SENATE BILL REPORT
HB 2441

As of February 21, 2012

Title: An act relating to limiting the impact of excess compensation on state retirement system contribution rates.

Brief Description: Limiting the impact of excess compensation on state retirement system contribution rates by redefining excess compensation.

Sponsors: Representatives Bailey and Alexander.

Brief History: Passed House: 2/14/12, 97-1.
Committee Activity: Ways & Means: 2/20/12.

SENATE COMMITTEE ON WAYS & MEANS

Staff: Erik Sund (786-7454)

Background: Calculation of monthly defined benefit retirement allowances in the plans and systems of the Washington State Retirement Systems is most commonly done through a multiplication of average pension-eligible compensation, referred to in the retirement plans as reportable compensation or compensation earnable, over a plan's average final compensation period by the percentage of pay that a retiree has earned through years of service in a member's retirement plan.

For example, a member of the Public Employees' Retirement System Plan 2 begins calculation of retirement benefit on the highest five consecutive years of reportable compensation, multiplied by the number of years of service in the plan, with each year earning the member 2 percent of the average final salary in retirement allowance. If the member earned a final average salary of $70,000 per year over the five-year period, and had 25 years of service credit, the member would be eligible for a $35,000 per year retirement allowance at age 65, without any other adjustments being taken into account. A variety of other factors, such as the choice of survivor benefits or early retirement, can adjust the final calculated amount of an individual member's retirement allowance.

Since 1984 excess compensation has been defined in the pension statutes as consisting of specific types of reportable compensation when the payment increases the member's retirement allowance. If reportable compensation included in a retiree's retirement allowance calculation qualifies as excess compensation, then the applicable employer is responsible for

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the resulting liability to the pension fund. Without such an employer payment, the excess compensation-related liability would effectively be spread amongst all employers, and paid for through the contribution rate structure for the plan.

The employer paying employees reportable compensation that qualifies as excess compensation is liable to the pension fund for the total estimated cost of all present and future retirement benefits attributable to the excess compensation. Definition of payments as excess compensation does not affect the calculation of individual pension benefits.

Excess compensation includes the following payments, when used in the calculation of the member's retirement allowance:

- a cashout of more than 240 hours of annual leave;
- a cashout of any other form of leave;
- a cashout in lieu of the accrual of annual leave;
- any payment added to salary or wages, concurrent with a reduction of annual leave;
- any payment that exceeds twice the regular daily or hourly rate of pay;
- a payment for, or in lieu of, any personal expenses or transportation allowance, to the extent that the payment qualifies as reportable compensation in the member's retirement system; or
- any termination or severance payment.

The excess compensation statutes apply to all of the retirement systems administered by the Department of Retirement Systems, including the Public Employees' Retirement System, the Teachers' Retirement System, the School Employees' Retirement System, the Law Enforcement Officers' and Firefighters' Retirement System, and the Washington State Patrol Retirement System.

Summary of Bill: An additional category of excess compensation is created to include the portion of total reportable compensation used in the calculation of the employee's retirement allowance that exceeds one and one-half times the employee's reportable compensation over the calculation period, excluding reportable compensation from overtime, bonuses, cash outs of any form of leave, or lump-sum payments.

Appropriation: None.

Fiscal Note: Available.

Committee/Commission/Task Force Created: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: Recently we've seen individuals retire with benefits based on two and three times their basic compensation. This bill won't change the benefits that employees received, but will change who pays for them by sending a bill to employers to cover the costs of pension spiking. Currently, these pension costs are paid by all employers and also by members. Please consider delaying the effective date of this legislation. Employer behavior will change under this bill; however, employers need some time to make changes to their current practices and prepare for these changes.

Persons Testifying: PRO: Representative Bailey, prime sponsor; Julie Murray, Office of Financial Management.