Metropolitan Domestic Water Improvement District
Board of Directors Meeting

May 14, 2012

Sick Leave Pay-Out Policy

Synopsis

The Board of Directors is requested to review and provide direction regarding the sick leave pay-out policy.

Background

As discussed at the April 30, 2012 study session, it was determined that an analysis of the current sick leave pay-out policy be undertaken to determine the short and long-term financial liability exposure to the District. Established in 2003, the initial concept of the policy was to reward those District employees who have benefitted the District by not calling in sick on a frequent basis. However, the liberal nature of the policy has potentially created a financial burden for the District as a number of staff are preparing for their retirements. The current policy as included in the District's Personnel Manual reads:

> "A portion of, or all of, accrued sick leave will be paid to an employee upon voluntary or "no-cause" separation from employment only under the following scenarios: 1) An employee who was with the District for ten (10) years shall receive fifty-percent (50%) of unused sick accrued leave. 2) An employee who was with the District for fifteen (15) years shall receive seventy-five percent (75%) of unused accrued sick leave. 3) An employee who was with the District for twenty (20) years shall receive one hundred (100%) of unused accrued sick leave."

Report

Staff has researched what the other local jurisdictions have in regards to sick leave pay-out at retirement. Attached is a description of those policies. None of the other jurisdictions pay-out at 100% of total sick leave at any of their levels or years of service. Also, only the City of Tucson and the Town of Oro Valley do not have a cap on the amount of time that is paid out at retirement but they are paid at 50% of the total amount.

When reviewing the financial liability to the District based upon what currently is on the books for sick leave, the current exposure for all employees is $502,950.00 based on current years of service. That cost will be significantly higher at the end of next fiscal year. While not everyone in the District is eligible to retire, this is the number that our auditors have identified as our potential liability. Attached is a more detailed breakdown of how this number was derived and also an indication of those with years of service approaching 20 years.

Based on Board member comments, it appears that a change to the sick leave policy is prudent to avoid having a significant financial burden in the coming years as our workforce begins to look at retirement. Two common elements have developed out of those discussions and they include a cap on the total amount to be paid out and a reduction in the percentage amount to be paid. Having a cap will lessen the volatility of large yearly fluctuations when a long term employee with significant accumulated hours retires. The reduction in percentage would also bring us more in line with an industry standard for this area.

Normally when a policy of this magnitude is changed, it is grandfathered for current employees as compared to a change that affects all participants equally. Example would be ASRS where the 47%-53% retirement contribution rate was changed but it affected all employees the same whereas a significant policy such as the point system changed on July 1, 2011 with all employees hired before that date being under the 80 point rule and those hired after being under a 85 point rule.

One thing that should be considered by the Board is that for the long-term employees that will leave under the sick pay-out policy, the District could recoup the dollars paid out within a couple of years for the possible difference in the starting salary for the new hire as compared to the long- term employee that is probably near the top of the pay range.

Another issue that needs to be considered is that if we modify the policy to a maximum number of hours, it somewhat deters from the original intent of the policy to reward employees for not being sick. It also gives the current employees under the maximum cap an unfair advantage as compared to the employees exceeding those numbers of hours. For example, an employee may have forgone transferring available sick hours each year to vacation time because the employee assumed he or she would get paid for the sick time when they retired. If the maximum pay-out was reduced to 750 hours, they would not be able to recoup those hours lost that could have been taken as vacation, whereas, someone approaching the 750 hours would know upfront that they might as well transfer the sick hours to vacation; otherwise, they will be lost upon leaving the District. Plus, there may be employees above 750 hours that would start being sick much more often that could affect work productivity.

That being said, the overall financial stability of the District is paramount and with that in mind, a reasonable cap on the total amount of hours to be paid out at retirement should be 750 hours. Alternatively, we could also look at lowering the percentages of what is being used for the pay-out. Attached is a table showing the liability exposure for a 750 hour cap pay-out, which would total $395,364.00 as it is currently calculated. When looking at a reduction on the percentage basis the numbers were generally lower; however, as hours continue to accumulate over time, there is the same issue that we currently face in that the amount continues to grow and it was felt that having a cap on the total amount to be paid out still provides the benefit to the employee as originally envisioned.

To put things in better perspective, a final table was prepared to compare potential liabilities at the end of next fiscal year (our forthcoming budget year). A liability of $658,269.00 would exist based on a number of employees that would have 20 years of service with the District if no changes were made to the policy. That amount would grow substantially over the years as we have a high number of long-term employees. In comparison, when you look at the 750 cap on total hours, the increase is relatively minimal and as the years progress and retirements take place, the increases stay fairly even and manageable.

One other point that should be discussed is that both the City and the County tie their sick leave pay-out to their respective retirement systems. Specifically, they limit the eligibility to those employees who retire from service with the City or County into the retirement system (Arizona State Retirement System). This requirement protects them from long-term employees leaving to go to another job instead of actually retiring. While the overall attempt with the District's policy is to reward employees who have not abused their sick leave, it does seem prudent to tie the benefit with that of actually retiring. With having it tied to the employee entering the ASRS, it would provide the incentive of keeping the employee longer at the District in lieu of seeking other employment based on his/her experienced gained from their years of service at the District.

Recommendation

It is recommended that the Board of Directors discuss the long-term financial implications of continuing the current policy of sick leave pay-out upon employees leaving the District. Additionally, the Board should consider the merits of capping the total hours of the policy to a maximum of 750 hours, leaving the time frames and percentages the same, and to consider requiring the pay-out only be for employees who enter the Arizona State Retirement System.

Suggested Motion

I move to reduce the total hours of the sick leave pay-out policy to a maximum of 750 hours, leave the time frame and percentages the same, and to require that employees are eligible for the pay-out only is they enter the Arizona State Retirement System.

Respectfully submitted;

Mark R. Stratton
General Manager