

HOUSE BILL REPORT

HB 2922

As Reported By House Committee On: Appropriations

Title: An act relating to clarifying the trusteeship role of the state investment board and the employee retirement benefits board.

Brief Description: Administering the deferred compensation plan.

Sponsors: Representatives Carlson, H. Sommers, Alexander and Huff; by request of Department of Retirement Systems.

Brief History:

Committee Activity:

Appropriations: 2/2/98, 2/5/98 [DPS].

HOUSE COMMITTEE ON APPROPRIATIONS

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 27 members: Representatives Huff, Chairman; Alexander, Vice Chairman; H. Sommers, Ranking Minority Member; Doumit, Assistant Ranking Minority Member; Gombosky, Assistant Ranking Minority Member; Benson; Carlson; Chopp; Cody; Cooke; Crouse; Grant; Keiser; Kenney; Kessler; Lambert; Linville; Mastin; McMorris; Parlette; Poulsen; Regala; D. Schmidt; Sehlin; Sheahan; Talcott and Tokuda.

Staff: Denise Graham (786-7137).

Background:

Deferred Compensation Plan. The Washington State Deferred Compensation Plan (DCP) is a voluntary income deferral plan for state employees and employees of 276 participating political subdivisions. The DCP was established in 1981 and was administered by the Committee for Deferred Compensation (CDC) from that time until June 30, 1996. Effective July 1, 1996, the duties and responsibilities of the CDC were given to the Department of Retirement Systems (DRS) and to the Employee Retirement Benefits Board (ERBB). The ERBB was created within DRS in 1995 with the enactment of the Teachers' Retirement System Plan III, and was made responsible for selecting investment options for both members of TRS Plan III and participants in the DCP.

Changes in United States Internal Revenue Code. Current state law requires that all monies in the deferred compensation account remain solely the property of the state (until made available to the participating employee or beneficiary) subject to the claims of the state's general creditors. This language exists because of requirements contained in the United States Internal Revenue Code prior to 1996.

In 1996, Congress amended the Internal Revenue Code to require that the assets of government deferred compensation plans be held for the exclusive benefit of employees in a trust, custodial accounts, or qualifying insurance contract. Existing plans have until January 1, 1999, to place their plan assets into the trust, account or insurance contract. If this change is not made, employee contributions under the Deferred Compensation Plan could become subject to federal income taxes beginning in 1999.

Fiduciary Responsibilities. Current state law provides that the ERBB select the investment options for the DCP. Fiduciary counsel for the SIB has advised that the SIB and the ERBB would have unclear and overlapping fiduciary duties with regard to the DCP investments if the SIB were to be made the trustee while the ERBB continued to select the investment options for participants. The ERBB does not have staff to assist with the evaluation of potential investment options nor to monitor the performance of investment options.

Liability. DCP participants can self-direct the investment of their funds within a range of investment options. The federal Employee Retirement Income Security Act (ERISA) and federal Department of Labor (DOL) regulations protect qualified private-sector pension plans against lawsuits from members who are unhappy with the self-directed investment decisions they have made. The ERISA and DOL provisions do not apply to government pension and deferred compensation plans. Under current state law, it is not clear whether members would be permitted to bring legal actions against the SIB, ERBB or the state, based on common law trust and fiduciary principles, if they were unhappy with the returns on their self-directed investments.

Summary of Substitute Bill: The assets of the Washington State Deferred Compensation Plan (DCP) are placed in trust with the Washington State Investment Board for the exclusive use of the plan's participants and beneficiaries.

The SIB is responsible for establishing investment policy and developing participant investment options, after consulting with the Employee Retirement Benefits Board, for the participants in the DCP.

The state is relieved of any liability for losses or deficiencies resulting from participant selection of investment options. The ERBB and the SIB are relieved of liability for any losses that may result from reasonable efforts to implement participant investment options.

The Department of Retirement Systems (DRS), with the approval of the Office of Financial Management, may determine when excess balances in the deferred compensation administrative account are to be transferred to the deferred compensation principal account.

Substitute Bill Compared to Original Bill: The original bill would have made the State Investment Board responsible for the accounting and reporting for the Deferred Compensation Plan assets. The substitute bill provides that DRS will continue to perform the accounting and reporting for the plan, unless it enters into an agreement with SIB for such services.

Appropriation: None.

Fiscal Note: Available.

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

Testimony For: This bill clarifies the roles of the State Investment Board and the Department of Retirement Systems and leverages SIB's investment knowledge.

Testimony Against: None.

Testified: John Charles, Director of the Department of Retirement Systems; and Jim Packer, Washington State Investment Board.