Approved February 19, 1990
Date

MINUTES OF THE SENATE COMMITTEE ON WAYS AND MEANS.

The meeting was called to order by SENATOR AUGUST "GUS" BOGINA at
Chairperson

11:10 a.m./XX. on JANUARY 30, 1990 in room 123-S of the Capitol.

All members were present except:

Committee staff present:

Research Department: Diane Duffy, Leah Robinson
Revisor: Norm Furse, Gordon Self
Committee Staff: Judy Bromich, Administrative Assistant
Ronda Miller, Committee Secretary

Conferees appearing before the committee:

Ben Barrett, Associate Director, Legislative Research Department
Senator Ed Reilly
Charles Dodson,Director, Kansas Association of Public Employees
Representative Kathleen Sebelius
Shelby Smith, Secretary, Department of Administration

Senator Harder called the meeting to order for the Chairman who was temporarily detained in another committee meeting.

SB 426 - AN ACT relating to the legislature; requiring certain actions on prefiled bills and resolutions introduced by committees as a result of studies conducted in the interim between regular sessions; amending K.S.A. 1989 Supp. 46-804 and repealing the existing section.

Ben Barrett told the Committee that SB 426 was recommended by the Special Committee on Federal and State affairs in order to (1) make the legislative process work more effectively, (2) cut out one stage of committee deliberations, (3) motivate interim committees to recommend bills in their final form, and (4) encourage the Legislative Coordinating Council to be more selective in topics for interim studies and in appointments to interim committees. Mr. Barrett noted that SB 426 does not cause anything to happen that cannot already happen under current rules of the legislative body. In answer to a question, it was stated that after an interim bill or resolution passed the first House, it would be referred to a standing committee in the second House.

Senator Ed Reilly appeared before the Committee in support of SB 426 and noted that in addition to expediting the legislative process, SB 426 would give creditability to interim studies. He called attention to concerns within the Minority Report and noted that Senator Fred Kerr signed it. Senator Reilly indicated that approximately 40% of the bills and resolutions resulting from interim studies ultimately become legislation.

SB 435 - AN ACT concerning state officers and employees; prescribing the implementation of certain programs of the department of administration therefor; amending K.S.A. 75-5540, 75-6512 and 75-6520 and repealing the existing section.

Norm Furse gave a brief explanation of SB 435.

Charles Dodson reviewed Attachment 1. In answer to a question, he said that numbers provided by the Division of Personnel Services (DPS) or approximately 4% of employees earning less than $24,000 were used to calculate the costs of delaying implementation of the programs.

Representative Sebelius reviewed Attachment 2. In answer to a question, Rep. Sebelius said that the Federal deductible is a maximum of $2400, regardless of the number of children. Anyone whose child care expenses are above the

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

$2400 per year range could use both tax advantages. For those at the lower salary bracket, it is more advantageous to use the Federal deductible first and then piggyback the dependent care assistance. Those in the higher bracket would probably reverse the order because the tax free income is a better deal than the Federal tax deduction.

Secretary Shelby Smith reviewed Attachment 3. The Committee noted that SB 435 is a result of frustrations of the Legislature; 1) the costs of delaying these programs to employees and the state, and 2) the Department of Administration's use of money (appropriated during the 1989 Legislature) for software instead of implementation. It was called to the Committee's attention that the original contract with Peat/Marwick was for $3,688,500. It was amended by adding $355,000 for a total of $4,043,500. In October a contract was signed when no competition existed for $1,035,090 to provide programming support necessary for the implementation of an integral payroll/personnel software package with Business Information Technology. The fact that the additional million dollar contract was signed without legislative authorization was cited as another source of frustration.

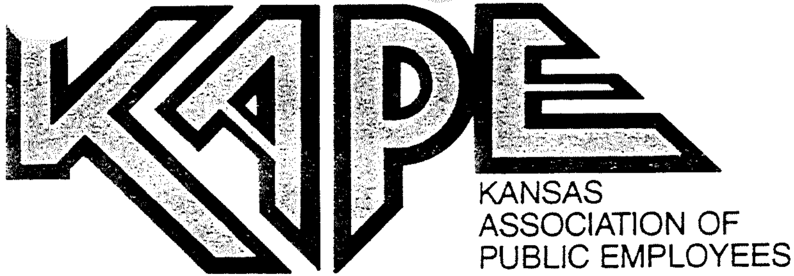
Secretary Smith noted implementing the plan within 180 days would require programming of the KIPPS system. He felt this would be unwise because the KIPPS program would be discarded with the implementation of the KFIS system. He stated that estimates of the costs involved in delaying implementation of the payroll plan would be guesswork on the part of the Department. In answer to a question, Secretary Smith said that if SB 435 is not passed, pilot testing of an agency will start in June, 1990 and the Department will begin phasing new agencies into the system in December, 1990. He stated that because programming personnel are unfamiliar with the KIPPS system, it would be unrealistic to plan on implementing the programs in 6 months. However, the implementation of the programs on the KFIS system within 6 months should be realistic. Sherry Brown, Department of Administration, stated that implementation of the two programs should result in savings for the state, although part of the savings would be used for administering the programs.

The meeting was adjourned at 12:15 P.M.

GUEST LIST

COMMITTEE: SENATE WAYS AND MEANS DATE: 1-30-90

NAME (PLEASE PRINT)	ADDRESS	COMPANY/ORGANIZATION
Charles Dodson	Topeka	KAPE
Wayne K Wianecki	Topeka	AFSCME
Lesa Zagar	Topeka	[illegible]
Ray Hauke	Topeka	Bd of Regents
Ted D. Ayres	Topeka	Bd of Regents
Susan Irza	Topeka	Dept of Admin
Julie Hein	Topeka	Unisys
Jim M. Diedrich	Atchison	Rep. Sebelius
Nancy Echols	Topeka	SRS
Jerry Sloan	"	OJA
Louis Chabira	Topeka	Div. of Budget
Walt Darling	Topeka	Div. of Budget
Mike Woolcock	Topeka	DOB



Presentation to

SPECIAL COMMITTEE ON WAYS AND MEANS

by

Charles Dodson, Director
Kansas Association of Public Employees

January 30, 1990

Mr. Chairman, members of the committee, thank you for this opportunity to appear in support of Senate Bill 435.

I believe this is the seventh time I have made a presentation in support of the dependent care cafeteria program and direct deposit of pay checks for state employees.

Besides the inconvenience, the delay in implementing these programs costs state workers $35,000 to $75,000 each month. A break down of even the most conservative estimate is explained in the copy of our presentation to the interim committee as attached.

Since that interim committee study, two significant events have occurred that need to be mentioned. First the Supreme Court has refused to issue a writ of mandamus to force implementation of these programs. Their opinion held that indeed the Secretary of Administration does have the latitude to implement these programs based on the availability of computer capacity or

400 West 8th Ave. Suite #103 Topeka, Kansas 66603 913-235-0262

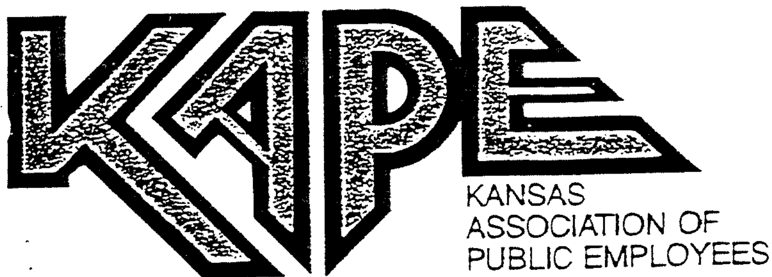
SWAM
Jan. 30, 1990
Attachment 1

facilities. According to the Court, the Secretary acted within the guidelines of the law.

Second, a fourth processor has been added to the present computer system which adds 25 to 30 percent more capacity and faster response times. It is unfortunate this was not done in 1988. Possibly we could have had these programs implemented long ago if it had been.

We do not know the magic date for implementation. We know the Department hopes to have the new system fully operational by January 1, 1991. But, I think even they will agree that the date is optimistic and uncertain. We are concerned that failure to set a date certain in the statutes could mean more and more delays.

Thank you for allowing me this time. I will be happy to answer any questions you may wish to ask.



PRESENTATION OF
CHARLES DODSON
TO SPECIAL COMMITTEE ON WAYS AND MEANS/APPROPRIATIONS
September 18, 1989

Of the three items on the agenda for this section of your agenda, the implementation of the employee dependent care assistant program is the most important. It has a direct impact on the pay checks of state employees. That impact is significant.

Using the DPS conservative estimate that as few as 4% of employees will participate in the program, each month implementation is delayed costs state employees about $35,000.

A one year delay costs $420,000, and the delay to January 1, 1991, will mean state employees will have needlessly lost $630,000 of disposable income.

(4% x 37,000 employees x $35/week DC costs
x 15% tax bracket)

This is an extremely conservative estimate based on only one child needing child care with the employees top income tax bracket at 15%.

We understand that $630,000 is not a huge sum when considering the entire payroll costs for state employees.

However, since the average salaries of state workers when compared to all other states has seen a fall from a ranking of 32nd in the nation to 41st in the nation, we need to do everything to insure they have every disposable dollar possible.

For an employee who takes home $870 per month, and there are thousands of them, a $22.50 tax savings is the equivalent of a two and one-half percent increase in take-home pay.

This, however, ignores the primary concern. That is, what has happened to the notion that state government should be the leader in employee relations. We're looking at a cost of $65,600 for 1600 hours of programming, or $41 per hour to provide a real and meaningful benefit to hundreds, if not thousands, of state

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employees. The Department of Administration has refused to implement or schedule this benefit even though sufficient funds were appropriated by the 1988 legislature.

This same department, however, has no reservations about hiring a [1] high-priced law firm at two or maybe even three times that rate to appeal a case one single employee won in district court which would have given him a small increase in gross pay.

How did we manage to get our priorities so screwed up that this is the message we send very clearly to our employees?

This attitude is further evidenced by failure to implement the direct deposit program. This program is needed for one single reason. Some employees in outlying areas do not receive their paychecks on payday.

Payday should be payday, but some employees cannot count on their check arriving on time. These people do not have large reserves. That money is needed. The landlord wants the rent, the cupboard is bare and the day care center wants their money.

The last issue has to do with KAPE dues deduction. This is, of course, not an issue with which you are concerned, and that's as it should be. I will mention it only to clarify some points.

We were informed that it would take some 1800 hours to reprogram the existing system at a cost of $75,000 to change our dues structure from a fixed dollar amount per member to a percentage of gross pay. We decided to wait for the new system when we were informed it would only take 200 hours of programming time on the new system. Our organization just couldn't afford $75,000.

We assumed that if anything the hourly costs on the new system would be cheaper since they would have trained programmers and a much better documented set of programs. Even if the $41 per hour costs were constant, $8,000 is much easier to raise than $75,000.

We have now been informed that programming costs on KFIS is going to be $125 per hour.

Thank you for allowing me to speak. I will be happy to try to answer some of your questions.

[1] Law firm of Sloan, Listrom, Eisenbarth, Sloan and Glassman on appeal of Mulford vs. Ks. DHR and DOA.

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HOUSE OF
REPRESENTATIVES

CHAIR: SHAWNEE COUNTY DELEGATION
COMMITTEE ASSIGNMENTS
RANKING MINORITY MEMBER: FEDERAL AND STATE AFFAIRS
MEMBER: JUDICIARY
ELECTIONS
SENTENCING COMMISSION

Testimony on SB 435
Senate Ways & Means Committee
January 30, 1990

Chairman Bogina, Members of the Committee:

This is an attempt to briefly review the long path which brought us to this hearing today. Unfortunately, this saga has become all too familiar to the 1990 Legislature because it involves the overwhelming legislative approval of a specific issue which the Administration chose not to implement.

In 1988, Representative Robert Miller and I co-sponsored HB 2850 on Dependent Care Assistance Accounts. This measure allows a state employee to take advantage of tax breaks for child care as outlined by the IRS. Each employee can designate up to $5,000 of his or her salary to be put into a special account and paid tax-free to the employee as reimbursement for child care expenses. As the attached article explains it has become one of the most popular child care benefits, and can be used in conjunction with the federal tax credit, as long as child care expenses exceed the tax credit allowable limit.

Although there are some start-up costs for the state - establishing the seperate account, programming the computer for an additional deduction and most importantly, educating the state employees about the possible advantages of this measure - there is good news for the state. Estimates from other states indicate that if 1% to 5% of our eligible employees take advantage of this plan, there will be a <u>cost savings</u> to the state because FICA and unemployment taxes no longer have to be paid on the portion of the state employee's salary isolated in the Dependent Care Assistance Account.

In the House Committee in 1988 the Secretary of Administration, Ed Flentje, originally opposed this measure. He told the Committee that the Department of Administration "was planning" to implement this program, but would prefer not to have a mandate. When Representative Miller and I pointed out to the Committee that permissive language had been in statute for 5 years and no action had been taken, the

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Committee overwhelmingly agreed that the mandate was needed. We then agreed to a delay of the starting date of the bill until July 1, 1989, to give the Department ample time for program development. The bill overwhelmingly passed the House.

In the Senate Committee, the Secretary had a change of heart and appeared in favor of HB 2850. He did ask that the phrase "approval of the Secretary of Administration to assure adequate data processing resources" which was in the statute from the early 80's, be applicable to this new section, but assured the Committee that it was not intended as a delay tactic. The Senate unanimously approved the bill and the Legislature appropriated adequate funds to implement the program.

The Governor signed both the implementation legislation and the funding authorization and used the passage of HB 2850 as a highlight of benefits for state employees in the 1988 Session.

It came to my attention prior to July 1, 1989 that no action had been taken by the Department to implement this program. When I made inquiries of the Secretary and asked for an update on the materials which were being developed, I was told that I would receive a written response as to the progress of this implementation. Almost six weeks later, I received a written report from the Secretary, which was delivered and explained to the Summer Interim Committee.

Secretary Smith indicated that the Dependent Care Assistance Program had not been implemented by the Department, and that the Legislature had not been informed of the decision which was made in March, 1989. The Department based their refusal to implement the plan on three reasons; they did not have access to a trained computer programmer, there were unanswered questions about the effect of implementation dates, and there weren't available funds. Under questioning by the summer Committee, it became clear that none of these reasons was valid. In spite of the fact that there were people in the room this summer who testified that they could provide the state with a program under contract, the Department admitted that there had been no attempt to contract out for the required program. In addition, the Department explained to the Committee that resources allocated by the 1988 Legislature had been spent for computer software, not to implement the Dependent Care Assistance Account. Finally, although the Department continued to state that they had unanswered questions, the

Secretary admitted that he had never asked the questions to either the IRS, to other states who have similar programs, to the City of Topeka who has a dependent care assistance account, or to any of the many school districts across Kansas who have DCAA's in place.

It has come to my attention that while there were some question of computer capacity in the past, this issue has also been clearly resolved because the Department of Administration has added computer capacity which has increased its output by over 20%. In spite of that, this benefit program for state employees has still not been implemented.

I applaud the Interim Committee's decision to put a timetable on implementation. We thought that the original legislation had such a timetable, but clearly the application of pre-existing language gave the Department an "out" which they chose to use. As a policy maker, I am very frustated about the time and energy we spend passing legislation, only to find our efforts thwarted by the Executive Branch. It is unfortunate if it takes the effort of three legislative sessions to get a program implemented, in spite of the overwhelming approval from the Legislature. I can only hope that if this measure is approved by the 1990 Legislature, state employees will finally receive the beneift which we intended.

Thank you for this opportunity to appear in favor of SB 435

Employers can't run from child care issues

Jane Bryant Quinn
Staying ahead

NEW YORK — If your company hasn't yet wrestled with the child-care issue, you have an experience in store.

No employer can run away from this problem — at least not for long.

Female middle managers who are thirty-something hear the loud ticking of their biological clocks. Companies need good child-care policies to lure these valuable employees back to work.

Lending urgency to this issue is the onrushing worker shortage. The new generation of young adults is a small one. To keep the wheels turning, corporations will have to recruit people not now in the work force. Mothers at home are just such a resource. But they won't budge unless good care is found for their kids.

When a company starts discussing a child-care benefit, one issue that comes to the fore is fairness. If a special benefit is added for parents of young children, how will the other employees feel? Will they push for a matching benefit for themselves?

Dana Friedman, of the Families and Work Institute, says that — in real life — that's a non-issue. Employers worry about it in advance, she says. But once the benefit is installed, it's not controversial.

One reason is that the companies broaden the benefit's scope. It's set up for "dependent care" — so it covers elderly parents as well as young children. "With this broad definition, there's virtually no employee who might not use the benefit some day," Friedman says.

Furthermore, a number of benefits favor one group over another, says Susan Velleman, an employee-benefits adviser at the Boston office of the consulting firm Mercer-Meidinger-Hansen. A worker with a family gets more of a subsidy for his or her medical benefits than a worker without. The funding formulas for pension plans pay more to workers who are close to retirement than to younger workers. "People accept that," Velleman says.

A more serious fairness issue, Friedman says, involves how the company chooses to make day care available. To subsidize a day-care center is to favor that kind of child care over the alternatives. Some parents might prefer to have their children tended in the home of a neighbor. Others might want a center closer to their homes.

Doubts about fairness as well as cost are what keep many companies from supporting day-care centers directly, Friedman says. Their preference is to make it easier for parents to finance their own day care, by providing them with special tax-favored day-care accounts.

Under these plans, an employee contributes part of his or her salary up to $5,000 a year. Child-care bills are then sent to the company, which pays them out of that account. No income or Social Security tax is owed on the money you set aside, so you're funding your child-care bills with pre-tax dollars. That saves you 15 to 28 percent, or more.

Only 11 percent of the companies that offer child-care spending accounts make a corporate contribution to the fund, Susan Koralik of the consulting firm, Hewitt Associates, told my associate Virginia Wilson. Some of those that do may limit the benefit to lower-income employees who otherwise might not be able to afford child care at all.

Child care may also be offered as part of a comprehensive flexible-benefits program — something else that employers perceive as fair. Under flexible benefits, each employee gets a certain number of credits. They use them to "buy" the particular benefits they want. The list may include child and elder care, extra dental services, legal assistance, more disability benefits, and so on.

"But benefits aren't the universal answer," Velleman says.

They work well for married people. One person can cut back on medical benefits, because he or she is covered by the spouse's plan. Those extra credits can be used to fund child care. But a single parent doesn't have that luxury.

He or she may need every bit of life and medical insurance offered. So the child-care benefit may be unaffordable. Any flexible-benefit plan should be constructed with this obstacle in mind.

It seems clear that the child-care problem won't be solved by relying on corporate subsidies for parents with young children. Most companies believe that the cost is too great. Says Friedman, "The corporations see that they've got to get the government involved."

Washington Post Writers Group

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DEPARTMENT OF ADMINISTRATION 1/30/90
TESTIMONY ON SENATE BILL 435

Thank you, Mr. Chairman.

At the outset let's clarify what appear to be some misunderstandings regarding the delay in implementing dependent care assistance and electronic fund transfer. Conferees before the interim Committee on Ways and Means/Appropriations and a newspaper article referred to a lack of computer capacity as the cause. Implementation of the dependent care assistance program has nothing to do with computer capacity. As previously communicated to the Legislature, the problem is programming. We recently negotiated an upgrade of the Unisys center that provides some needed capacity relief until the machine is shut down. This mainframe computer center will be phased out and removed sometime between January to June of 1991. The seven-year gridlock on computer decisions is behind us.

I believe a brief review of the Department's history with respect to the dependent care assistance program and direct deposit of employee paychecks may be helpful. The Department of Administration supported and testified in favor of both the dependent care assistance and electronic fund transfer programs. Our support continues to be unwavering.

In February 1989, I determined, in accordance with Kansas statutes, that the Department did not have adequate data processing resources to implement the dependent care assistance

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Attachment 3

program by July 1, 1989. The reasons were twofold. First, KIPPS is a poorly designed and poorly documented system. It is an extremely fragile payroll system. The design and lack of documentation mean that modifications to the system present real risks of inadvertent disruptions to the entire payroll process of Kansas. As proposed in this bill, the dependent care assistance program would require numerous modifications to the Unisys/KIPPS system.

At the time of my decision, the last programmer who had experience in the original development of KIPPS had just resigned, leaving no programmers with even a year of experience working with KIPPS. KIPPS poses problems and risks for even the most experienced staff. To take on a complex programming project at that point posed, in our judgment, an unacceptable and unnecessary risk to producing paychecks for state employees.

Second, the Department had just embarked on a major project to replace our old personnel/payroll system (KIPPS) and our old accounting system (CASK), and to install for the first time a computer system for the State's purchasing function. Since the new system (KFIS) is equipped to handle dependent care assistance and electronic fund transfer, without the prospects of a missed payroll, the advantages outweighed the disadvantages. The common sense of not spending money, time and scarce programming resources on something you are going to throw away was persuasive. As much as I regret the

disappointments of not having these desirable programs available sooner, I remain comfortable that our decisions were sound, the legal authority to delay was clear, and the best long-term interests of state employees were being served. The legality issue, in fact, was resolved this fall when the Supreme Court summarily denied the writ of mandamus filed by KAPE.

Shortly after the 1989 Session, we began receiving inquiries from a few legislators about the status of our implementation of dependent care assistance. In response to the concerns, we explored alternatives to programming KIPPS to see if we could accelerate the availability of the program. In every instance, we encountered problems that made the alternatives impractical or impossible. A full report dated July 28, 1989, was presented to the interim Committee on Ways and Means/Appropriations, and a copy of that report is attached to this testimony. At that time I expressed regret that we had not brought this situation more forcefully to the Legislature in the 1989 Session.

The interim Committee, nevertheless, has recommended introduction of S.B. 435, which requires us to implement direct deposit and dependent care assistance within 180 days of its effective date.

To each member of this Committee, I regrettably say we must vigorously oppose this bill. We are as anxious as you to

implement these programs, but a timely and accurate payroll must be our first priority. Under KIPPS, the issuance of each payroll is tenuous. We avoid and resist even the most simple modifications to this fragile software. I do not want to be an alarmist, but the timeframe imposed by Senate Bill 435 places the state payroll in jeopardy. To compound the problem, if we devote the next six months to a re-programming effort on KIPPS, it delays the KFIS program and lengthens our dependence on an unreliable system.

A delay of KFIS impacts other employee benefits. Under KFIS, we plan to offer employees a flexible spending account for medical costs not covered by the State health insurance plan. This feature, like the electronic fund transfer, provides a benefit to a far larger number of state employees than the dependent care assistance program, which may benefit only two to four percent of the State's employees.

You have very legitimate concerns about the need to proceed with the programs embodied in S.B. 435. The Department of Administration shares your concerns. We are well on our way to implementation, and you have before you a draft of the materials that will be distributed to employees for the dependent care assistance program enrollment. Our plans call for making the dependant care assistance and electronic fund transfer programs, as well as the new medical cost deduction,

available as we start phasing agencies onto the new personnel/payroll system in December.

In conclusion, Mr. Chairman, let me reiterate our three-fold objection: one, a real risk of missing a state payroll; two, a delay in implementing other benefits for employees under KFIS; and three, a waste of taxpayer's money, which this administration cannot support.

Just plain economic sense dictates you do not spend time and money on something you will throw away in a few months. Additionally, no legislative committee, no legislator or any legislation should tell the Executive Branch from whom they should buy hardware or software, or what equipment to use. This bill tells us to run dependent care assistance and electronic fund transfer on the Unisys/KIPPS system, and that the gridlock on computer decisions is not ended.

Your cooperation and understanding are appreciated as we go through this major transition period to provide better services and more benefits to state employees.

7640A

July 28, 1989

Kansas Department of Administration

Report on Dependent Care Assistance
(IRS Flexible Spending Account Salary Reduction)

The Department of Administration has conducted an exhaustive review of its February 1989 decision to delay implementation of the dependent care assistance program (authorized under the Internal Revenue Service Code as a flexible spending account salary reduction). The Department also considered the related issues of electronic fund transfer (direct deposit of employee paychecks) and payroll deduction of revised dues for the Kansas Association of Public Employees (KAPE). This report is intended to summarize our review and clarify a number of issues which have been raised. We have sought to challenge every assumption and consideration that supported the initial decision, in order to ensure that no reasonable alternative was overlooked.

Background

The 1988 Legislature, in House Bill 2850, authorized the Secretary of Administration to establish a state employee dependent care assistance program. The program was to take effect not later than July 1, 1989. But the Legislature recognized the potential lack of resources and made the timing of the program subject to the "approval of the Secretary of Administration to assure adequate data processing resources ..." [K.S.A. 1988 Supp. 75-6512(c)]. In February 1989, the Secretary found that adequate data processing resources were **not** available. The major complicating factor was the schedule for replacing the Department's central software systems, a project which also was authorized by the 1988 Legislature.

At that time, funding was provided for a new personnel/payroll software system and new software for the Division of Purchases. The Department subsequently included acquisition of accounting software in its plans and began the Kansas Financial Information Systems (KFIS) project.

During the 1989 Session, attacks on the KFIS project by the Unisys Corporation became the central focus of legislative attention for the Department. While, in retrospect, the Department regrets its failure to provide a status report during the Session on implementation of the dependent care assistance program, the battle with Unisys eclipsed all other issues.

Data Processing Issues

The decision to delay the dependent care assistance program has been attributed in media reports to "computer capacity" problems, but this is not accurate. Certainly the Unisys machine is at full capacity and the Department wishes to avoid additional workload on the system if possible, as the Department moves to a different computer system with more capacity. However, processing the dependent care assistance program would place minimal demand on the Unisys machine.

The real problem is the lack of computer programmers who are familiar with the State's current personnel/payroll system (KIPPS). Turnover among this staff is a constant concern and a continuing problem. KIPPS is a complex, poorly documented and, therefore, **extremely fragile** system. Programming changes by inexperienced technicians entail the risk of an inadvertent disruption of the entire payroll process. For example, the Department found it impossible to implement the new pay plan with longevity payments and Phase III of the classification study without problems. Although the amount of pay will be accurate, some employees will find that their year-to-date balances are incorrectly reported on their August 1 paychecks. This occurred despite the Department's emphasis on an accurate and timely payroll as its highest priority.

The February decision to delay implementation came on the heels of a resignation by an experienced programmer and was made in recognition of the need to devote as many man-hours as possible to the KFIS project. The estimate at that time was that 2,400 man-hours of programming would be required to implement the dependent care assistance program. In the Department's view, that level of resources simply did not exist.

In response to concerns expressed by Governor Hayden and certain legislators regarding the delay, the Department decided in mid-June to review its position and explore other alternatives. First, the Division of Accounts and Reports noted that a current deduction field for city income tax was not being used, and the existence of this field allowed DISC to revise the programming estimate from 2,400 hours ($98,400) to 1,600 hours ($65,600).

The Department also investigated the possibility of contracting with a private firm or one of the universities to calculate payroll for employees who chose to participate in the dependent care assistance program. However, due to the enormous lead time that would be necessary--to comply with federal Internal Revenue Service requirements, to allow employees time to assess whether the program would be beneficial in their individual circumstances, and to process employee enrollments--no alternative was found that would allow the Department to offer the program before the spring of 1990.

Lastly, the Department explored the potential for turnkey contractual services for implementation of the dependent care assistance program--on the old KIPPS system--in an effort to expedite the process. This approach also proved to be without merit, for the following primary reasons:

- Hiring an outside consultant service for computer programming presented the same problem that existed with the use of in-house personnel--e.g. lack of familiarity with the Unisys/KIPPS system which would necessitate a lengthy training period and/or significant risk to the fundamental payroll process;

- The implementation deadline would not have been significantly enhanced, even with early completion of the required computer programming, due to necessary consulting services for implementation of the program; and

- Funding was not available for these services.

Plans for the implementation of KFIS have been continuous since the appointment of a full-time program manager in November 1988. The tentative schedule for implementing the new KFIS system calls for payroll production for a pilot agency in May or June 1990, with all agencies operating under the new system by late fall of that year. (This timeframe will be reviewed again by October 30, 1989.)

This schedule means that, even if we begin immediately with dependent care programming on KIPPS, the program may be available only a month or two sooner than it otherwise would be available under the new KFIS system. Conversely, proceeding now with dependent care assistance would mean a delay for the new KFIS system and would lengthen the time during which the Department will have to rely on old software and on a computer which already is operating at capacity.

The wisdom of investing significant effort and funding in a system that is being phased out, in order to make marginal gains in the schedule for implementation of the dependent care assistance program, is even more questionable today than it was in February.

It should be noted that Unisys has proposed to solve the computer capacity problem by offering a hardware upgrade at "no additional cost to the State." It has been suggested that this upgrade would accelerate implementation of the dependent care assistance program. However, it could take as long as nine months to complete the computer upgrade, which would delay dependent care and/or KFIS even further. Furthermore, the proposed upgrade could **not** be accomplished without additional costs, for which no funds are available. Finally, although the upgrade would solve computer capacity problems, a very significant number of programming hours still would be required.

In summary, the initial decision to delay implementation of the dependent care assistance program was based on the lack of experienced programmers to support the requirements of the Department. For the reasons enumerated above, the Department's re-evaluation continues to support this finding.

Additional Dependent Care Assistance Issues

The media attention given to the delay in implementation of the dependent care assistance program illustrates what appears to be a very limited understanding of this benefit. At the time the initial legislation was passed, the uncertainties of the federal tax regulations involved made it very difficult for either Department officials or legislators to fully identify the ramifications of such a plan.

The dependent care assistance program is governed by the provisions of Sections 125 and 129 of the federal Internal Revenue Code. In general, the program allows a taxpayer to exclude from gross income an amount not to exceed $5,000. This amount is to be set aside to reimburse the employee for expenses incurred for dependent care.

There are several caveats about the program which must be recognized:

1) An employee who designates an annual dependent care salary reduction but does not incur expenses at this level forfeits the difference. It cannot be returned to the employee as taxable income.

2) Many employees--virtually all employees with annual incomes below $24,000--would find it more advantageous to take the existing federal dependent care tax credit. Using the dependent care assistance program would preclude one from also taking the federal dependent care tax credit.

3) An employee cannot simply receive a check for dependent care expenses. Instead, they must document their dependent care costs and submit claims for reimbursment.

4) Flexible spending accounts must be tested under Section 89 of the federal Internal Revenue Code to ensure that the program does not discriminate in favor of highly paid employees. Should such discrimination be found, a highly compensated employee could be liable for additional income tax.

These restrictions probably explain why other employers offering this program typically experience a participation rate of 2 to 4 percent of eligible employees.

Another aspect worthy of mention is the considerable administrative apparatus required by the Federal Government. The dependent care assistance program is available only under the broader, IRS-designated umbrella of a flexible compensation (cafeteria benefits) plan. As mentioned earlier, such a plan must be in compliance with Section 89 of the federal Internal Revenue Code.

IRS regulations in this area are extensive and complex. In many instances, they are even at this late date not finalized. It is questionable whether the Department has adequate expertise to ensure compliance with IRS requirements, and it appears that consultant services are inescapable. Our current flexible compensation plan will have to be revised. A flexible compensation plan document must incorporate all legal provisions and provide various taxable and non-taxable options.

Other administrative issues also must be resolved. These include decisions regarding internal or third-party administration, minimum check disbursement, disbursement timing, and enrollment and reimbursement claims forms.

Perhaps the most extensive requirement involves the educating of state employees about the program, as to both in its advantages and its limitations. A particularly difficult issue may be the proposed IRS requirement that we calculate, for every interested employee, the difference between using the state dependent care assistance program versus the federal dependent care tax credit.

A final issue to be resolved is the question of when the program legally can be

implemented. Our plan year begins January 1. It clearly is impossible for us to offer the program by January 1, 1990. If IRS does not allow introduction of a new program for less than a full plan year, we could not offer the dependent care assistance program as part of our flexible compensation plan before January 1, 1991. We are seeking clarification on this item.

Electronic Fund Transfer and KAPE Dues

Virtually all of the previous discussion under "Data Processing Issues" applies as well to electronic fund transfers and KAPE's proposed change in its dues structure. The latter two programs do not involve the administrative and legal complexity that the dependent care assistance program presents, but they do entail demands which our limited programming and financial resources cannot accommodate. It is worth noting that KAPE itself elected to delay its new dues structure until the KFIS system is implemented, thereby saving more than 1,800 hours ($75,000) in programming costs.

The Future

Despite the many problems and concerns that attend the issues in this report, implementation of the new financial information system (KFIS) holds much promise. For example, the 1,600 man-hours of programming required to implement the dependent care assistance program under our current KIPPS/Unisys system would be reduced to 120 hours under KFIS--a savings of more than $60,000.

Following the February decision to delay implementation, monies appropriated for programming were used to acquire the flexible compensation component of KFIS. From a programming standpoint, the new system makes it much easier for the Department to offer expanded benefits. In fact, we plan to offer a flexible spending account for health care expenses at the same time the dependent care assistance program becomes available. This program mirrors the dependent care assistance program, but typically benefits a significantly greater number of employees. Participation rates for health care expense accounts, for example, average 15 to 25 percent of eligible employees--compared to 2 to 4 percent participation rates for dependent care accounts.

A discussion of KFIS belongs in a more comprehensive context than the subject of this report. In general, KFIS offers the State a more stable, comprehensive and cost-effective financial management system. The relative ease with which programming for the dependent care assistance program can be handled under KFIS is only one illustration of the benefits we expect to derive from this new software.

Conclusion

The Department's decision to delay the implementation of the dependent care assistance program was not made lightly. We share the frustrations and concerns

that have been expressed. It is unfortunate that the many legal, financial and other constraints outlined in this report were not fully understood at the time the enabling legislation was passed. On the other hand, the Legislature was foresighted enough to recognize that implementation of the program must be timed with the availability of resources; provision was made in the statutes for the Secretary of Administration to exercise discretion in this regard.

In light of this most recent review of the dependent care assistance program and related issues, the Department reaffirms its February 1989 decision to delay implementation. In our judgement, this decision is in the best interest of state employees and the taxpayers of Kansas.

DRAFT

STATE OF KANSAS

OFFICE OF THE GOVERNOR
State Capitol
Topeka 66612-1590
(913) 296-3232

Mike Hayden *Governor*

Date

Dear Fellow Employee:

The State's employees are its most valuable resource. The State is committed to provide stable employment and quality benefits to you now and in the future.

Under our new **KansasCares** Spending Account Program you may be able to save taxes and increase your spendable income.

I am pleased that Kansas can enhance your benefit coverages with this new plan for you and your family. Please take the necessary time to review the enclosed information and share it with your family.

Sincerely,

Mike Hayden

ГRODUCING: THE *KansasCares* SPENDING ACCOUNT PROGRA...

The *KansasCares* Spending Account Program is like a bank account. You deposit part of your pre-tax salary and later reimburse yourself for dependent day care expenses. Based upon the expenses you expect to pay in the coming year, you decide how much you want to set aside.

The account provides tax savings and may increase your take home pay. The account is subject to IRS limitations under Sections 129 of the Internal Revenue Code. Take time to read the information about *KansasCares* carefully before deciding to enroll in this benefit program.

HOW *KansasCares* WORKS

The *KansasCares* Spending Accounts are made possible under the State of Kansas Flexible Compensation Plan. It is a salary reduction plan which allows pre-tax dollars to be placed into flexible spending accounts. You decide by how much you want your salary reduced.

If you are a newly hired employee, you may participate in the *KansasCares* Spending Account effective the first day of the month following 60 days from your date of employment. If you are a current employee eligible to participate in the *KansasCares* Spending Account, you elect the salary reduction amount during the open enrollment period before the beginning of the Plan Year (January 1.) The salary reduction is then made before federal and social security taxes are deducted from your paycheck.

During the year, as you pay eligible expenses not reimbursable from other sources, you submit claims for reimbursement from your *KansasCares* Spending Account. You may be reimbursed from your Spending Account up to the total amount that you choose to deposit into it.

It is important to determine carefully the expenses you think you will have during the year, because the Internal Revenue Service regulations say that if there is any money left in an account at the end of the year, the money is forfeited.

WHO IS ELIGIBLE TO PARTICIPATE

Any employee who works for the State in an Employee-Employer relationship and is eligible for coverage under the Heath Care Plans established by the Health Care Commission is eligible to participate in the *KansasCares* Spending Account program.

FAMILY STATUS CHANGES

The Plan Year for your *KansasCares* Spending Account begins on January lst and ends on December 31st. Once you have elected how much money you want to put into an account, that amount cannot change unless you experience a significant life event. The Internal Revenue Service says that the change must be caused by and consistent with one of the following events:

- Marriage, divorce, or legal separation of the employee;
- Death of a spouse or a dependent;
- Birth or adoption of a dependent;
- Dependent changing household as the result of a custody agreement;
- Pregnancy or loss of an unborn child;
- Termination or commencement of employment of a spouse;
- Change in employment status of spouse or employee (such as part-time to full-time, full-time to part-time, or unpaid leave of absence);
- Significant changes in health coverage of employee or spouse that are "attributed to the spouse's employment."

KansasCares AND SOCIAL SECURITY

Enrollment in **KansasCares** reduces your taxable pay. This could result in a slight reduction in your ultimate Social Security benefit. However, the savings realized from paying for benefits with tax-free dollars should more than offset any reductions in the social security benefit. Your retirement benefits from KPERS will not be affected by a salary reduction in a *KansasCares* Spending Account. Contact a tax advisor for information

(over)

regarding your individual Social Security benefit and the impact *KansasCares* may have on it.

AVERAGE FORFEITURE AMOUNTS

The IRS requires that you forfeit any money in an account at the end of the Plan Year. If you estimate your annual expenses carefully, leftover funds should not be a problem. According to a recent national survey, the average employee using spending accounts, forfeits $15 per year in dependent day care account.

KansasCares SPENDING ACCOUNT ADMINISTRATION COSTS

The State of Kansas pays for the entire cost of the administration of this plan. Every dollar that you put into the *KansasCares* Spending Accounts is available for the dependent day care expenses.

TERMINATION OR LOSS OF ELIGIBILITY TO PARTICIPATE

In the event you terminate from state service or otherwise become ineligible to participate in ***KansasCares***, your access to the ***KansasCares*** Spending Accounts stops unless you apply for COBRA (Consolidated Ombusman Reconciliation Act). If you do not apply for COBRA, you may submit claims for 90 days after your termination or loss of eligibility for expenses incurred during the period you were eligible to participate in the program. Any money left in an account after 90 days will be forfeited.

If you apply for COBRA, you may continue to make after-tax contributions to the account and continue to submit claims for the entire period you were covered by the account.

If you terminate from State service and return during the same Plan Year or regain eligibility during the Plan Year, you may not elect additional salary reductions to an existing ***KansasCares*** Spending Account until the open enrollment period for the next Plan Year or you satisfy the waiting period for eligibility, whichever is later.

KansasCares SPENDING ACCOUNT OVERPAYMENT

In the event that you are overpaid from a ***KansasCares*** Spending Account, you must pay back any overpayment. The overpayment could be due to termination of employment, change to ineligibility status, or family status change.

ABOUT THIS INFORMATION PACKET

This information packet summarizes the major features of the ***KansasCares*** Spending Account Program. Every effort has been made to ensure that this information is clear, easy to understand and accurate. The official plan document contains complete plan provisions and is available for inspection, upon request, in the Division of Personnel Services. In case of any discrepancy between this information packet and the official plan document, the official plan document will govern.

Nothing in the ***KansasCares*** Spending Account Program shall be construed as a contract of employment between the State of Kansas and any employee, nor as a guarantee of any employee to be continued in the employment of the State, nor as a limitation on the right of the State to discharge any of its employees with or without cause.

KansasCares DEPENDENT DAY CARE ACCOUNT

The Dependent Cay Care Account is intended to permit reimbursement of expenses related to child care, or care for a disabled dependent, so that you and your spouse may continue to work. Any expense that would qualify for a dependent care tax credit on your federal income tax return is eligible for reimbursement in the ***KansasCares*** Dependent Day Care Account.

Expenses eligible for Dependent Cay Care reimbursement include:

- o Charges for a licensed day care facility or nursery school; or
- o Charges for a baby sitter in your home (other than your spouse, a qualified dependent under the age of 19, or a housekeeper); or
- o Charges for care for an adult who qualifies as a dependent for income tax purposes.

Because the Dependent Day Care Account is designed to enable you and your spouse to work, certain qualifications must be met for you to use this account. You must be a single parent, or if you are married, your spouse must work or qualify as a full-time student for at least five (5) months during the year. In addition, the dependent who is being cared for must be a dependent child under age 13 for whom you are entitled to claim an exemption under IRS rules, or any other dependent (including your spouse) who is incapable of self-care.

KansasCares AND THE FEDERAL INCOME TAX CREDIT

Generally, if your combined family income is less than $24,000 per year, it may be to your advantage to claim a dependent care tax credit on your federal income tax return rather than using the ***KansasCares*** Dependent Day Care Account. You will want to determine which option is best for you by comparing your expected federal tax credit with your expected savings using the ***KansasCares*** Dependent Day Care Account. A comparison worksheet is included in this information packet or check with a tax advisor.

MAXIMUM AND MINIMUM CONTRIBUTIONS

The maximum contribution is $5,000 per year or $2,400 per year if you are married filing separate returns. The minimum contribution is $240 per year regardless of federal income tax filing status. If you or your spouse earn less than $5,000 per year, then your total contribution may not exceed the amount of the lower paid spouse's annual earned income.

HOW TO PROCESS A CLAIM

In order to be reimbursed for eligible expense you must complete a ***KansasCares*** Spending Account Reimbursement Claim Form. Claim Forms are available for the ***KansasCares*** Spending Account Program from (Name and Address of third party administrator).

EVIDENCE OF EXPENSE

Claims must include acceptable evidence of your expenses. To process a **Dependent Day Care** Claim you must include the name of the dependent for whom the dependent care was provided, a written statement from the provider stating that the dependent care expense has been incurred and the date and the amount of the expense and the dependent care provider's name, address, and either Tax Identification Number or Social Security Number. The only exception to providing the Tax Identification Number is if the provider is a church or other charitable organization.

To process a **Health Care** Claim you must include the name of the employee, spouse or dependent for whom the service or product was provided, a written statement from the provider which includes the provider's name and address stating that the medical expense has been incurred and the date and the amount of the expense. You must also include an Explanation of Benefits (EOB) from the insurance carrier.

MINIMUM CLAIM

No payment will be made from your ***KansasCares*** Spending Account until your total unpaid claims for Health Care and/or Dependent Day Care expenses total $50.00.

ACCOUNT STATEMENTS

The FSA Management Company is responsible for preparing and distributing periodic account statements. An explanation of your reimbursement activity and account status will be mailed to you within 30 days of the close of each calendar quarter.

Additionally, all participants regardless of whether or not they have submitted any claims, will receive a statement prior to the end of the Plan Year. A final statement and summary will be mailed 90 days following the end of the Plan Year.

YEAR END CLAIMS PROCESSING

You have 60 days after the end of the Plan Year (March 1), to submit claims for expenses incurred during the Plan Year. At the end of the Plan Year, all unpaid claims (even if they total less than $50.00) will be paid up to the account balance in either the Dependent Day Care or Health Care account. Any unused account balances will be forfeited on April 18.

PROCESSING TIME FOR REIMBURSEMENTS

Reimbursement checks will be mailed once a month from (name of thirdy party administrator) on the 27th of the month. Claims received by the 18th of the month will be processed by the 27th.

Additionally, you should plan ahead for the effect of your ***KansasCares*** Spending Account contributions on your paycheck during the first month of the participation in the program. Your contributions come out of your salary in advance, so the result is a delay between the time your money is taken out of your paycheck and the time you can get it back in the form of a reimbursement check.

At the beginning you will be paying your dependent care and health care bills as a salary reduction and again as a payment to your provider. As you receive your reimbursement checks, your payments will be equal and, by the end of the Plan Year, things will even out.

QUESTIONS CONCERNING YOUR CLAIM

Contact (third party administrator toll free number) during the hours of 8:30 am to 4:30 pm Monday through Friday.

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HOW TO ENROLL IN THE *KansasCares* SPENDING ACCOUNT PROGRAM

To make your ***KansasCares*** Spending Account Program work for you, it is important that you plan carefully in predicting your eligible dependent day care expenses. Be conservative in your estimates so that your pre-tax dollars can be used wisely and you can avoid forfeiture.

If you are interested in enrolling in the ***KansasCares*** Spending Account Program, review and complete the enclosed enrollment form. If you are a new hire or have just become eligible to participate in the ***KansasCares*** Spending Account Program, you have thirty (30) days from your eligibility date to complete and submit the enrollment form. If you are a current eligible employee, complete the enrollment form and submit it to your Agency Personnel Officer no later than October 31. It will become effective with the new Plan Year.

With careful planning, your ***KansasCares*** Spending Account program can be one of your most valuable benefits. If you have questions regarding the plan, contact your Agency's Personnel Officer or the Benefits Specialist in the Division of Personnel Services at 913/296-0209.

An Example Using *KansasCares* Spending Account Program

The following is an example of the potential advantages of participating in the ***KansasCares*** Spending Account Program. Assume for this example you are married with two dependent children, and you and your spouse each claim two dependents for withholding on your income tax. Your combined annual income is $45,000 (your spouse earns $20,000). You know that your child care will cost $3,500. To cover these expense, you elect to fund your Dependent Day Care Account with $3,500 through pre-tax salary reductions.

	Using ***KansasCares***	Without ***KansasCares***
Combined Annual Income	$45,000	$45,000
Dependent Day Care Account	- 3,500	
Taxable Income	$41,500	$45,000
Federal Income Tax	- 4,003	- 4,590
Social Security Tax	- 3,175	- 3,380
Take-Home Income	$34,322	$37,030
Federal Tax Credit		+ 700
Dependent Day Care Expenses		- 3,500
Year-End Income	**$34,322**	**$34,230**

In this example, you could save as much as $92 during the Plan Year by funding your ***KansasCares*** Spending Accounts with pre-tax salary reductions.

DEPENDENT DAY CARE WORKSHEET

Use this worksheet to estimate your tax savings precentage and to decide which option, the Federal Tax Credit or the *KansasCAres* Dependent Day Care Account, is better for you.

Estimated Dependent Care Tax Credit Percentage

1. Estimated dependent day care expenses (this cannot be greater than Line 2 or Line 3 below): ____________
2. Your annual earned income: ____________
3. Your spouse's annual earned income: ____________
4. Add Line 2 and Line 3: ____________
5. Multiply $1,900 times number of eligible dependents: ____________
6. Subtract Line 5 from Line 4: ____________
7. Based on Line 6 above, select the tax credit percentage from the Following Table: ____________

Estimated KansasCares Dependent Day Care Account Percentage

8. Your annual earned income: ____________
9. Eligible dependents (same as Line 5): ____________
10. Subtract Line 9 from Line 8: ____________
11. Based on Line 10 above, select the total tax percentage from the Following Table: ____________

Which is better? Compare your Tax Credit percentage on Line 7 with your *KansasCares* Dependent Day Care Account percentage on Line 11. Generally, you would choose the option that shows the greater percentage of savings. Consult your tax advisor for confirmation or addtional information.

ENROLLMENT FORM

Form to be provided by third party administrator