

**LEGISLATIVE SERVICES AGENCY  
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS**

301 State House  
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**FISCAL IMPACT STATEMENT**

**LS 7302**

**BILL NUMBER: HB 1879**

**NOTE PREPARED:** Feb 18, 2003

**BILL AMENDED:**

**SUBJECT:** Conversion of Unused Accrued Leave.

**FIRST AUTHOR:** Rep. Oxley

**FIRST SPONSOR:**

**BILL STATUS:** CR Adopted - 1<sup>st</sup> House

**FUNDS AFFECTED:**  GENERAL  
 DEDICATED  
 FEDERAL

**IMPACT:** State

**Summary of Legislation:** This bill provides that the rate at which a state agency employee's unused excess accrued vacation and sick leave is converted to a contribution to deferred compensation for the employee must be increased to 100% of the employee's daily pay per day of unused leave. The bill requires the State Personnel Department to establish a plan under which retiring state employees may convert certain accrued excess leave to a nontaxable monetary contribution to pay the retiring employees' group health insurance premiums.

**Effective Date:** July 1, 2003.

**Summary of Net State Impact:** The minimum estimated cost to the state is between \$0.5 M to \$2.3 M annually. The state may realize reduced expenditures related to overtime, reduced staff turnover, and training costs. These savings cannot be estimated at this time.

**Explanation of State Expenditures:** The total cost of this bill depends upon several factors. These factors include the number of leave hours converted, amount of reduced mandatory overtime costs, amount of reduced staff turnover costs, and associated lower staff training and hiring costs. This estimate assumes that the program is granted tax exempt status by the IRS. The State Personnel Department is required to adopt rules pursuant to this requirement. It is anticipated that the Department can do this with the current budget and staffing at no additional cost.

Current statute requires the State Department of Personnel to adopt rules to implement a leave conversion program which allows the conversion of excess unused leave at a rate of at least 60% of the employee's daily rate. This bill increases the reimbursement rate from at least 60% to 100% and includes two additional leave conversion options. (1) The first allows an individual in good standing who separates from state employment to have excess leave converted and contributed to a deferred compensation plan - contingent upon rules adopted by the State Personnel Department. (2) The second provision allows an employee that retires to have

all excess unused leave converted into a monetary contribution either to a deferred compensation plan - contingent upon rules adopted by the State Personnel Department; or a plan that pays, on a nontaxable basis, the group insurance premium for the retiree.

The costs presented below are contingent upon administrative action. The State Department of Personnel is required to adopt rules to: (1) allow conversion of excess unused leave for employees and employees that separate from service, and (2) establish a health insurance premium plan for employees that retire. The leave conversion programs established by both of these rules may not be implemented without IRS approval.

If the State Department of Personnel adopts rules for a yearly leave conversion program the costs for retiree leave conversion may be lower. If a yearly leave conversion program is implemented, the leave would be converted at the present daily reimbursement rate for the employee. If the Department does not adopt rules for a yearly leave conversion program then the leave would be converted when the employee retires from state employment. It is likely that the rate paid for leave converted upon separation is higher than the rate the employee was paid when the leave actually accrued. Thus, it is likely that a yearly leave conversion program would reduce the amount paid to employees for excess unused leave upon separation. Total cost of these provisions is dependent upon administrative action.

**Table 1: Unpaid Excess Leave for Employees Separating in 2002.**

<b>Leave Type</b>	<b>Separatees @ 60%</b>	<b>Separatees @ 100%</b>	<b>Difference Separatees</b>	<b>Retirees @ 60%</b>	<b>Retirees @ 100%</b>	<b>Difference Retirees</b>
<b>Vacation</b>	\$379,879	\$633,131	\$253,252	\$362,275	\$603,791	\$241,516
<b>Sick</b>	\$1,184,767	\$1,974,612	\$789,845	\$1,441,791	\$2,402,985	\$961,194
<b>Personal</b>	\$73,303	\$122,172	\$48,869	\$23,908	\$39,846	\$15,938
<b>Total</b>	\$1,637,949	\$2,729,915	\$1,091,966	\$1,827,973	\$3,046,622	\$1,218,649
<b>Number</b>	6,076			587		

*(1) State Employees Separating from Employment:* This provision is subject to State Department of Personnel administrative action. The bill states that an employee who at separation from service has accrued unused leave in excess of the amount the state compensates may elect to have the excess leave converted and contributed to their deferred compensation account.

The current statute states that the Department shall adopt rules necessary to implement the leave conversion program. Current statute requires that a day of leave converted must be at least 60% of the employee's daily rate. Based upon 2002 data and 100% conversion factor, the minimum cost could range from \$0.25 M to \$1.1 M. This cost is the difference between leave converted at 100% rate instead of 60%, and assumes that all vacation leave at a minimum and all leave (including vacation, sick, and personal) at the maximum is converted respectively (see Table 1 for more details). Total cost may be higher or lower than this amount and is contingent upon administrative action. The Department of Personnel is responsible for adopting rules that govern how much leave can be converted and when. In addition, this new provision may create an incentive for some state employees to separate from state employment. The extent of this is unknown.

*(2) State Retirees:* An individual that meets the stated retirement criteria may elect to convert unused leave at 100% of value as either one or both of the following (1) monetary contribution to a deferred compensation fund (the amount of unused excess leave converted is subject to Department of Personnel rules regarding conversion of leave to a monetary value contribution to a defined compensation account); or (2) monetary contribution to pay for health insurance benefits.

This provision does not specify what leave may be converted. Under current retiree flexible spending account provisions, all types of leave may be converted to a cash value to pay for medical expenses. Based upon 2002 data, the minimum cost could range from \$.24 M to \$1.2 M. This range assumes that all vacation leave at a minimum and all leave (including vacation, sick, and personal) at a maximum is converted at 100% rate instead of 60% respectively (see Table 1 for more details). Total cost is contingent upon administrative action and IRS approval of the conversion plan. In addition, this new provision may create an incentive for some state employees to retire from state employment. The extent of this is unknown.

*Potential Cost Savings:* The cost savings associated with this bill are difficult to quantify. These savings depend upon the amount of reduced mandatory overtime costs, amount of reduced staff turnover costs, and associated lower staff training and hiring costs realized as a result of this bill. For example the Department of Correction uses a mandatory overtime system to accommodate vacation requests and regular staff shortages. Mandatory overtime cost the Department \$30.6 M this past fiscal year (FY 2002 as of 4/24/02). The Department has an average turnover rate of 25.7% - adult custody staff 24.11% and juvenile custody staff 36.01% (FY 2001 data). The Department incurs a cost of \$4,500 to train each new employee. Given the number of employees that left during FY 2001, this represents a total training cost of \$5.7 M. The staff turnover rate for all state government averaged 18.7% from 1999-2001.

*Background:* During 2002 there were 6,663 employees that separated from state government. Of these 587 retired and 6,076 left for other reasons. The total value of unpaid leave for these employees was \$3.05 M for the retirees and \$2.73 M for the others (see Table 1 for more detail). The total current value of unused sick and vacation leave for active employees is approximately \$183 M.

On average, employees use approximately 70% of vacation leave accrued during a given year. Over time, employees may accrue very large leave balances. Current policy states that employees can be reimbursed for six weeks of unused vacation leave upon separation from state service. Employees are eligible for 67.5 hours of sick leave per year. On average, employees use approximately 67% of accrued sick leave over the course of a given year. Current policy states that employees cannot be reimbursed for unused sick leave upon separation from state service. This bill would allow employees to be reimbursed for all unused leave hours upon separation from state employment.

**Table 2: Annual Accumulation of Leave Based Upon Current Usage Patterns.**

<b>Years of Service</b>	<b>Vacation Earned</b>	<b>Vacation Used</b>	<b>Vacation Balance</b>	<b>Sick Earned</b>	<b>Sick Used</b>	<b>Sick Balance</b>	<b>Total Balance</b>
<b>0-4.99</b>	90	57.39	32.61	67.5	38.79	28.71	<b>61.32</b>
<b>5-9.99</b>	112.5	78.91	33.59	67.5	44.28	23.22	<b>56.81</b>
<b>10-19.99</b>	150	106.17	43.83	67.5	47.55	19.95	<b>63.78</b>
<b>20 and over</b>	187.5	134.98	52.52	67.5	50.42	17.08	<b>69.6</b>

Table 2 presents the amount of vacation and sick leave earned, average leave used, and the associated remaining leave balances from one year. However, the impact that this program will have on leave usage patterns is unclear at this time given the new financial incentive for employees to accrue leave time. Active employees have a total leave balance worth approximately \$182.8 M (see Table 3 for more detail).

**Table 3: Current Unused Leave Totals.**

	<b>Total Hours</b>	<b>Total Value</b>
<b>Vacation Leave</b>	5,403,514	\$99,156,818
<b>Sick Leave</b>	4,282,234	\$83,624,672
<b>Total</b>	9,685,748	\$182,781,490

Current as of 1/9/03

Under current retiree flexible spending account provisions all types of leave may be converted to a cash value to pay for medical expenses. However, the amount converted is capped at \$5,000, and leave is converted at varying conversion factors dependent upon length of employment.

**Explanation of State Revenues:**

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:**

**State Agencies Affected:** All.

**Local Agencies Affected:**

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