

Approved: 2-6-97
Date

MINUTES OF THE HOUSE COMMITTEE ON APPROPRIATIONS.

The meeting was called to order by Chairperson Phil Kline at 1:34 p.m. on February 4, 1997 in Room 514-S of the Capitol.

All members were present except: Representative O'Connor - Excused

Committee staff present: Alan Conroy, Russell Mills, Stuart Little, Legislative Research Department;
Jim Wilson, Mike Corrigan, Revisor of Statutes Office;
Marcia Ayres, Appropriations Secretary; Helen Abramson, Administrative Aide

Conferees appearing before the committee: Mr. Paul Schraeder, Buck Consultants, Inc.
Mr. Meredith Williams, KPERS

Others attending: See attached list

Paul Schraeder, consulting actuary with Buck Consultants, was introduced to discuss the consultant study on developing a permanent policy on post-retirement benefit adjustments by the Kansas Public Employees Retirement System (KPERS). He reviewed a handout (Attachment 1) and answered questions from the committee members.

Meredith Williams, executive secretary of KPERS, brought notebooks for the members which give an overview of KPERS. (copies available in Legislative Research) He commented that he agreed with many of the bottom lines drawn by the consultant, but he cautioned that some of the comparisons are difficult to judge. He believes the state of Kansas has been very responsible in dealing with KPERS and explained some of the recent history. He covered some of the areas of the report where he agreed with the consultant and some where he differed.

A motion was made by Representative Mollenkamp, seconded by Representative Spangler, to introduce a bill clarifying conflicting statutes in the real estate appraisal board's budget. The motion carried.

The members were reminded that no meeting has been scheduled for tomorrow. The meeting adjourned at 3:10 p.m.

The next meeting is scheduled for February 6, 1997.

APPROPRIATIONS COMMITTEE GUEST LIST

DATE: FEB. 4, 1997

NAME	REPRESENTING
Kirk Decker	City of Hesston
Dean Anderson	Kansas Farm Bureau
Rick P... <i>(Signature)</i>	Kansas Farm Bureau
Ernie Mikereff	Kans. Farm Bureau
Margaret Mikereff	Ks. Farm Bureau
Verona Hibbel	Hesston Economic Development
Gary BURTON	KFB
Connie Burton	KFB
Tom Young	AARP
Rail Cowley	KRTA
Debbie Kueser	KFB
Dail Kueser	KFB
Emily Gulfield	KFB
Phil Miller	KFB Winfield
Amie Glaves	Intern-Rep Minor
Frances Jelts	Farm Bureau
Cal Dickinson	AARP
Kent ELKins	Kansas Farm Bureau
Ange JimAO	Intern

Loren Elkens KFB

**DEVELOPMENT OF A
POST RETIREMENT BENEFIT ADJUSTMENTS POLICY
FOR THE
KANSAS PUBLIC EMPLOYEES RETIREMENT SYSTEM**

Appropriations
2-4-97
Attachment 1

**PRESENTATION TO
SENATE WAYS AND MEANS COMMITTEE, AND
HOUSE APPROPRIATIONS COMMITTEE
KANSAS LEGISLATURE**

**BUCK CONSULTANTS
FEBRUARY 4, 1997**

OBJECTIVES OF STUDY

1-2

- **Analyze need for Post-Retirement increases**
- **Consider alternatives**
- **Analyze both short-term and long-term costs**
- **Consider financing alternatives**
- **Propose policy statements**

BACKGROUND

1-3

- **The Legislature has granted frequent and significant ad hoc Post-Retirement benefit increases in the past**
- **No increases granted in 1995 or 1996**
- **Substantial improvements made to KPERS benefits in the 1980's and 1990's**
- **KPERS contributions are less than actuarially required amounts**

PAST KPERS POST-RETIREMENT INCREASES

1-1

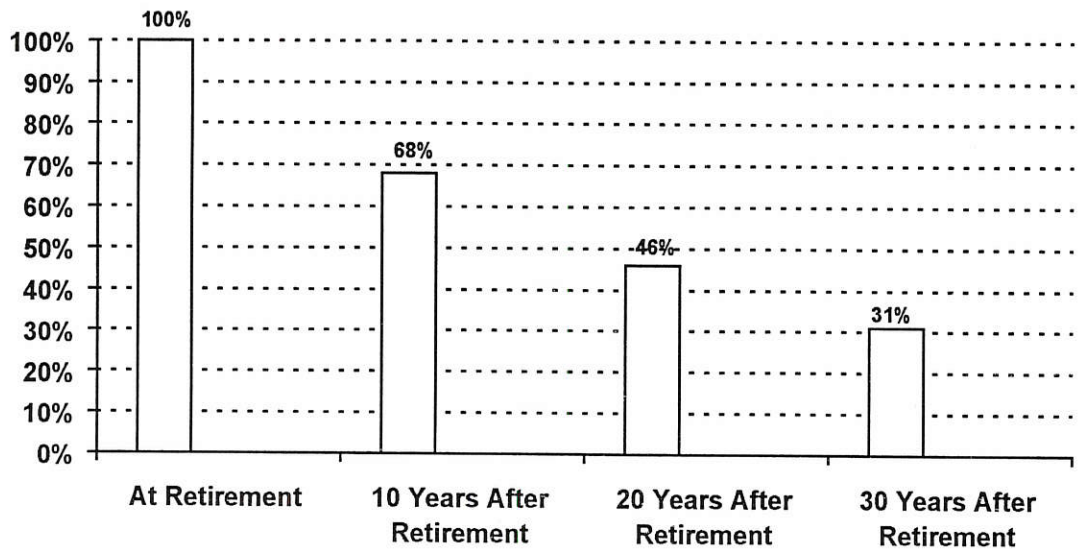
Year	CPI	CPI - 1%	KPERS Increases
'77	6.4%	5.4%	5.0%*
78	5.9	4.9	1.1**
79	6.5	5.5	--
80	9.9	8.9	8.3
81	14.3	13.3	--
82	11.2	10.2	10.0
83	7.4	6.4	--
84	3.5	2.5	10.0
85	3.5	2.5	5.0
86	3.1	2.1	3.0
87	1.3	.3	2.0
88	4.2	3.2	3.0
89	4.0	3.0	4.0
90	4.7	3.7	4.0
91	5.4	4.4	1.0
92	3.7	2.7	4.2***
93	3.0	2.0	14.0***
94	2.6	1.6	4.5***
95	2.8	1.8	--
96	2.6	1.6	--
Compound Annual Rate	5.3%	4.3%	3.6%

- * One time increase only (13th check)
- ** Increases greater for members retiring before 1976
- *** Average Increase

NEED FOR POST-RETIREMENT BENEFIT INCREASES TO REPLACE LOSS OF PURCHASING POWER

1-5

4% Annual Inflation



Purchasing Power of Fixed Benefit

SURVEY OF POST-RETIREMENT INCREASES FOR STATE RETIREMENT SYSTEMS

1-6

Work Place Economics Survey

- Statewide Retirement Plans Covering State Employees
- All 50 States
- 1996

Post-Retirement Benefits	% of Systems
Ad Hoc Only	48%
Automatic - CPI Based*	30%
Automatic - Flat Benefit*	20%
Based on Investment Performance	2%

*Average annual increase is 3.1% assuming 4% inflation

STATE OF WISCONSIN RETIREMENT RESEARCH COMMITTEE

1-7

- Statewide Retirement Systems
- 83 Systems
- August 1994

Post-Retirement Benefits	% of Systems
Ad Hoc Only	29%
Automatic - CPI Based*	47
Automatic - Flat Benefit*	18
Based on Investment Performance	6

***Average annual increase is 3% assuming 4% inflation**

EXAMPLES

8-1

- **75 % of CPI if age 65 or older**
50% of CPI if less than age 65
- **CPI - Cap of 3.5% plus investment surplus**
- **80% of CPI, maximum of 5%**
- **3.1% automatic**
- **100% of CPI, 5% cap**

TYPES OF POST RETIREMENT INCREASES

1-9

- **Automatic or Ad Hoc**
- **Tied to Index fully or partially**
(e.g. - CPI, GNP Deflator, Wages)
- **Flat \$ or %**
- **To maintain some or all purchasing power**
- **Employee financed**
- **Combination**

POST RETIREMENT BENEFIT INCREASE ELIGIBILITY PRACTICES

1-10

- **Normal and Early retirees only**
- **After fixed age, or number of years of retirement**
- **Deferred Vested members**
 - ◆ **After benefits commence**
 - ◆ **Index considering deferral period**
- **Death and Disability benefits**
- **All periodic payments**

IF POST-RETIREMENT BENEFITS ARE INDEXED:

11

- **Most frequently tied to CPI**
- **Consensus that CPI overstates inflation for retirees (at least 1% per year)**

RETIREMENT INCOME REPLACEMENT NEEDS COMPARED TO BENEFITS AVAILABLE FROM KPERS AND SOCIAL SECURITY

1-12

- **Career employee considered retiring at age 62 with 30 years service and final annual salary of \$35,000**
- **Based on Federal and Kansas taxes**
- **Work and Age Related Expenses from the Retiree Project - Georgia State University**
- **Current KPERS benefits and Social Security**
- **Measure of ability of KPERS and Social Security to replace spendable income at time of retirement**

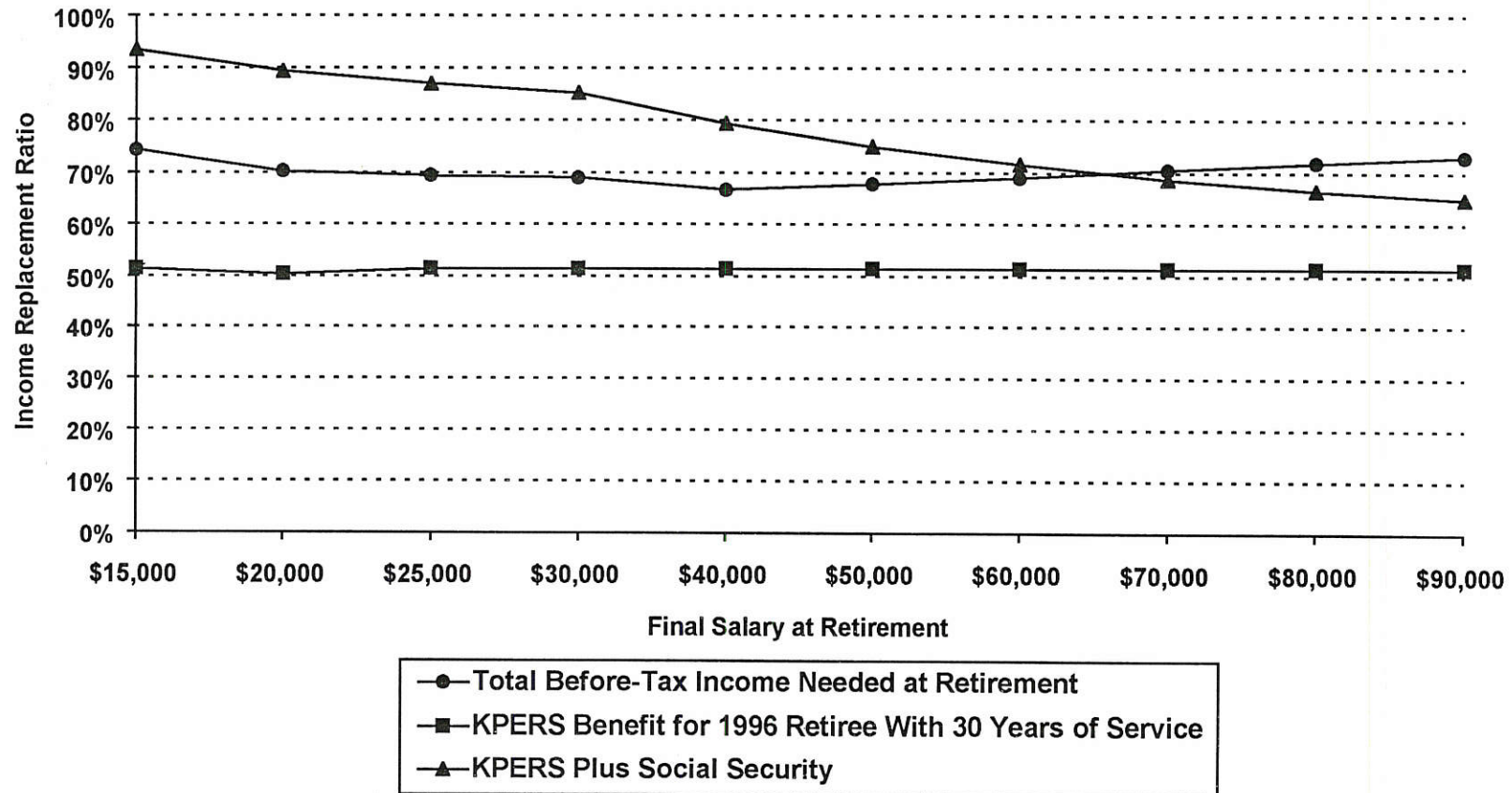
Kansas Public Employees Retirement System

Income Replacement Ratios Upon Retirement in 1996 as a Function of Taxes and Expenditures for a Career Employee Retiring at Age 62 with 30 Years of Service Taxation of Social Security Benefits at 85% with \$34,000 Threshold

1-13

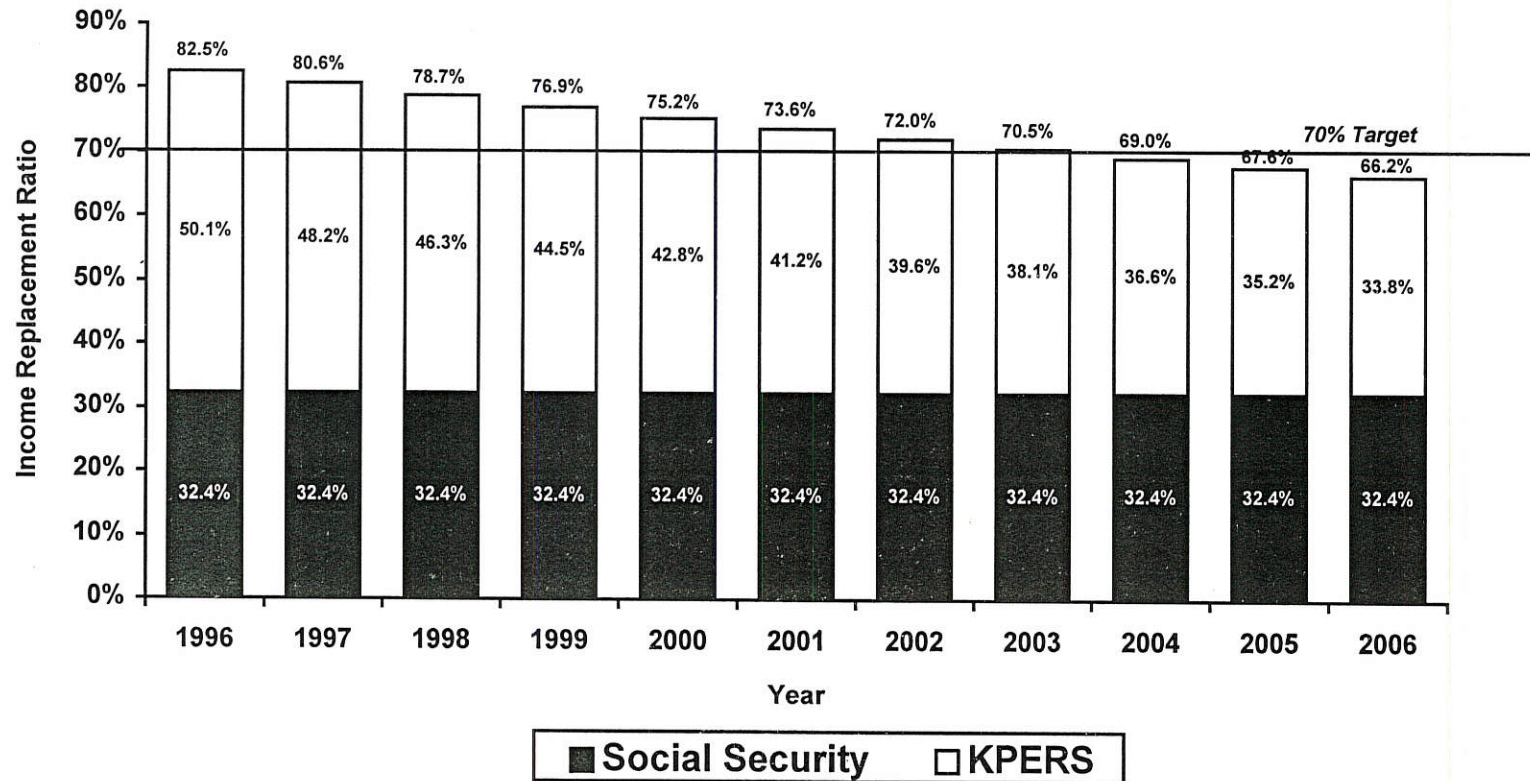
	\$15,000	\$20,000	\$25,000	\$30,000	\$40,000	\$50,000	\$60,000	\$70,000	\$80,000	\$90,000
1. Gross Pre-retirement Salary										
As a Percentage of Pre-retirement Salary	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
2. Less Contribution to KPERS	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
Less Social Security Taxes	7.7%	7.7%	7.7%	7.7%	7.7%	7.7%	7.7%	7.0%	6.3%	5.8%
4. Less Federal Taxes	7.9%	9.5%	10.5%	11.1%	14.5%	17.0%	18.6%	19.9%	21.1%	22.1%
5. Less State and Local Taxes	<u>2.8%</u>	<u>3.3%</u>	<u>3.6%</u>	<u>4.2%</u>	<u>5.2%</u>	<u>5.8%</u>	<u>6.2%</u>	<u>6.5%</u>	<u>6.7%</u>	<u>6.9%</u>
6. Pre-retirement After-Tax Income	77.7%	75.6%	74.3%	73.0%	68.7%	65.6%	63.5%	62.6%	61.8%	61.3%
7. Less Work & Age Related Expenses	<u>3.4%</u>	<u>5.4%</u>	<u>5.9%</u>	<u>5.8%</u>	<u>4.9%</u>	<u>3.7%</u>	<u>2.5%</u>	<u>1.5%</u>	<u>0.4%</u>	<u>-0.5%</u>
8. Income Available for Post-Retirement Consumption	74.3%	70.2%	68.4%	67.2%	63.8%	61.9%	61.0%	61.2%	61.4%	61.7%
9. Plus Post-Retirement Federal Income & Social Security Taxes	0.0%	0.0%	1.0%	1.7%	2.9%	5.8%	8.0%	9.3%	10.4%	11.2%
10. Plus Post-Retirement State and Local Income Taxes	<u>0.0%</u>	<u>0.0%</u>	<u>0.0%</u>	<u>0.0%</u>	<u>0.0%</u>	<u>0.0%</u>	<u>0.0%</u>	<u>0.0%</u>	<u>0.0%</u>	<u>0.0%</u>
11. Total Before-Tax Income Needed at Retirement	74.3%	70.2%	69.4%	69.0%	66.7%	67.8%	69.0%	70.5%	71.8%	73.0%
12. Social Security Benefit	<u>42.1%</u>	<u>38.0%</u>	<u>35.6%</u>	<u>33.8%</u>	<u>27.9%</u>	<u>23.5%</u>	<u>20.1%</u>	<u>17.3%</u>	<u>15.1%</u>	<u>13.4%</u>
13. Benefit Needed From KPERS to Replace Pre-Retirement Income (Line 11 minus Line 12)	32.3%	32.2%	33.8%	35.2%	38.8%	44.3%	48.8%	53.2%	56.7%	59.6%
14. KPERS Benefit for 1996 Retiree With 30 Years of Service	<u>51.4%</u>	<u>51.4%</u>	<u>51.4%</u>	<u>51.4%</u>	<u>51.4%</u>	<u>51.4%</u>	<u>51.4%</u>	<u>51.4%</u>	<u>51.4%</u>	<u>51.4%</u>
15. Deficit / (Surplus) KPERS Benefit (Line 13 minus Line 14)	-19.2%	-19.2%	-17.6%	-16.2%	-12.6%	-7.2%	-2.6%	1.8%	5.2%	8.2%

KPERS INCOME REPLACEMENT NEEDED TO MAINTAIN LIVING STANDARD FOR CAREER EMPLOYEE RETIRING AT AGE 62 WITH 30 YEARS SERVICE

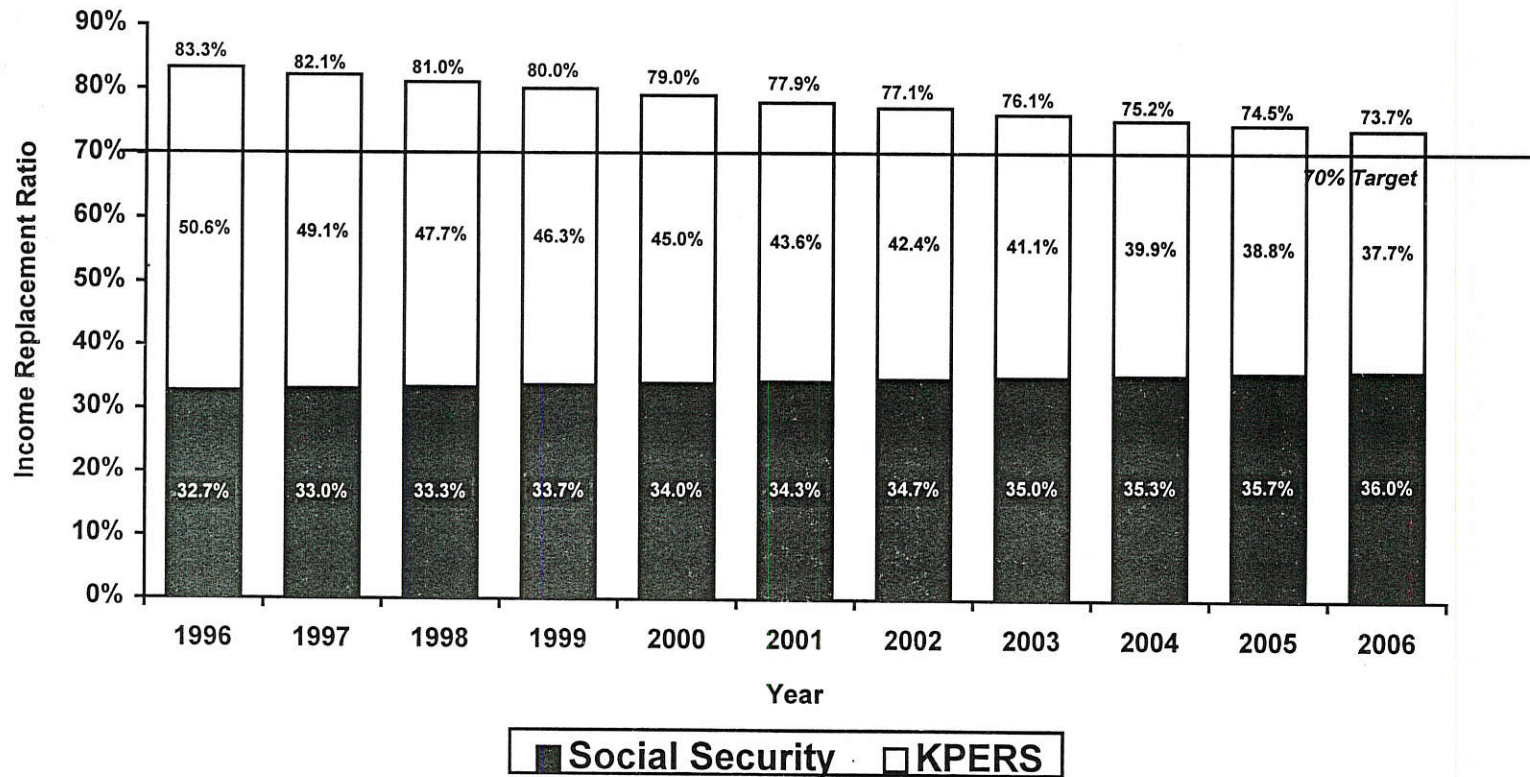


KPERs CAREER EMPLOYEE RETIRING IN 1995 10 YEAR PROJECTION OF INCOME REPLACEMENT RATE WITHOUT COLA ADJUSTMENTS ON KPERs BENEFIT ASSUMING CPI NEEDED (4%)

1-15



KPERS CAREER EMPLOYEE RETIRING IN 1995 10 YEAR PROJECTION OF INCOME REPLACEMENT RATE WITHOUT COLA ADJUSTMENTS ON KPERS BENEFIT ASSUMING CPI-1% NEEDED (3%)



CONCLUSIONS FOR EMPLOYEES RETIRING WITH CURRENT KPERS BENEFITS

1-17

- For most employees income replacement need is about 70% of pay
- For most employees, the combination of KPERS and Social Security is in excess of income replacement need. Short-fall is at high wage levels
- Need for Post-Retirement increases is not immediate

PAST KPERS RETIREES

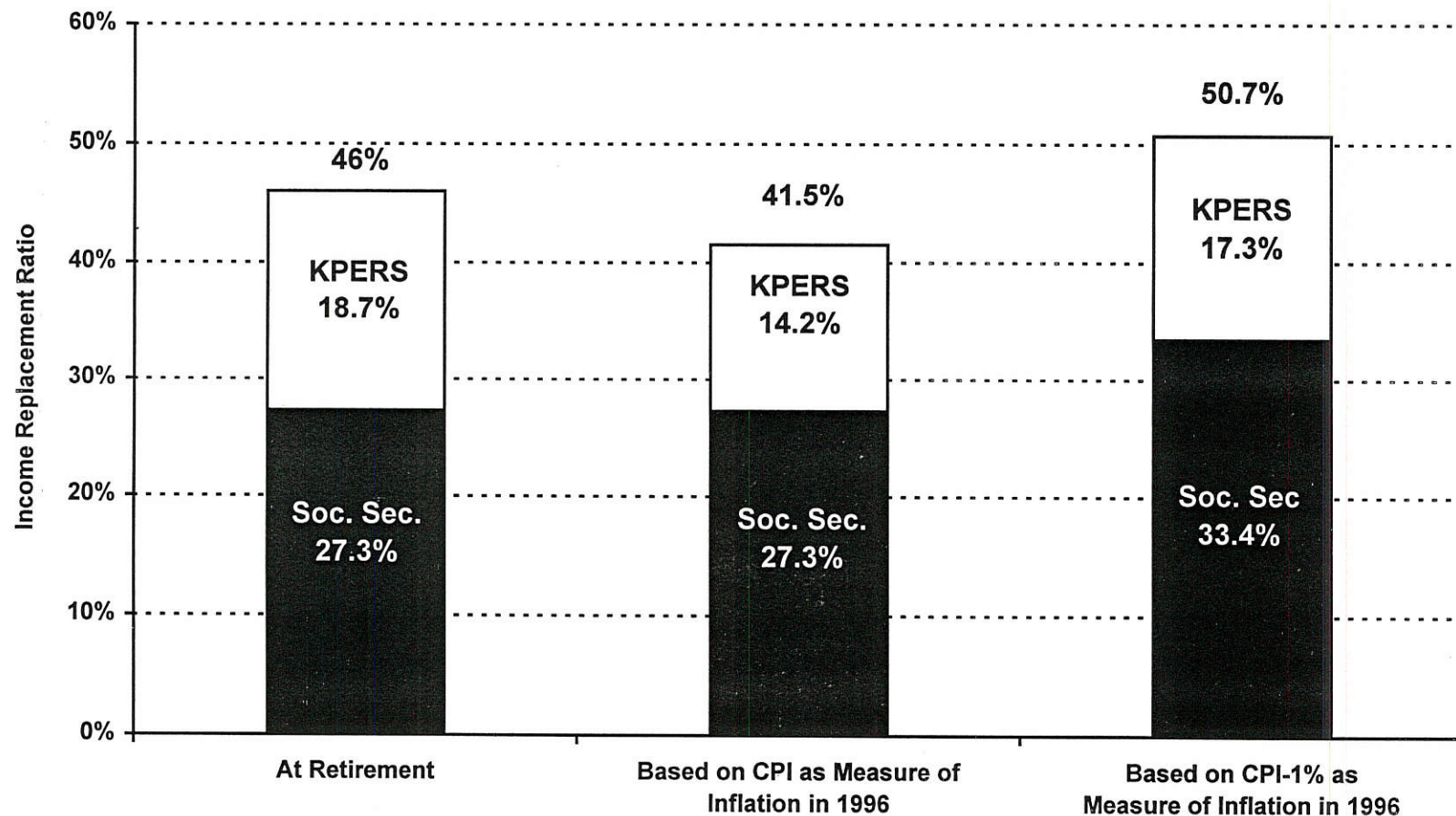
81-1

- **Retired under different conditions**
 - ♦ **KPERS Benefits (lower formula, prior service benefit, early retirement reduction, final average salary)**
 - ♦ **Social Security**
 - ♦ **Frequent Post-Retirement increases**

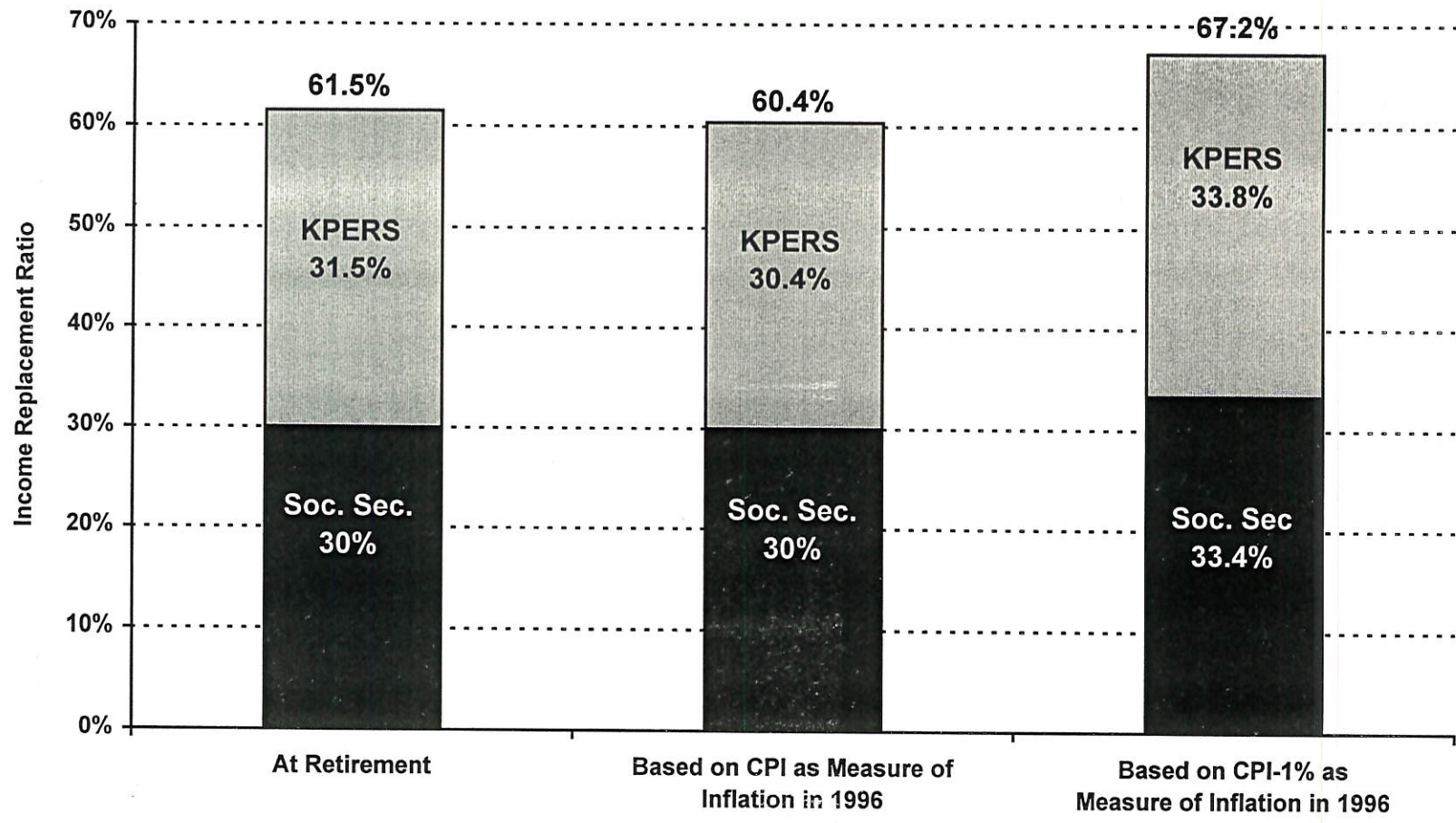
- **Projections for “Average” employee**
 - ♦ **Initial income replacement**
 - ♦ **Inflation adjusted income replacement today**

CAREER KPERS EMPLOYEE RETIRING IN 1975 MEASURE OF LOSS OF PURCHASING POWER

1-19

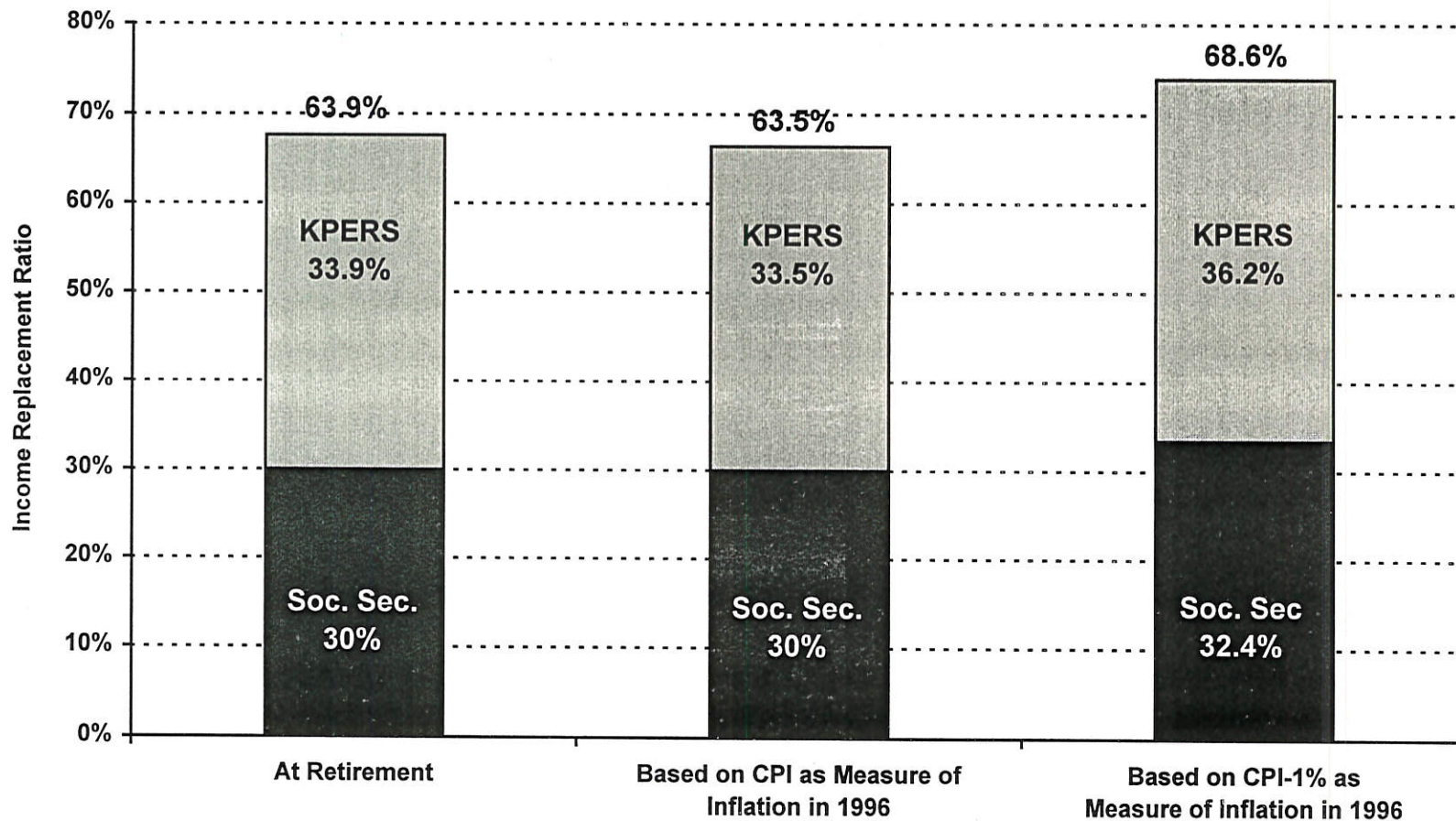


CAREER KPERS EMPLOYEE RETIRING IN 1985 MEASURE OF LOSS OF PURCHASING POWER



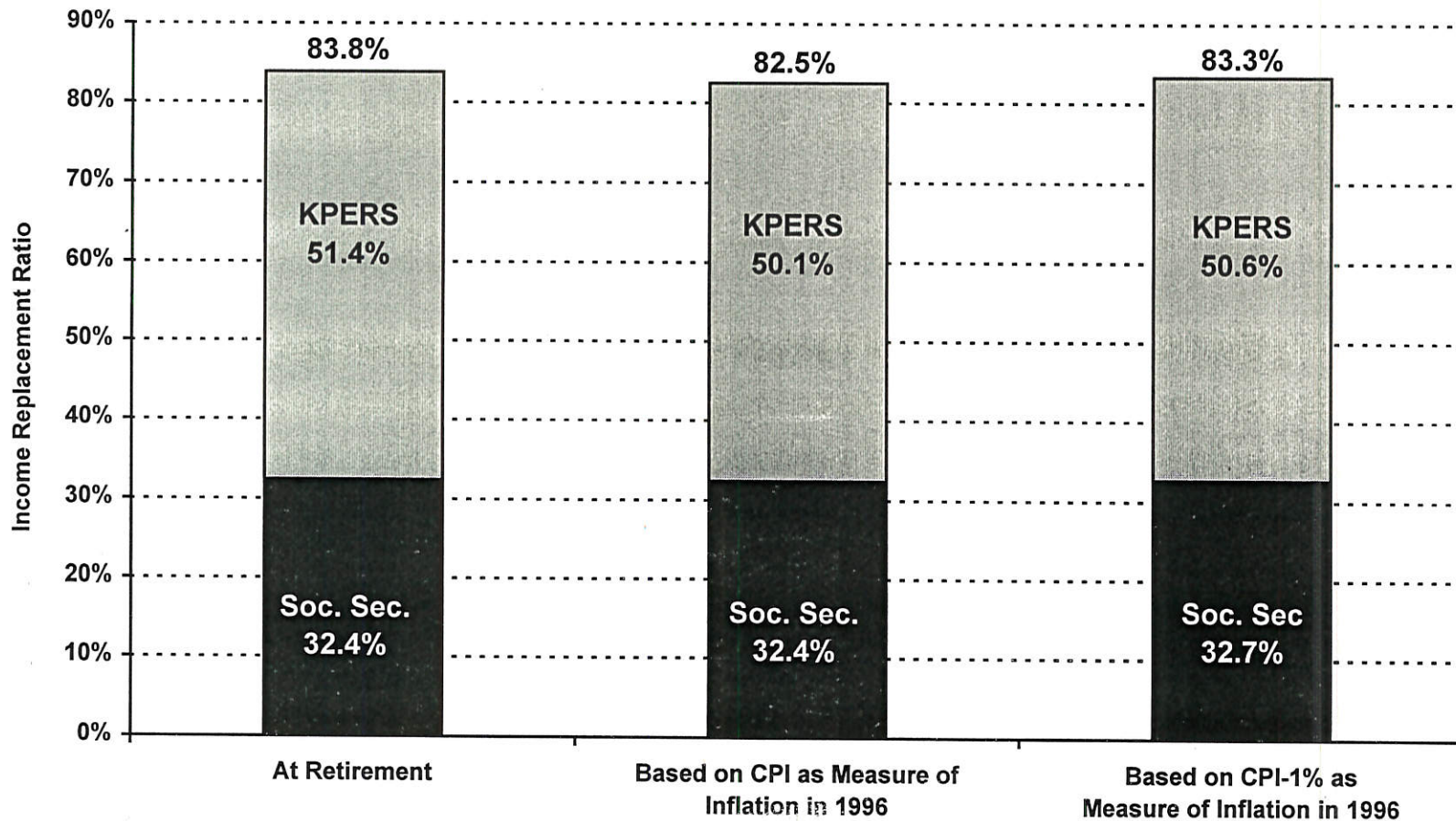
CAREER KPERS EMPLOYEE RETIRING IN 1988 MEASURE OF LOSS OF PURCHASING POWER

1-21



CAREER KPERS EMPLOYEE RETIRING IN 1995 MEASURE OF LOSS OF PURCHASING POWER

1-22



CONCLUSIONS FOR CURRENTLY RETIRED KPERS MEMBER WHO RETIRED WITH LESSER BENEFITS

1-23

- **Career employees retiring in the past were not likely to retire at income replacement amounts equal to 70% target**
- **However, purchasing power has been maintained based on CPI as inflation measure, and enhanced based on CPI-1%**
- **More immediate need for continuing Post-Retirement increases, but no significant short-fall currently**

POST-RETIREMENT BENEFITS FINANCING ALTERNATIVES

1-24

Pay-As-You-Go



From Favorable Experience



Appropriations



Advance Funding

FAVORABLE EXPERIENCE EXAMPLES

1-25

- **All or Shared Gains**
(e.g. - 50% of investment gains in excess of actuarially assumed investment return or some higher rate)

- **Interest Dividend**
(e.g. - investment return in excess of actuarial basis for annuity)

ESTIMATED COST OF ONE-TIME INCREASE ONLY (STATE AND SCHOOL ONLY)

1-26

Increase Benefits for Retired Members By	Increase in Unfunded Benefits	Increase in Contribution Rate*
4%	\$88M	.30% of Pay
3%	66M	.22% of Pay
2%	44M	.14% of Pay
1%	22M	.07% of Pay

Note: Investment gain based on actuarial value of assets was \$280M for 1996 fiscal-year.

***Funded over 15 years**

LONG-TERM COST OF POST-RETIREMENT INCREASES

L-27-1

All Members	Estimated Increase in Contributions as % of Pay*
4% Annual Compound Increase	5.9%
3% Annual Compound Increase	4.2
2% Annual Compound Increase	2.6
1% Annual Compound Increase	1.2
Currently Retired Members Only	Increase in Contributions as % of Pay*
4% Annual Increase	2.3%
3% Annual Increase	1.6
2% Annual Increase	1.0
1% Annual Increase	.5

* Additional Unfunded Liabilities for retired employees funded over 15 years; for active employees over KPERS funding period policy

EMPLOYEE FINANCED POST-RETIREMENT BENEFITS:

82-1

To Receive a Benefit With an Annual Compound Increase of	Employee Could Reduce Initial Pension Amount By:
1%	8.0%
2%	17.2
3%	27.6

Note: A 22% reduction in the KPERS benefit would meet the 70% income replacement target.

PRELIMINARY FINDINGS

1-29

- **CPI probably overstates inflation for retirees by at least 1% per year**
- **KPERS career employees retiring at current benefit levels:**
 - ♦ **Exceed initial income replacement needs**
 - ♦ **Can self-finance some Post-Retirement inflation protection**
 - ♦ **Additional inflation protection required is deferred or modest if moderate inflation occurs**
- **Past Post-Retirement practices have been generous and have maintained purchasing power of KPERS retirement benefits. However, the initial income replacement levels were significantly less than current amounts**
- **It is unlikely that past practices can be maintained without significant increases in contribution requirements, or exceptional investment return, or delay in meeting actuarially required contributions**

SAMPLE POST-RETIREMENT BENEFIT INCREASE POLICY STATEMENTS

1-30

- **Post-Retirement benefit increases are intended to help maintain purchasing power, not to solve inadequate benefits at retirement or correct past wage levels**
- **The need for Post-Retirement KPERS benefit increases will consider:**
 - ♦ **The cost-of-living as measured by the CPI-1%**
 - ♦ **Benefits from both KPERS and Social Security for career employees retiring at age 62 with 30 years of service**
 - ♦ **A 70% income replacement target from Social Security and KPERS for an average retiree**
- **All periodic benefits will be considered for Post-Retirement increases**
- **Employees who retired at benefit levels less than current KPERS benefit levels have a greater need**

SAMPLE POST-RETIREMENT BENEFIT INCREASE POLICY STATEMENTS (CONTINUED)

1-31

- **Financing for any Post-Retirement increases will not jeopardize or delay the equilibrium point for meeting the actuarially required contributions**
- **Until the actuarially required contribution is met, actuarial or investment gains should be used to shorten the period until equilibrium, not to improve benefits.**
- **Pre-funding of Post-Retirement increases is a preferred approach to any funding method that shares favorable experience (e.g. Diet COLA) to achieve fairness for both employees and taxpayers**
- **The long-term costs, affordability and likelihood of Post-Retirement increases will be communicated to employees so that they can adequately plan for their retirement**
- **The strategy will be dynamic and react to changes in KPERS benefits, Social Security, and measures of inflation**

SAMPLE POST-RETIREMENT BENEFIT INCREASE POLICY STATEMENTS (CONTINUED)

1-32

- All proposals for Post-Retirement increases will disclose:
 - ◆ Increase in Unfunded Liabilities
 - ◆ Long-term costs if proposal is continued annually
 - ◆ Delay in meeting equilibrium point

- Targeted annual Post-Retirement increases to meet the above objectives are:
 - ◆ For employees who retire at current KPERS benefit levels
 - If CPI-1% is 3% or more: 1%
 - If CPI-1% is less than 3%: 0

 - ◆ For other retirees
 - If CPI-1% is 3% or more: 2%
 - If CPI-1% is 2%: 1%
 - If CPI-1% is less than 2%: 0