MINUTES

JOINT COMMITTEE ON PENSIONS, INVESTMENTS AND BENEFITS

November 4, 2015
Room 548-S—Statehouse

Members Present

Representative Steven Johnson, Chairperson
Senator Jeff King, Vice-chairperson
Senator Anthony Hensley
Senator Mitch Holmes
Representative John Edmonds
Representative Daniel Hawkins
Representative Charles Macheers
Representative Gene Suellentrop
Representative Ed Trimmer

Members Absent

Senator Laura Kelly
Senator Ty Masterson
Representative John Alcala
Representative Jerry Henry

Staff Present

Reed Holwegner, Kansas Legislative Research Department
J.G. Scott, Kansas Legislative Research Department
Mark Dapp, Kansas Legislative Research Department
Gordon Self, Office of Revisor of Statutes
Daniel Yoza, Office of Revisor of Statutes
David Weise, Office of Revisor of Statutes

Conferees

Alan Conroy, Executive Director, Kansas Public Employees Retirement System
Jim MacMurray, Senior Vice President – Finance, Kansas Development Finance Authority
Laurel Murdie, Legislative Post Audit
G.A. Buie, Executive Director, United School Administrators of Kansas
Sue Givens, Superintendent, El Dorado School District
Glen Suppes, Superintendent, Smokey Valley School District

Others Attending

Dodie Wellshear, United School Administrators of Kansas

Chairperson Steven Johnson called the meeting of the Joint Committee on Pensions, Investments and Benefits to order at 10:06 a.m. on Wednesday, November 4, 2015, in Room 548-S of the Statehouse. The Chairperson welcomed Committee members, conferees, and members of the audience.

2014 Valuation of Kansas Public Employees Retirement System

Alan Conroy, Executive Director, Kansas Public Employees Retirement System (KPERS), provided a review of the 2014 actuarial valuation, which is a snapshot of the financial condition of the Retirement System as of December 31, 2014. The actuarial valuation, which is different from the market valuation, was estimated to be $15.662 billion. Actuarial assets are calculated by "smoothing" investment gains and losses over a five-year period. A market value higher than the actuarial value means that deferred investment gains will flow through valuations over the subsequent four years. There is an estimated $660 million in deferred gains that could be realized in the outlying years. Due in large part to investment gains over the past three years, the funding status has improved for all membership groups (KPERS state, school, and local groups; Kansas Police and Firemen's Retirement System; and Judges' Retirement System). The Unfunded Actuarial Liability (UAL) decreased in 2014 by $298 million, leaving $9.468 billion remaining to be funded. The funded ratio increased from 59.5 percent in 2013 to 62.3 percent in 2014. Legislative reforms enacted in 2012, including increased employer and employee contributions, will continue to improve funding. Assuming all actuarial assumptions are met in the future, KPERS will be fully funded at the end of the amortization period in calendar year 2031. The valuation does not include the proceeds of the recently issued pension obligation bonds, which will be included in the 2015 actuarial valuation report (Attachment 1).

Senator Holmes requested Mr. Conroy provide a detailed explanation of the changes made to the actuarial method used that resulted in a lesser UAL amount.

Responding to a question from Representative Trimmer, Mr. Conroy stated future bond payments are not reflected in the report because debt payments are the State's responsibility through the Department of Administration and not through KPERS.

Chairperson Johnson, noting the actuarial assumption of 4.0 percent growth in payroll, asked if the State would be required to increase its contributions in the future. Mr. Conroy said the actuary examines salary history, which includes promotions and cost-of-living adjustments in addition to growth in the number of employees.

Chairperson Johnson requested Mr. Conroy provide a detailed explanation on the smoothing calculations.

Pension Obligation Bonds

Jim MacMurray, Senior Vice President – Finance, Kansas Development Finance Authority (KDFA), presented information to the Committee regarding the issuance of the Series 2015H pension obligation bonds (Attachment 2).

Responding to a question from Senator King, Mr. MacMurray said KPERS received the proceeds of the bonds on August 20.

Responding to a question from Senator King, Mr. Conroy said the bond proceeds were spread across KPERS' current asset allocation arrangement; funds were distributed to asset managers within 24 hours of receipt.

Senator King expressed appreciation to KDFA and KPERS for their professional administration in the issuance of the bonds and the investment of the proceeds.

KPERS Performance Audit Report: Evaluating Controls to Detect and Prevent Fraud and Abuse

Laurel Murdie, Legislative Post Audit (LPA), briefed the Committee on the findings of the Performance Audit Report: Evaluating Controls to Detect Fraud and Abuse (Attachment 3). The audit report found KPERS had most of the controls needed to help ensure it collects accurate retirement contributions and distributes its controls to detect and prevent fraud and abuse. LPA identified one significant control weakness, the suspension of field audits for almost two years. KPERS reports it has since resumed that function, which helps ensure KPERS receives accurate employer contributions. LPA identified options that would help KPERS verify the ongoing eligibility of disability recipients. Other identified issues were isolated in nature and have been since corrected.

Mr. Conroy thanked LPA for its work and presented the Committee with an overview of KPERS' actions to address shortcomings identified in the audit (Attachment 4). KPERS has entered into discussions with the Kansas Departments of Revenue and Labor to provide employee-related data that can be used to discern if an employee is a member of the Retirement System or not.

Responding to questions from Chairperson Johnson, Mr. Conroy explained that once a retiree dies, KPERS is often times contacted by funeral home directors to begin the process of claiming a death benefit. If a deceased retiree has received KPERS benefits, which are usually deposited electronically, the death benefit is reduced accordingly. If necessary, KPERS will ask the estate of the deceased for any overpayments made. KPERS has access to death certificates from the Kansas Department of Health and Environment and information from the U.S. Social Security Administration.

Chairperson Johnson recognized the attendance of Ernie Claudel, member of the KPERS Board of Trustees.

The Committee recessed for lunch at 11:48 a.m., and reconvened at 1:40 p.m.

Afternoon Session

2015 Senate Sub. for HB 2095; Working After Retirement

David Weiss, Office of Revisor of Statutes, provided an overview of the provisions of 2015 Senate Sub. for HB 2095, regarding working after retirement (Attachment 5).

Mr. Conroy explained the impact of Senate Sub. for HB 2095 on current KPERS members who are working after retirement. Under the current provisions there are no employer contributions paid on the first $20,000 earned; under the new provisions employer contributions will be paid on the first dollar paid to employed retirees (Attachment 6).

Chairperson Johnson requested Mr. Conroy provide copies of a grid-analysis of the new working-after-retirement provisions the Executive Director had used in his briefing.

Chairperson Johnson informed the Committee members there was a memorandum in their meeting packets from the Department of Education that listed the hard-to-fill teacher positions as certified by the State Board of Education (Attachment 7).

Chairperson Johnson recognized G.A. Buie, Executive Director, United School Administrators of Kansas; Sue Givens, Superintendent, El Dorado School District; and Glen Suppes, Superintendent, Smokey Valley School District. The conferees explained that a task force of 15 school superintendents from across the state was formed to evaluate the recently passed working-after-retirement legislation. The task force members initially were skeptical of the applicability, but as they applied the new provisions to various scenarios, they saw the effort taken to address many of the circumstances that can arise when hiring a retired teacher. In employment situations involving emergency or hardship circumstances, the conferees expressed concern that using a legislative hearing process may not be practical. The conferees recommended an assurance protocol be utilized by a school district that would communicate the steps taken to fill a position, would be signed by the school's superintendent and board president, and filed with KPERS (Attachment 8).

The conferees requested the Committee members consider having participating employers pay any additional actuarial cost as established by KPERS.

Representative Hawkins stated a 30 percent surcharge had been discussed previously.

Responding to a question from Representative Macheers, Mr. Suppes and Ms. Givens said the amount of time that teachers give notice to school districts about their retirement varies across the state.

Chairperson Johnson suggested the Committee should focus upon hardship procedures and the income cap.

Answering a question from Representative Hawkins, the conferees replied they use all means to fill positions, including active recruiting.

Senator King suggested that guidelines for determining hardship could be adopted by the Committee and incorporated in its Committee report to the Legislature. The Report would be a means to inform school districts how to prepare for an extension request. The earliest a request could be heard by the Committee would be in 2018, after a year-long hardship position had been filled.

Representative Suellentrop concurred with Senator King's suggestion.

Chairperson Johnson concluded that the question that will have to be decided in the future is the extent to which the Joint Committee wishes to administer the working-after-retirement policy versus provide oversight.

Deferred Compensation and Final Average Salary

Mr. Conroy provided information on current deferred compensation and final average salary calculations (Attachment 9). Annual pension benefits for most retirees are based on the formula: final average salary multiplied by years of service, multiplied by a percentage multiplier. The final average salary variable—depending upon the member's plan, tier, and membership date—is based on an average of three to five years of "compensation" or "salary," as those terms are defined in statute, which include definitions for all salary and wages payable to a member for personal services performed for a participating employer. Both definitions specifically include deferred compensation derived from savings plans authorized by sections 403(b) and 457 of the Internal Revenue Code (IRS). There are two types of 457 plans, a 457(b) plan, which is offered by governmental employers to most, if not all, state and local government employees, and a 457(f) plan, which is used by employers to retain certain employees. A 457(f) plan is usually limited to particular employees; the employer establishes and funds the plan in a contract with the employee. The employee does not receive any income until the end of the contract period.

KPERS has found the use of 457(f) plans to be extremely rare; out of approximately 90,000 retirements in the past 20 years, there has been 3 instances where 457(f) benefits were included in the final average salary. Current retirement law caps the effect of 457(f) benefits on final average salary by excluding the salary amount which is greater than 15 percent or 7.5 percent for Tier 1 or Tier 2 members, respectively. A 457(f) plan would have a smaller impact on the KPERS 3 Cash Balance Plan because those benefits are calculated on an account basis rather than on final average salary. KPERS 3 accounts reflect compensation earned throughout a member's career, not the highest three or five years. Contributions to a 457(f) plan which is paid at or near retirement would earn interest for a limited period of time. The Internal Revenue Service (IRS) annually sets a contribution limit based on annual earnings and membership date. Kansas has adopted the IRS limitation levels by statute.

Answering a question from Chairperson Johnson, Mr. Conroy said moneys in 457(f) savings plans could be limited when calculating final average salaries—so long as the provision applied prospectively.

Submission of KPERS Reports and Other Requested Information

Mr. Conroy provided an overview of the KPERS Alternative Investment Policy and the implications of the legislative changes made to the KPERS systems in 2012 (Attachment 10), and the Sudan Divestment Report (Attachment 11).

Chairperson Johnson informed the members there was a memorandum in their meeting packets from the Office of Revisor of Statutes regarding information previously requested (Attachment 12).

Committee Discussion and Recommendations to the 2016 Legislature

Vice-chairperson King requested the report should thank the superintendents for their effort in evaluating the new working-after-retirement provisions and for making suggestions to improve the State's retirement laws. The Joint Committee should finalize guidelines during the 2016 Legislative Interim.

Representative Hawkins requested the report include consideration by the Legislature of a 30 percent surcharge. Vice-chairperson King concurred, adding that the Legislature and KPERS should examine requirements of the IRS when discussing a surcharge.

Senator Anthony Hensley requested the report note that the Joint Committee is required by 2015 Senate Sub. for HB 2095 to study the issue of whether the compensation limit should be adjusted.

With no objection, the Committee agreed for the above items to be made part of its report to the 2016 Legislature.

The Committee adjourned at 3:23 p.m.

Prepared by Mark Dapp
Edited by Reed Holwegner

Approved by the Committee on:

December 31, 2015
(Date)