

# SENATE BILL REPORT

## EHB 2771

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As of February 23, 2012

**Title:** An act relating to employer and employee relationships under the state retirement systems.

**Brief Description:** Addressing employer and employee relationships under the state retirement systems.

**Sponsors:** Representatives Pettigrew, Cody and Springer.

**Brief History:** Passed House: 2/13/12, 83-14.

**Committee Activity:** Ways & Means: 2/22/12.

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### SENATE COMMITTEE ON WAYS & MEANS

**Staff:** Erik Sund (786-7454)

**Background:** The Department of Retirement Systems (DRS) was created in 1976 to administer the various retirement systems that provide benefits for state and local government employees in Washington, collectively referred to as the Washington State Retirement Systems (retirement systems). Retirement systems include the Public Employees' Retirement System (PERS), the Teachers' Retirement System (TRS), the School Employees' Retirement System (SERS), the Law Enforcement Officers' and Fire Fighters' System (LEOFF), the Washington State Patrol Retirement System, and the Public Safety Employees' Retirement System (PSERS).

The retirement systems administered by DRS are limited to government employees under the federal Internal Revenue Code. By operating the retirement systems in conformance with these federal laws, certain employer and employee contributions, as well as investment earnings upon those contributions, receive preferential individual federal income tax treatment for their employees. A retirement system or retirement plan operated in conformance with federal rules is commonly referred to as a qualified plan.

A private employer entity acting as a governmental contractor may be found under federal tax law to be an instrumentality of a public agency if specified criteria are met. The employees of a private nonprofit or for-profit entity that does not meet the federal law definition of an instrumentality of a public agency may not participate in a federal tax law-qualified governmental retirement plan such as PERS.

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

If employees of a private nonprofit entity that the Internal Revenue Service does not regard as an agency or instrumentality of a public agency are included in the PERS plan, it may adversely affect the qualified status of the plan and potentially all of the participants in the plan.

Under federal and state law, whether an individual may be considered an employee, rather than an independent contractor, depends on a set of behavioral, financial, and business relationship factors. The tests for an employment relationship with a worker are similar under state and federal law. These factors are considered alongside other concerns, such as whether the entity has a right to control what the worker does, and how the worker does it; whether there are written contracts between the entity and the worker; and whether employee-type benefits like pensions and health benefits are exchanged between them. For purposes of the state retirement systems, the factors considered in evaluating an employer-employee relationship are detailed in WAC 415-02-110.

In January 2012 the Supreme Court of Washington ruled upon reconsideration in *Dolan v. King County*, Case No. 82842-3. The court ruled that employees of several private nonprofit public defender agencies which provide services to King County by contract are also employees of King County for purposes of PERS, and that King County has such a right of control over the defender organizations that they are arms and agencies of the county.

**Summary of Bill:** The intent of the Legislature in providing retirement systems is not to provide eligibility to the employees of government contractors. The Legislature intends to more clearly state that employees of for-profit and not-for-profit corporations providing services under government contracts are not eligible for membership in the retirement systems. The act is curative and remedial, but shall have no application to the Supreme Court of Washington's decision in *Dolan v. King County*.

For PERS, TRS, SERS, PSERS, and LEOFF, the term employer in regards to the retirement system does not include a government contractor. Government contractors are defined to include partnerships, limited liability companies, for-profit and nonprofit corporations, or persons, that provide services pursuant to a contract with a retirement system employer.

The determination of whether an employer-employee relationship exists is not based on the relationship between a government contractor and a retirement system employer, but solely on the relationship between a government contractor's employee and a retirement system employer.

**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: The creation of retirement systems for public employees and the determination of criteria for eligibility for those systems are legislative prerogatives. In the past, certain employees of certain non-profit entities were enrolled in the state plans, but that was changed. The public defenders covered by the *Dolan* case were ruled to be eligible for PERS by the Washington Supreme Court, based largely on the definition of employer; however, these employees were very closely controlled by the county. This bill protects the *Dolan* class but states that other government contractors aren't eligible for PERS unless the legislature acts to authorize their membership. This bill has one clear goal: the prospective clarification of the relationship between government agencies and contract employees. This bill doesn't undo the *Dolan* decision or reduce the rights of the employees covered by that case. The *Dolan* decision is broad and unclear, which is why the legislature joined cities, counties, and prosecuting attorneys in requesting reconsideration last summer. This bill is narrowly constructed to preserve the authority of the Legislature to define and clarify the terms of eligibility for state retirement systems. This legislation won't change the Employee Misclassification Act, since it is purely about pension eligibility.

CON: While we appreciate the protection provided to the *Dolan* class in the amended form of this bill, this bill does not address what the courts have ruled. The Washington Supreme Court did not rule that government contractors are entitled to PERS membership; instead, it issued a very narrow decision stating that these entities are actually arms and agencies of King County and, therefore, that public defenders are not actually government contractors. Actual facts control legal matters, not labels. Since this bill is unnecessary, we ask that you oppose it. This bill would make it easier for government agencies to create captive corporations to outsource government employee jobs. Contracting out hides the true size of government payrolls and makes government less transparent. This legislation would create two tiers of public employees: one that enjoys benefits and prospects for advancement, and another that does not. We are not convinced of the need to move forward with this bill. We are thankful for the carve-out for the *Dolan* case, but we don't want to inadvertently harm the rights of future employees.

**Persons Testifying:** PRO: Senator Fraser; Genesee Adkins, King County; Monty Cobb, WA Assn. of County Officials; Scott Merriman, WA State Assn. of Counties; David Nelsen, Department of Retirement Systems.

CON: Lani Todd, Service Employees International Union; Lynn Prunhuber, Bendich, Stobaugh, and Strong; David West, Center for a Changing Workforce.