

Late Employer Reporting/Dolan

Issue

A recent State Supreme Court case (*Dolan v. King County*¹) added approximately 900 existing contract employees to the Public Employees' Retirement System (PERS). As a result, those employees were awarded retroactive credit for service earned back to the beginning of their careers. This results in late reporting of an unprecedented size and cost to the system. The current settlement agreement would pass the cost to other plan members and employers.

Background

Impact To Plan Funding

Late and under-reporting of service creates a cost to the retirement system due to the shortening, or removal, of prefunding.

The funding policies for all of Washington's open retirement plans require regular contributions over time (known as systematic actuarial funding). These regular contributions are invested, and the interest earned helps offset the total cost of benefits.

Markets will vary, but generally when the time available for investing is shortened the investment returns will be smaller. Thus, the offset to plan costs will be smaller as well.

Unless the lost investment returns are offset with additional contributions, the loss is absorbed as a cost to the system. In other words, that cost is passed to all other members and employers in the form of larger contribution rates.

Administrative Process

Service is reported on a monthly cycle, and plan contributions are made when service is reported. For example, the service for a given month must be reported, and the contributions paid, by the fifteenth of the following month.²

Contributions can arrive late because the payments are made late, or because the service was either reported late or under-reported.

When contributions are received late, the Department of Retirement Systems (DRS) has discretionary authority³ to bill the responsible employer for interest on those

¹ *Dolan v. King County*, 172 Wn. 2d 299 (2011).

² See the [DRS Employer Handbook](#) for more information.

³ RCW 41.50.125.

contributions (in other words, collecting the contributions that should have been made plus interest.)

For example, DRS charges 12 percent annual interest on late payments where service is reported in a timely basis, but the contributions are not made on time.

Legal History

Original Court Case

In 2006, an employee of King County's Office of the Public Defender (OPD) filed suit on behalf of himself and a similarly situated class of employees. In brief, the suit alleged that the OPD employees are treated no different from other agency employees of King County, and are thus entitled to membership in PERS.

The OPD is a private, non-profit corporation. It is one of several similar corporations on contract with the county to provide public defense legal representation to indigent citizens.

According to the court, over time the county has exerted greater and greater control over the privately-held public defender agencies it contracts with. For example, the county controls the OPD's budget, and the ability to hire and fire employees.⁴

The court held that King County's exertion of control over many aspects of the OPD rendered the OPD an arm and agency of the county. As a result, approximately 900 employees of public defender organizations were made eligible for state retirement system membership.⁵

Settlement

After the Supreme Court determined that the employees were eligible for retroactive PERS membership, the county and employees crafted a settlement to determine the practicalities of entering those members into PERS.

Some of the settlement terms at issue are as follows. The settlement agreement:

- ❖ Calculated the amount of late contributions owed by King County.
- ❖ Waived the interest to be paid on the late employer and employee contributions.
- ❖ Required the PERS trust fund to pay the attorney's fees.
 - Or alternatively, King County could pay the attorney's fees out of the employee contributions it owed to the PERS trust fund. DRS would then be expected to make up the

⁴ See *Dolan*, 172 Wn. 2d at 319, for a more complete list of the types of control that impacted the court's decision.

⁵ For reference, the court did not mandate PERS membership, but stated that the employees were eligible for PERS membership.

difference by deducting money from class members' pension checks when they retire.

- ❖ Waived the statute of limitations on the action.

Intervention/Appeal

The settlement was ostensibly between the county and the employees, and DRS was never made a party to the case. However, the terms of the settlement bound DRS, impacted the PERS trust fund, and would create a cost to the retirement system. In response, DRS filed to intervene and challenge the settlement.

As of October 13, 2014, this case is currently on appeal with the Court of Appeals, Division 2. Oral arguments were held on September 4, 2014.

The main legal question on appeal is whether or not a settlement agreement can bind an entity that was never made party to the case (e.g. DRS) to a settlement agreement which requires that same non-party to bear the costs of the settlement.

Fiscal Impacts

The fiscal impacts from this case are unknown at this time. The Office of the State Actuary (OSA) typically relies on DRS to obtain raw data from respective employers, and prepare that data for analysis. As of October 13, 2014, OSA does not have the needed data.

Legislation

Passed: Plan Membership

The Legislature responded to the *Dolan* decision by enacting EHB 2771 (2012 c 236). This bill aimed to prevent similar outcomes by stating that employees of for-profit and not-for-profit corporations providing services under government contracts are not eligible for membership in Washington's retirement systems.

While the bill states that it is "curative and remedial", it explicitly has no impact on the *Dolan* decision.

Proposed: Late Reporting

In the 2013 and 2014 Sessions, the Legislature considered SHB 2018 (2013). In both sessions of the biennium (2013 and 2014), this bill made it to the Senate floor, but did not pass.

This bill would have required the Pension Funding Council (PFC) to adopt employer-specific rates whenever either⁶ of two conditions are present:

1. Contributions are made other than immediately after the service is rendered; and/or
2. Those contributions are so insufficient that they cause an increase in contribution rates for other employers or employees within a retirement system.

The employer-specific rates must be sufficient to ensure other employers and employees do not bear the cost of lost investment returns or interest resulting from the late contributions.

A fiscal note was prepared (and updated in 2014) for SHB 2018. However, the fiscal note does not provide a best estimate cost due to a lack of data regarding:

- ❖ The *Dolan* impact specifically.
- ❖ The likelihood that future incidents of late reporting will be of sufficient magnitude to trigger the additional rate.

As such, the fiscal note instead offered a hypothetical example to illustrate the potential impact. Additional data is required before a more detailed and accurate estimate can be prepared.

Committee Activity

The Executive Committee scheduled this briefing for the October 21, 2014, meeting.

Staff Contact

Aaron Gutierrez, MPA, JD
Senior Policy Analyst
360-350-9779

aaron.gutierrez@leg.wa.gov

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⁶ The original bill (HB 2018) said both conditions must be present to trigger the rate. The most recent version of the bill (SHB 2018) said either must be present.