3) and (D) of this section.

Sec. 3302.037. The department of education shall conduct a study to evaluate the validity and usefulness of using the "similar students measure," as created by the California charter schools association, to calculate student academic progress, using a regression model to take into account demographic differences, for each public school.

Not later than December 1, 2016, the department shall prepare and submit a report regarding its findings and recommendations to the state board of education and the general assembly in accordance with section 101.68 of the Revised Code.

Sec. 3307.01. As used in this chapter:

(A) "Employer" means the board of education, school district, governing authority of any community school established under Chapter 3314. of the Revised Code, a science, technology,

engineering, and mathematics school established under Chapter 3326. of the Revised Code, college, university, institution, or other agency within the state by which a teacher is employed and paid.

(B)(1) "Teacher" means all of the following:

(a) Any person paid from public funds and employed in the public schools of the state under any type of contract described in section 3311.77 or 3319.08 of the Revised Code in a position for which the person is required to have a license issued pursuant to sections 3319.22 to 3319.31 of the Revised Code;

(b) ~~Any~~ Except as provided in division (B)(2)(b) or (c) of this section, any person employed as a teacher by or faculty member in a community school or a science, technology, engineering, and mathematics school pursuant to Chapter 3314. or 3326. of the Revised Code;

(c) Any person having a license issued pursuant to sections 3319.22 to 3319.31 of the Revised Code and employed in a public school in this state in an educational position, as determined by the state board of education, under programs provided for by federal acts or regulations and financed in whole or in part from federal funds, but for which no licensure requirements for the position can be made under the provisions of such federal acts or regulations;

(d) Any other teacher or faculty member employed in any school, college, university, institution, or other agency wholly controlled and managed, and supported in whole or in part, by the state or any political subdivision thereof, including Central state university, Cleveland state university, and the university of Toledo;

(e) The educational employees of the department of education, as determined by the state superintendent of public instruction.

In all cases of doubt, the state teachers retirement board shall determine whether any person is a teacher, and its decision shall be final.

(2) "Teacher" does not include any of the following:

(a) Any eligible employee of a public institution of higher education, as defined in section 3305.01 of the Revised Code, who elects to participate in an alternative retirement plan established under Chapter 3305. of the Revised Code;

(b) Any person employed by a community school operator, as defined in section 3314.02 of the Revised Code, for whom the operator withholds and pays employee and employer taxes pursuant to 26 U.S.C. 3101(a) and 3111(a), unless the person had contributing service in a community school in the state within one year prior to the later of July 1, 2016, or the date on which the operator for the first time withholds and pays employee and employer taxes pursuant to 26 U.S.C. 3101(a) and 3111(a) for that person;

(c) Any person who would otherwise be a teacher under division (B)(2)(b) of this section who terminates employment with a community school operator and has no contributing service in a community school in the state for a period of at least one year from the date of termination of employment.

(C) "Member" means any person included in the membership of the state teachers retirement system, which shall consist of all teachers and contributors as defined in divisions (B) and (D) of this section and all disability benefit recipients, as defined in section 3307.50 of the Revised Code. However, for purposes of this chapter, the following persons shall not be considered members:

(1) A student, intern, or resident who is not a member while employed part-time by a school, college, or university at which the student, intern, or resident is regularly attending classes;

(2) A person denied membership pursuant to section 3307.24 of the Revised Code;

(3) An other system retirant, as defined in section 3307.35 of the Revised Code, or a superannuate;

(4) An individual employed in a program established pursuant to the "Job Training Partnership Act," 96 Stat. 1322 (1982), 29 U.S.C.A. 1501;

(5) The surviving spouse of a member or retirant if the surviving spouse's only connection to the retirement system is an account in an STRS defined contribution plan.

(D) "Contributor" means any person who has an account in the teachers' savings fund or defined contribution fund, except that "contributor" does not mean a member or retirant's surviving spouse with an account in an STRS defined contribution plan.

(E) "Beneficiary" means any person eligible to receive, or in receipt of, a retirement allowance or other benefit provided by this chapter.

(F) "Year" means the year beginning the first day of July and ending with the thirtieth day of June next following, except that for the purpose of determining final average salary under the plan described in sections 3307.50 to 3307.79 of the Revised Code, "year" may mean the contract year.

(G) "Local district pension system" means any school teachers pension fund created in any school district of the state in accordance with the laws of the state prior to September 1, 1920.

(H) "Employer contribution" means the amount paid by an employer, as determined by the employer rate, including the normal and deficiency rates, contributions, and funds wherever used in this chapter.

(I) "Five years of service credit" means employment covered under this chapter and employment covered under a former retirement plan operated, recognized, or endorsed by a college, institute, university, or political subdivision of this state prior to coverage under this chapter.

(J) "Actuary" means an actuarial professional contracted with or employed by the state teachers retirement board, who shall be either of the following:

(1) A member of the American academy of actuaries;

(2) A firm, partnership, or corporation of which at least one person is a member of the American academy of actuaries.

(K) "Fiduciary" means a person who does any of the following:

(1) Exercises any discretionary authority or control with respect to the management of the system, or with respect to the management or disposition of its assets;

(2) Renders investment advice for a fee, direct or indirect, with respect to money or property of the system;

(3) Has any discretionary authority or responsibility in the administration of the system.

(L)(1) Except as provided in this division, "compensation" means all salary, wages, and other earnings paid to a teacher by reason of the teacher's employment, including compensation paid pursuant to a supplemental contract. The salary, wages, and other earnings shall be determined prior to determination of the amount required to be contributed to the teachers' savings fund or defined contribution fund under section 3307.26 of the Revised Code and without regard to whether any of the salary, wages, or other earnings are treated as deferred income for federal income tax purposes.

(2) Compensation does not include any of the following:

(a) Payments for accrued but unused sick leave or personal leave, including payments made under a plan established pursuant to section 124.39 of the Revised Code or any other plan established by the employer;

(b) Payments made for accrued but unused vacation leave, including payments made pursuant to section 124.13 of the Revised Code or a plan established by the employer;

(c) Payments made for vacation pay covering concurrent periods for which other salary, compensation, or benefits under this chapter or Chapter 145. or 3309. of the Revised Code are paid;

(d) Amounts paid by the employer to provide life insurance, sickness, accident, endowment, health, medical, hospital, dental, or surgical coverage, or other insurance for the teacher or the teacher's family, or amounts paid by the employer to the teacher in lieu of providing the

insurance;

(e) Incidental benefits, including lodging, food, laundry, parking, or services furnished by the employer, use of the employer's property or equipment, and reimbursement for job-related expenses authorized by the employer, including moving and travel expenses and expenses related to professional development;

(f) Payments made by the employer in exchange for a member's waiver of a right to receive any payment, amount, or benefit described in division (L)(2) of this section;

(g) Payments by the employer for services not actually rendered;

(h) Any amount paid by the employer as a retroactive increase in salary, wages, or other earnings, unless the increase is one of the following:

(i) A retroactive increase paid to a member employed by a school district board of education in a position that requires a license designated for teaching and not designated for being an administrator issued under section 3319.22 of the Revised Code that is paid in accordance with uniform criteria applicable to all members employed by the board in positions requiring the licenses;

(ii) A retroactive increase paid to a member employed by a school district board of education in a position that requires a license designated for being an administrator issued under section 3319.22 of the Revised Code that is paid in accordance with uniform criteria applicable to all members employed by the board in positions requiring the licenses;

(iii) A retroactive increase paid to a member employed by a school district board of education as a superintendent that is also paid as described in division (L)(2)(h)(i) of this section;

(iv) A retroactive increase paid to a member employed by an employer other than a school district board of education in accordance with uniform criteria applicable to all members employed by the employer.

(i) Payments made to or on behalf of a teacher that are in excess of the annual compensation that may be taken into account by the retirement system under division (a)(17) of section 401 of the "Internal Revenue Code of 1986," 100 Stat. 2085, 26 U.S.C.A. 401(a)(17), as amended. For a teacher who first establishes membership before July 1, 1996, the annual compensation that may be taken into account by the retirement system shall be determined under division (d)(3) of section 13212 of the "Omnibus Budget Reconciliation Act of 1993," Pub. L. No. 103-66, 107 Stat. 472.

(j) Payments made under division (B), (C), or (E) of section 5923.05 of the Revised Code, Section 4 of Substitute Senate Bill No. 3 of the 119th general assembly, Section 3 of Amended Substitute Senate Bill No. 164 of the 124th general assembly, or Amended Substitute House Bill No. 405 of the 124th general assembly;

(k) Anything of value received by the teacher that is based on or attributable to retirement or an agreement to retire;

(l) Any amount paid by the employer as a retroactive payment of earnings, damages, or back pay pursuant to a court order, court-adopted settlement agreement, or other settlement agreement, unless the retirement system receives both of the following:

(i) Teacher and employer contributions under sections 3307.26 and 3307.28 of the Revised Code, plus interest compounded annually at a rate determined by the board, for each year or portion of a year for which amounts are paid under the order or agreement;

(ii) Teacher and employer contributions under sections 3307.26 and 3307.28 of the Revised Code, plus interest compounded annually at a rate determined by the board, for each year or portion of a year not subject to division (L)(2)(l)(i) of this section for which the board determines the teacher was improperly paid, regardless of the teacher's ability to recover on such amounts improperly paid.

(3) The retirement board shall determine both of the following:

(a) Whether particular forms of earnings are included in any of the categories enumerated in

this division;

(b) Whether any form of earnings not enumerated in this division is to be included in compensation.

Decisions of the board made under this division shall be final.

(M) "Superannuate" means both of the following:

(1) A former teacher receiving from the system a retirement allowance under section 3307.58 or 3307.59 of the Revised Code;

(2) A former teacher receiving a benefit from the system under a plan established under section 3307.81 of the Revised Code, except that "superannuate" does not include a former teacher who is receiving a benefit based on disability under a plan established under section 3307.81 of the Revised Code.

For purposes of sections 3307.35 and 3307.353 of the Revised Code, "superannuate" also means a former teacher receiving from the system a combined service retirement benefit paid in accordance with section 3307.57 of the Revised Code, regardless of which retirement system is paying the benefit.

(N) "STRS defined benefit plan" means the plan described in sections 3307.50 to 3307.79 of the Revised Code.

(O) "STRS defined contribution plan" means the plans established under section 3307.81 of the Revised Code and includes the STRS combined plan under that section.

(P) "Faculty" means the teaching staff of a university, college, or school, including any academic administrators.

Sec. 3309.011. "Employee" as defined in division (B) of section 3309.01 of the Revised Code, does not include ~~either any~~ of the following:

(A) Any person having a license issued pursuant to sections 3319.22 to 3319.31 of the Revised Code and employed in a public school in this state in an educational position, as determined by the state board of education, under programs provided for by federal acts or regulations and financed in whole or in part from federal funds, but for which no licensure requirements for the position can be made under the provisions of such federal acts or regulations;

(B) Any person who participates in an alternative retirement plan established under Chapter 3305. of the Revised Code;

(C) Any person who elects to transfer from the school employees retirement system to the public employees retirement system under section 3309.312 of the Revised Code;

(D) Any person whose full-time employment by the university of Akron as a state university law enforcement officer pursuant to section 3345.04 of the Revised Code commences on or after ~~the effective date of this amendment~~ September 16, 1998;

(E) Any person described in division (B) of section 3309.013 of the Revised Code.

Sec. 3309.013. (A) As used in this section, "operator" has the same meaning as in section 3314.02 of the Revised Code.

(B) "Employee," as defined in division (B) of section 3309.01 of the Revised Code, does not include either of the following:

(1) Any person initially employed on or after July 1, 2016, by a community school operator and for whom the operator withholds and pays employee and employer taxes pursuant to 26 U.S.C. 3101(a) and 3111(a) beginning with the first paycheck after commencing initial employment;

(2) Except as provided in division (C) of this section, any person who is a former employee of a community school operator who is reemployed on or after July 1, 2016, by that operator and for whom the operator withholds and pays employee and employer taxes pursuant to 26 U.S.C. 3101(a) and 3111(a) beginning with the first paycheck after commencing reemployment with that operator.

(C) Division (B)(2) of this section does not apply to either of the following:

(1) Any person who was employed by the same operator at any time within the period of July 1, 2015, to June 30, 2016, and whose date of reemployment is before July 1, 2017;

(2) Any person to whom both of the following apply:

(a) The person was employed by the same operator at any time in the twelve-month period preceding the date the operator for the first time withholds and pays employee and employer taxes pursuant to 26 U.S.C. 3101(a) and 3111(a) on behalf of its employees and had previously only contributed to the school employees retirement system;

(b) The person's date of reemployment is not more than twelve months after the date the operator for the first time withholds and pays employee and employer taxes pursuant to 26 U.S.C. 3101(a) and 3111(a).

Sec. 3313.12. (A) Each member of the educational service center governing board may be paid such compensation as the governing board provides by resolution, provided that any such compensation shall not exceed one hundred twenty-five dollars a day plus mileage both ways, at the rate per mile provided by resolution of the governing board, for attendance at any meeting of the board. No member of an educational service center governing board shall receive in compensation under this division a total amount greater than five thousand dollars per year for service on the governing board. Such compensation and the expenses of the educational service center superintendent, itemized and verified, shall be paid from the educational service center governing board fund upon vouchers signed by the president of the governing board.

(B) The board of education of any city, local, or exempted village school district may provide by resolution for compensation of its members, provided that such compensation shall not exceed one hundred twenty-five dollars per member for meetings attended. No member of a school district board of education shall receive in compensation under this division a total amount greater than five thousand dollars per year for service on the board of education. The board may provide by resolution for the deduction of amounts payable for benefits under section 3313.202 of the Revised Code.

(C) Each member of a district board or educational service center governing board may be paid such compensation as the respective board provides by resolution for attendance at an approved training program, provided that such compensation shall not exceed sixty dollars a day for attendance at a training program three hours or fewer in length and one hundred twenty-five dollars a day for attendance at a training program longer than three hours in length.

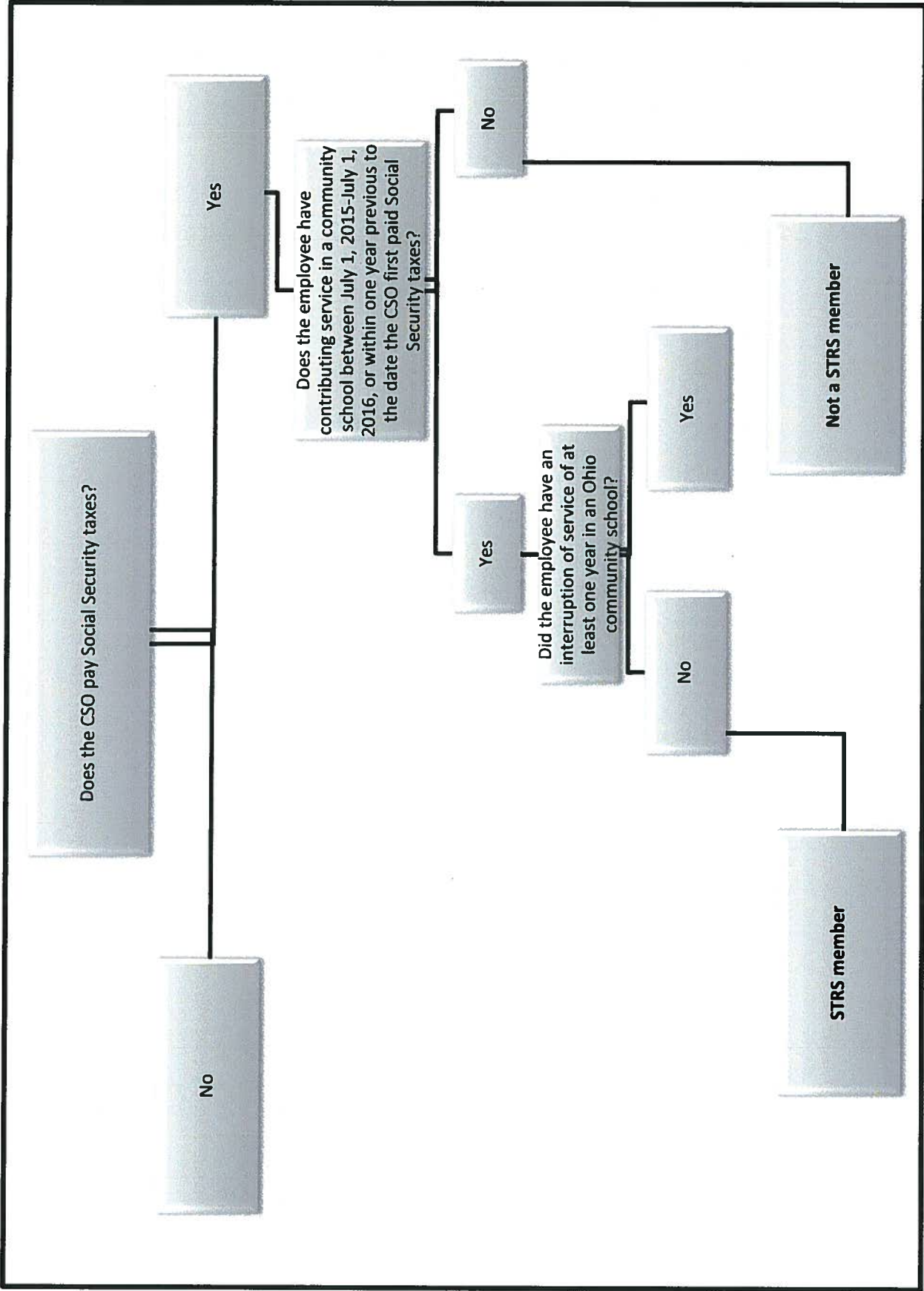
Sec. 3313.131. No person who is a member of the governing authority of a community school established under Chapter 3314. of the Revised Code shall be a member of a board of education.

Sec. 3314.011. (A) Every community school established under this chapter shall have a designated fiscal officer. Except as provided for in division (C) of this section, the fiscal officer shall be employed by or engaged under a contract with the governing authority of the community school.

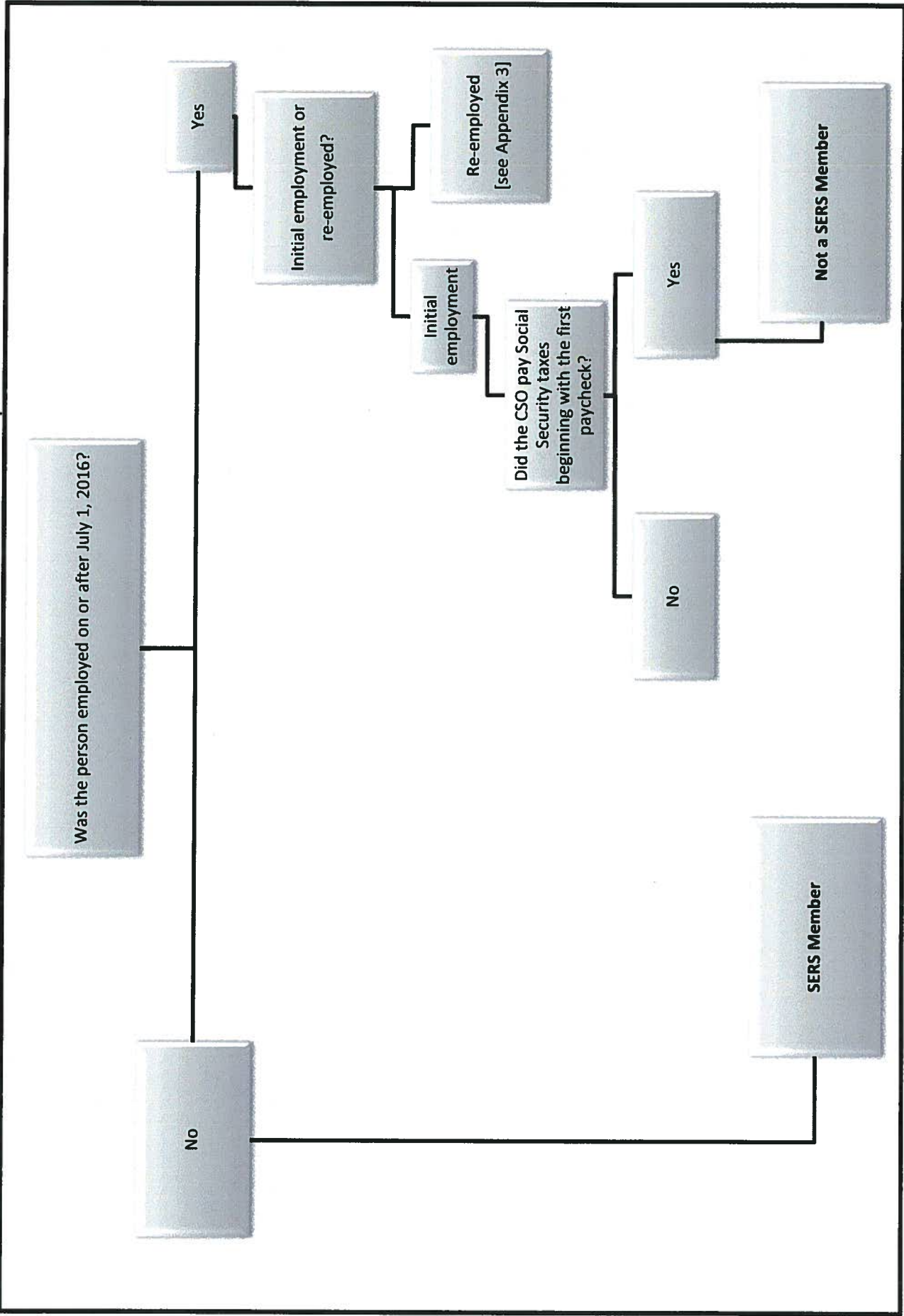
(B) The auditor of state may shall require by rule that the fiscal officer of any community school, before entering upon duties as fiscal officer of the school, execute a bond in an amount and with surety to be approved by the governing authority of the school, payable to the state, conditioned for the faithful performance of all the official duties required of the fiscal officer. Any such The bond shall be deposited with the governing authority of the school, and a copy thereof, certified by the governing authority, shall be filed with the county auditor.

(C) Prior to assuming the duties of fiscal officer, the fiscal officer designated under this section shall be licensed under section 3301.074 of the Revised Code. Any person serving as a fiscal officer of a community school on the effective date of this amendment March 22, 2013, who is not licensed as a treasurer shall be permitted to serve as a fiscal officer for not more than one year following the effective date of this amendment March 22, 2013. Beginning on that date and thereafter, no community school shall permit any individual to serve as a fiscal officer

Appendix 1: Employees of Community School Operators (CSO): STRS Membership Determination



Appendix 2: Employees of CSO: SERS Membership Determination



Appendix 3: Employees of CSO: SERS Membership Determination, Re-employed on or after July 1, 2016

