



STATE OF NEW MEXICO  
*Educational Retirement Board*

701 CAMINO DE LOS MARQUEZ  
P.O. Box 26129  
SANTA FE, NEW MEXICO 87502-0129  
PHONE: (505) 827-8030  
FAX: (505) 827-1855

MEMORANDUM

TO: NMERB Local Administrative Units

FROM: Roderick Ventura, NMERB General Counsel

A handwritten signature in blue ink, appearing to be "RV" with a checkmark, located to the right of the "FROM" line.

RE: Independent Contractors and Return to Work post-retirement

Date: July 12, 2017, revised July 30, 2019

**NOTE: This memo has been revised to incorporate changes in legislation from the 2019 legislature.**

Recently, it has come to NMERB's attention that some NMERB employers ("Local Administrative Units" or "LAUs") have been or are considering the idea of using third-party entities to fulfill their staffing needs. These third-party entities hire or contract with recent NMERB retirees to fill positions at LAUs, and sometimes place such retirees into the same or substantially similar positions they held prior to retirement. In many of these circumstances, such a strategy does not comply with NMERB statute and rule, and can place the retiree in a situation in which their retirement benefits may be terminated and any benefits paid to the employee during such an arrangement must be paid back.

In order to avoid potential problems, NMERB is providing this review of the return-to-work provisions, with the above scenario in mind.

**I. General Provisions Regarding Return To Work**

Under New Mexico law, an NMERB member is not allowed to be in retirement status and at the same time "be engaged in employment" with a Local Administrative Unit (LAU) unless the employment falls within an exception established by statute or rule of NMERB. Section 22-11-27(C) NMSA 1978.

Currently, there are two exceptions that allow for retired NMERB members to work for LAUs while still receiving retirement benefits: the Return to Work Program and the provision allowing retirees to work .25 FTE or less.

### **1) Return to Work Program**

Under Section 22-11-25.1 NMSA 1978, a retired member may work with an LAU under the Return to Work Program and continue receiving retirement benefits. To qualify for the Return to Work Program, a member must not render service to a local administrative unit for at least twelve consecutive months after the date of retirement. If an NMERB retiree becomes employed with a local administrative unit without this twelve month layout, the retiree will have their retirement benefits suspended. The retiree must submit a Return to Work application and receive approval from NMERB before beginning work for an LAU again.

A retired member may also return to employment with a local administrative unit and continue receiving their retirement benefit as long as they only work the equivalent of .25 FTE or less. A retired member must submit an application in regards to either of these two options. The application can be found on the NMERB website at [http://www.nmerb.org/pdfs/RTW%20Application\\_6\\_19.pdf](http://www.nmerb.org/pdfs/RTW%20Application_6_19.pdf).

## **II. Independent Contractors**

NMERB retirees who become independent contractors fall under a different circumstance than the exceptions listed above. An NMERB retiree who provides services to an LAU as an independent contractor does not have to suspend his or her retirement benefit. But, if a retiree wants to eventually return to employment for an LAU under the Return to Work program, the time spent working as an independent contractor for an LAU cannot be used as part of the required twelve month layout period.

Further, a retiree should carefully consider whether a work arrangement with an LAU meets all the legal tests for an independent contractor relationship. Simply changing a retiree's title to "independent contractor" is not sufficient. First, there must have been a bona fide termination of employment by the employee brought about by retirement. Second, the retiree must satisfy all the legal factors for being an independent contractor under New Mexico and federal law. This is why NMERB requires retirees who wish to become independent contractors with LAUs to submit an Independent Contractor Determination Application before engaging in work with an LAU as an independent contractor.

### **1) Bona fide termination**

NMERB is required to comply with Internal Revenue Code ("Code") provisions governing the NMERB retirement plan. The NMERB retirement plan is a tax-qualified defined benefit pension plan under Code section 401(a). Section 401(a) of the Code provides that a trust forming part of a pension plan of an employer constitutes a qualified trust only if the requirements of section 401(a) are met.

Federal regulations dictate that a pension plan under section 401(a) is a plan established and maintained primarily to provide systematically for the payment of benefits over a period of years, usually for life, *after retirement*. Treasury Regulation § 1.401-1(b)(1)(i)(emphasis added).

The Internal Revenue Service (IRS) has found that in accordance with this provision, because a qualified pension plan is generally not permitted to pay benefits before retirement, an employee who “retires” with the understanding between the employer and employee that upon retirement the employee will immediately return to service with the employer has not legitimately retired. See IRS Private Letter Ruling (“PLR”) 201147038.

In PLR 201147038 the IRS found that employees who “retire” on one day, then return the next or soon after, with the understanding between the employee and employer that they are not separating from service with the employer, are not legitimately retired. The IRS found that such “retirements” violate section 401(a) of the IRS Code and may result in disqualification of the plan under section 401(a)(1). The IRS found that if both the employer and employee know at the time of “retirement” that the employee will, with reasonably certainty, continue to perform services for the employer, a termination of employment has not occurred upon “retirement” and the employee has not legitimately retired. Thus post retirement return-to-work contracts, need to be considered carefully. Factors indicating that a retiree did not intend a bona-fide termination prior to receiving retirement benefits include, but are not limited to: contracts that create a working relationship between a retiree and the same employer the retiree worked for pre-retirement; retiree contracts that are effective immediately or soon after an employee’s retirement with little or no break in service; contracts that are negotiated prior to the retirement of the employee; and retirees returning to work in the very same or similar position they held prior to retirement.

Thus, state law requires NMERB retirees to either lay out twelve consecutive months after retirement before returning to work or to reduce their post-retirement employment to .25 FTE or less. These are objective means of determining that a bona fide termination of employment has occurred.

## **2) True Independent Contractor**

In addition to requiring a bona fide termination under the IRS code, NMERB rules provide that in determining whether an individual is an independent contractor as opposed to an employee, NMERB will consider a number of factors including “whether the person satisfies internal revenue service guidelines for determining that an individual is an independent contractor rather than an employee.” Subsection D of 2.82.2.11 NMAC. The factors detailed in IRS guidance include facts that indicate behavioral control, financial control, and the type of relationship between the parties. See *Employer’s Supplemental Tax Guide*, pgs. 7-10, IRS Publication 15-A (2016); and *Independent Contractor or Employee*, IRS Publication 1779 (Rev. 3-2012).

If a retiree’s employment arrangement does not meet the legal test for independent contractor in accordance with these factors, the retiree will be considered an employee of the LAU. Although each retiree’s circumstances must be looked at individually, the key common factors are the amount of control an employer has over an independent contractor. Other factors looked at when considering whether a retiree is an independent contractor include, but are not limited to the extent to which the retiree makes his or her services available to the relevant market; the permanency of the relationship between the employer and the retiree, and whether services provided are a key aspect of regular business activity. No one factor determines whether an

individual is an independent contractor or an employee – NMERB will look at all factors and make a determination.

Thus, while there are some tasks or projects that could be performed by independent contractors, many common jobs at LAUs cannot. Examples of jobs that are unlikely to be suitable for performance by an independent contract include:

- superintendent
- teacher
- administrator
- coach
- principal/assistant principal
- administrative support personnel.

NMERB is aware that there are third-party entities that may be marketing to NMERB retirees and offering the opportunity to contract with them after retirement. Retirees may believe that they may contract with these entities and then be placed in a position with an LAU as an independent contractor of the third-party entity rather than as an employee or contractor with the LAU. Retirees may be led to believe that this arrangement will allow them to perform the same duties that they performed before retiring, or to otherwise work for an LAU after retirement without suspending their retirement benefits. Retirees may believe this even though they are performing these duties immediately or soon after retirement and holding positions that place them under the behavioral and financial control of the LAU.

NMERB has determined that if a member contracts with one of these third-party entities and is placed in a position with an LAU, they are not automatically exempt from the restrictions of post-retirement employment. The employee's individual situation must be analyzed to consider whether they have undergone a bona-fide termination prior to receiving retirement benefits. Further, they must have a legitimate independent contractor status and not an employer-employee relationship. In other words, an employee cannot engage in a contract with an LAU or a third-party entity merely as a way to avoid return-to-work requirements under NMERB statute and rule.