

Excess Compensation

Issue

Some policy makers may question whether current statutory provisions are sufficient to mitigate the potential impact of excess compensation on the state's retirement systems. These policy makers may seek to expand the definition of excess compensation to include additional compensation amounts.

This raises the following key question for policy makers considering this issue:

- ❖ Is the current definition of excess compensation sufficient, or should it be expanded?

The Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board has requested joint coordination with the SPP on any legislation for this issue.

Background

Statute defines certain types of employee compensation as "excess compensation." This includes overtime and bonuses exceeding twice the regular rate of pay and certain other payments. Employers paying excess compensation are generally billed for the increased costs to the pension system resulting from the excess compensation. According to the Department of Retirement Systems (DRS), few employer billings are triggered for overtime or bonuses under current excess compensation provisions.

During the 2012 Legislative Session, a bill was introduced that would have expanded the definition of excess compensation in all the state-administered retirement systems to capture additional compensation related to overtime, bonuses, leave cash outs, and lump sum payments. The bill ([HB 2441](#)) did not pass the Legislature.

Policy Highlights

- ❖ Excess compensation can create unexpected costs for the pension system, which may impact intergenerational equity.
- ❖ Excess compensation provisions are designed to mitigate financial impacts on the retirement systems. They do not prohibit any pay practices or directly impact benefit calculations.
- ❖ The impact of overtime and bonuses on members' benefits is not determinable at this time due to lack of data. However, overtime and bonuses that are a relatively stable percentage of compensation over a career do not create unexpected costs for the pension systems.
- ❖ Overtime and bonuses may serve Human Resource needs.

- ❖ Current members likely have contractual rights to use excess compensation in the calculation of their pensions.
- ❖ Changing employer billings for excess compensation does not impact contractual rights.
- ❖ Increasing employer billings for excess compensation:
 - ◇ May impact recruitment and retention by providing an incentive for employers to change certain pay practices.
 - ◇ Has implications for cost sharing and plan costs.

Committee Activity

Excess compensation was discussed in the general educational briefing on pension spiking at the May SCPP meeting. The committee received an initial policy briefing on excess compensation and [HB 2441](#) at the October meeting. The committee held a public hearing on [HB 2441](#) in November.

Following the public hearing on [HB 2441](#), the committee directed staff to work with the DRS to prepare a revised bill draft. The revision is to address stakeholder concerns around possible billings for high-overtime occupations where the overtime is not creating unexpected costs for the retirement systems.

Revised Bill Draft

A revised bill draft expanding the definition of excess compensation is attached. The revised draft includes a new trigger for billing which:

- ❖ Captures increases in Average Final Compensation of more than 50 percent from the prior period as a result of overtime, bonuses, leave cash outs, and lump sum payments.
- ❖ Will likely generate more employer billings than under current law for a relatively small percentage of benefit calculations.
- ❖ Avoids billing where overtime is not creating unexpected costs.
- ❖ Will likely result in an indeterminate savings to the retirement systems.

Next Steps

A public hearing with possible executive action on the revised bill draft is scheduled at the December meeting.