Approved: 1/23/97
Date

MINUTES OF THE SENATE COMMITTEE ON ELECTIONS AND LOCAL GOVERNMENT.

The meeting was called to order by Chairperson Janice Hardenburger at 1:30 p.m. on January 16, 1995 in Room 529-S of the Capitol.

All members were present except: Senator Ben Vidricksen, excused
Senator Marge Petty, excused

Committee staff present: Dennis Hodgins, Legislative Research Department
Mike Heim, Legislative Research Department
Theresa Kiernan, Revisor of Statutes
Bonnie Fritts, Committee Secretary

Conferees appearing before the committee: William F. Caton, Pres., Kansas Development Finance Authority
Allan Foster, Senior Auditor, Legislative Division of Post Audit
Meredith Williams, Kansas Public Employees Retirement System

Others attending: See attached list

Chairperson Hardenburger asked for introduction of bills.

Bill Caton asked for introduction of a bill that seeks to amend K.S.A. 74-8903 (b) which provides for the composition of the KDFA's board of directors. It would eliminate the provision that the secretary of the department of commerce and housing serve on the board and addresses the political make-up of the board.

Senator Praeger moved to introduce the bill as recommended. Senator Lawrence seconded the motion. The motion carried.

Allan Foster appeared before the committee to explain a performance audit report by the Legislative Division of Post Audit reviewing benefits provided by the Kansas Public Employees Retirement System (KPERS) (Attachment 1). He gave an overview of the system and explained how benefits are calculated. He said KPERS provides an average benefit at a low price. This report provides data on how KPERS compares to other public and private pension systems with respect to contributions, vesting provisions, and benefit levels, and how Kansas can provide more flexibility and options for State employees to invest their retirement moneys. There is also a table detailing retirement benefits offered by a sample of other state retirement plans taken from a survey of state retirement systems conducted by the Government Finance Officers Association. The report concluded by stating it is clear that defined-benefit retirement plans aren't as beneficial to short-term employees as they are to long-term employees and mentions several ways to increase portability or flexibility for State employees such as, allowing employees to take employer contributions with them when they change jobs. This would likely increase the employer contribution rate needed to fund the system in the future. Likewise, having a shorter vesting period would increase the number of employees who are eligible for retirement, thus increasing the costs of the System.

Meredith Williams testified that KPERS is, has been, and continues to be a low cost issuer of employee benefits. He also said that 1996 was the first ever "billion dollar" year, where after all fees and expenses, investment activities totaled 1.095 billion dollars. The retirement system has a long tradition of consistent prudent and reasonable actuarial assumptions. Mr. Williams reported that there are currently 206,000 members in the retirement system, 48,000 of which are receiving monthly benefits, the remainder are working and contributing to the system. He said KPERS is a typical, public sector benefit plan, designed from the inception, to serve the needs of the "career" public servant as opposed to the "job hopping" public servant. He concluded by saying about $385 million will be paid in benefits this year. About 85% of their members continue to reside in Kansas so KPERS economic impact is about $327.5 million.

The meeting was adjourned at 2:30 p.m.

The next meeting is scheduled for January 21, 1997.

SENATE ELECTIONS AND LOCAL GOVERNMENT
COMMITTEE GUEST LIST

DATE: 1/16/97

NAME	REPRESENTING
Allan Foster	Legislative Post Audit
Bill Caton	KDFA
Rebecca Floyd	KDFA
Meredith Williams	KPERS
Jack Hawn	"
Anne Spiess	Peterson Public Affairs Group

LEGISLATURE OF KANSAS
LEGISLATIVE DIVISION OF POST AUDIT

MERCANTILE BANK TOWER
800 SOUTHWEST JACKSON STREET, SUITE 1200
TOPEKA, KANSAS 66612-2212
TELEPHONE (913) 296-3792
FAX (913) 296-4482

October 24, 1996

To: Members, Legislative Post Audit Committee

Senator Lana Oleen, Chair
Senator Anthony Hensley
Senator Phil Martin
Senator Alicia Salisbury
Senator Don Steffes

Representative Jim Lowther, Vice Chair
Representative Tom Bradley
Representative Duane Goossen
Representative Sheila Hochhauser
Representative Ed McKechnie

This report contains the findings and conclusions from our completed performance audit, *Reviewing Benefits Provided by the Kansas Public Employees Retirement System: A K-GOAL Audit.* The report also contains an appendix showing comparative information on the retirement plans and benefits provided by Kansas and most of the other states.

We would be happy to discuss the findings presented in this report with any legislative committees, individual legislators, or other State officials.

Barbara J. Hinton

Barbara J. Hinton
Legislative Post Auditor

SENATE ELECTIONS +
LOCAL GOVERNMENT
1-16-97
ATTACHMENT 1

EXECUTIVE SUMMARY

LEGISLATIVE DIVISION OF POST AUDIT

Question 1: How Does The Kansas Public Employees Retirement System Compare To Other Public And Private Pension Systems With Respect To Contributions, Vesting Provisions, and Benefit Levels?

The Retirement System's cash benefits generally compared favorably with other states, but health insurance and cost-of-living provisions were somewhat less generous than many other states provide. *The Retirement System pays an annual retirement benefit of $15,750 to an employee who worked 30 years and had a final average salary of $30,000. This benefit ranked 20th of the 37 states we reviewed for this measure, and was slightly below the average of $16,197. Paid health insurance and cost-of-living increases can enhance retirement benefits greatly. Thirteen states, including Kansas, pay all or part of the cost of retirees' health insurance premiums. Of those states, Kansas provided the smallest subsidy—15%. Four states provide health insurance at no cost to retirees. Nearly two-thirds of the states we reviewed gave automatic annual cost-of-living increases. Kansas was one of nine states that granted occasional increases. Kansas' vesting period is 10 years, while many other states allow their employees to become vested in five years or less. The Retirement System generally offered the same types of non-cash benefits other systems offered.* .... page 5

Employee contribution rates in Kansas were about average, and employer contribution rates were among the lowest of the states we reviewed. *State employees generally pay for a portion of their retirement benefits during the years they work by contributing a certain percentage of their salaries. In Kansas, employees contribute 4% of their salaries, which was about average. Employee contributions in other states ranged from 0% to 8.7% of salary. Kansas' employer contribution rate was the second lowest of all the states we reviewed. In fiscal year 1994, Kansas contributed 3.1% of employee salaries to fund the retirement system. Retirement System officials point to good investment performance as the main reason for Kansas' low rate. The contribution rate also is held artificially low to some extent because of a law passed in 1993, which spreads out employer contribution increases needed to fund benefit increases given that year.* .... page 8

The Retirement System wasn't as well funded as many of the other state retirement systems we reviewed. *How well-funded a retirement system is has to do with the assets it has available to invest so that it can pay retirement benefits to employees who are currently retired, or who will retire in the future. If a retirement system is 100% funded, that means that it has enough assets to cover all its current and future liabilities for retirement benefits. Our comparisons showed that for fiscal year 1994, the Retirement System was about 78% funded, compared with an average of about 88% for the other systems we reviewed. Officials from the Government Finance Officers Association told us the Retirement System's funding level shouldn't be of particular concern as long as the* ....page 9

employer contributions are actuarially determined and the Legislature appropriates enough money to make those contributions. Kansas is doing both those things.

Private pension systems may provide greater benefits than public systems. *There are two major types of retirement plans, defined-benefit plans, and defined-contribution plans. Defined-benefit plans offer a set retirement benefit based on years of service and final average salary. (Nearly all state retirement plans are defined-benefit plans.) Defined-contribution plans don't offer a set retirement benefit. The employer, and sometimes the employee, put money into an account for the employee, and the employee controls how the money is invested. The final benefit amount depends on how well those investments perform. Large private employers generally offer employees combined defined-benefit and defined-contribution plans. We gathered information from four large Kansas corporations—Blue Cross Blue Shield of Kansas, Goodyear Tire and Rubber Company, Security Benefit Life, and Cessna Aircraft Company. We found that each company provides both a defined-benefit plan and a defined-contribution plan for their employees. Two companies offer better defined-benefit plans than the State does. They also provide this benefit at no cost to the employee. All the companies also provide a defined-contribution plan with an employer match. It's difficult to estimate a benefit that would result from these defined-contribution plans. However, they are benefits the State doesn't offer.* ....page 11

Question 2: How Can Kansas Provide More Flexibility and Options For State Employees To Invest Their Retirement Moneys?

Defined-Benefit retirement plans, like the Retirement System's, lack portability and tend to penalize workers who change jobs. *Defined-benefit plans generally don't allow workers to take any of the employer contributions with them when they change jobs. This has become an important problem given todays less stable job market. When vested employees change jobs, they can leave their money in their retirement plans and receive a retirement benefit from each employer when they reach retirement age. However, they end up with a lower total annual retirement benefit than employees with similar salary histories who work for one employer their entire career. In contrast, defined-contribution plans—the other major type of retirement plan—generally are very portable. These plans usually allow employees to take some or all of the employer contributions with them, and benefits aren't affected by how often employees change jobs. In addition, they allow employees to choose how their retirement money is invested. The main disadvantages of these plans are that they shift the investment risk to the employee, they require employees to have investment knowledge, and they won't necessarily provide a larger benefit at retirement.* ....page 13

A few states have taken steps to make it easier for employees to take their retirement benefits with them when they change jobs, or to have more control over investment decisions. *Colorado and South Dakota have adopted retirement plans that give employees some of the employer contributions when they change jobs. For example, Colorado lets employees take the contributions they made plus interest, and then matches 50% of that amount with state money. Nebraska offers a non-* ....page 16

1-3

traditional defined-contribution plan that lets employees invest their retirement funds, but doesn't let them take employer contributions with them if they leave. Washington offers a combined defined-benefit and defined-contribution plan that provides employees with a retirement benefit even if they change jobs and withdraw their employee contributions. Four states have added features to their defined-benefit retirement plans that give employees more flexibility in how their final retirement benefits are determined. Many states, including Kansas, provide a portable defined-contribution plan for unclassified university employees. All of these alternatives have some actual or potential costs to the State or the employee.

Although defined-contribution plans can create more portability and investment choices for employees, these plans don't necessarily guarantee a larger retirement benefit. *Two scenarios we constructed to compare defined-contribution plans with defined-benefit plans showed that the portability of the defined-contribution plans may come at the cost of lower retirement benefits. One scenario that kept employer and employee contribution rates about the same as they are now failed to provide a retirement benefit as good as the current defined-benefit plan, even for the employees who changed jobs. It's only when contribution rates are increased substantially that the defined-contribution plan begins to provide a better benefit than the current defined-benefit plan.* .... page 19

Conclusion............... page 20

APPENDIX A: *Benefits Offered By a Sample of State Retirement Systems*............... page 21

APPENDIX B: *Estimates of the Annual Benefits Resulting From Two Defined-Contribution Retirement Plans*............... page 25

APPENDIX C: *Agency Response*............... page 29

This audit was conducted by Allan Foster. If you need any additional information about the audit's findings, please contact Mr. Foster at **the Division's offices. Our address is: Legislative Division of Post Audit, 800 SW Jackson Street, Suite 1200, Topeka, Kansas 66612.** You also may call (913) 296-3792, or contact us via the Internet at **LPA@postaudit.ksleg.state.ks.us.**

Reviewing Benefits Provided by the Kansas Public Employees Retirement System: A K-GOAL Audit

The Kansas Public Employees Retirement System (KPERS) provides retirement, disability, and survivor benefits for Kansas public employees and their beneficiaries. Legislative questions have been raised recently about the benefits provided by the Retirement System. Specific questions focus on how Kansas' retirement options compare with those of other employers, and whether Kansas needs to provide more flexibility in its retirement program, or more options to allow employees to maximize the amounts earned on their retirement funds.

The Kansas Governmental Operations Accountability Law (K-GOAL) requires Legislative Post Audit to conduct a performance audit of specified State agencies each year for the next several years. The purpose of these audits is to periodically review the operations of the selected agencies, determine the necessity, propriety, and legality of their operations, identify areas of inefficiency and ineffectiveness, and provide information to allow the Legislature to take action to retain appropriate and effective governmental operations, or to terminate inappropriate or obsolete governmental operations.

This audit addresses the following questions:

1. **How does the Kansas Public Employees Retirement System compare to other public and private pension systems with respect to contributions, vesting provisions, and benefit levels?**

2. **How can Kansas provide more flexibility and options for State employees to invest their retirement moneys?**

To answer these questions, we interviewed Retirement System officials and reviewed documentation about State employees' retirement benefits. For comparison purposes, we obtained a database of 1994 information on other states' retirement systems from the Government Finance Officers Association. We updated that information for 15 states by obtaining current information from those states. We also obtained comparative information about private companies' retirement benefits from four large private employers in Kansas. To obtain information about ways to provide more flexibility and portability of pension benefits, we interviewed officials of the Government Finance Officers Association and the National Conference of State Legislatures. We also reviewed relevant research and other states' retirement plans. In conducting this audit, we followed all applicable government auditing standards set forth by the U.S. General Accounting Office.

In general, we found that the Retirement System pays a retirement benefit that is about average compared to other state systems we examined. The employee contribution rate is also about average. Kansas is less generous in granting cost of living increases and in subsidizing health insurance than many of the other states. It also has the longest vesting period of the states we reviewed. At the same time, Kansas has the second lowest employer contribution rate among those states. Retirement System officials attribute the low rate to the System's good investment performance.

1-5

The Retirement System has as comparatively large unfunded liability, but it appears that the Legislature is handling it reasonably.

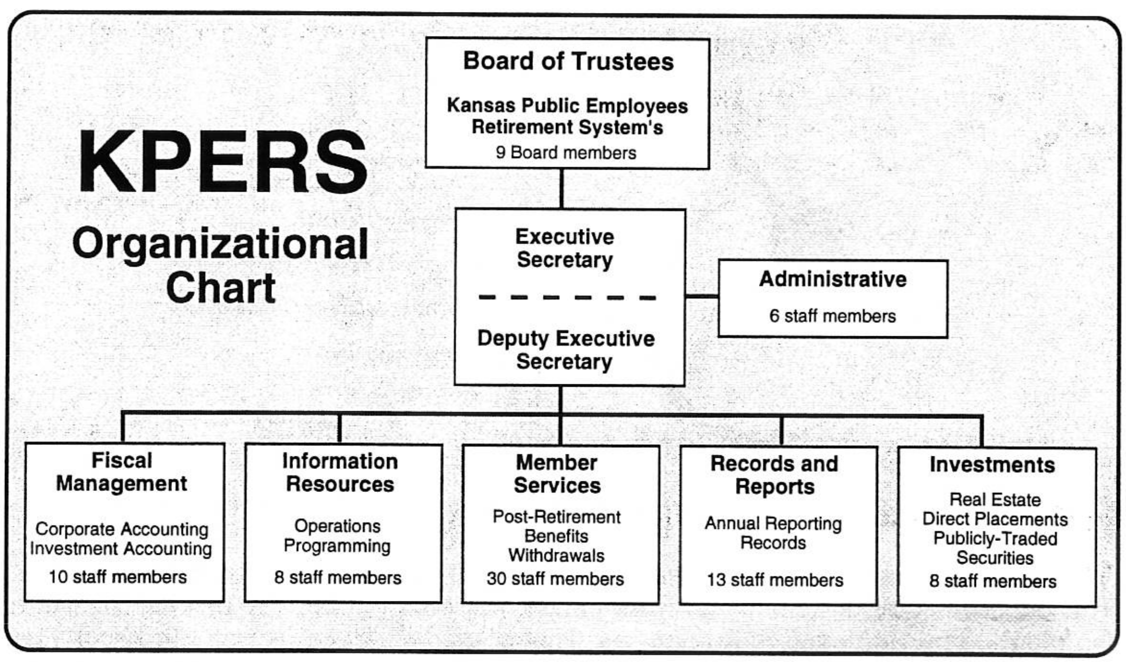
Defined-benefit retirement plans like the Retirement System generally aren't portable and tend to penalize workers who change jobs. A few states have begun to make it easier for employees to take retirement moneys with them when they change employers. They have done this by using a combination of defined-benefit and defined-contribution plans, or by allowing employees to take all or a portion of the employer contributions when they leave state employment. Some states also are giving employees options for how their retirement moneys can be invested, and providing alternative methods for computing retirement benefits that can be to the employee's advantage. Kansas also could increase flexibility by building aspects of defined-contribution retirement plans into its current plan. However, most alternatives have potential costs to the State or to employees. These and other findings are discussed more fully following a brief overview of the Retirement System.

Overview of the Kansas Public Employees Retirement System

The Kansas Public Employees Retirement System was established in 1961 to provide a systematic retirement plan for public employees in Kansas. In addition to the retirement plan, the System provides group life and disability insurance coverage for its members.

The Retirement System is actually an umbrella organization made up of three separate membership groups—the Kansas Public Employees Retirement System, the Kansas Police and Firemen's Retirement System, and the Retirement System for Judges. The System covers most state and local government employees in Kansas. On June 30, 1996, the System had 155,822 members (active and inactive), 46,746 retirees, and 1,344 participating employers.

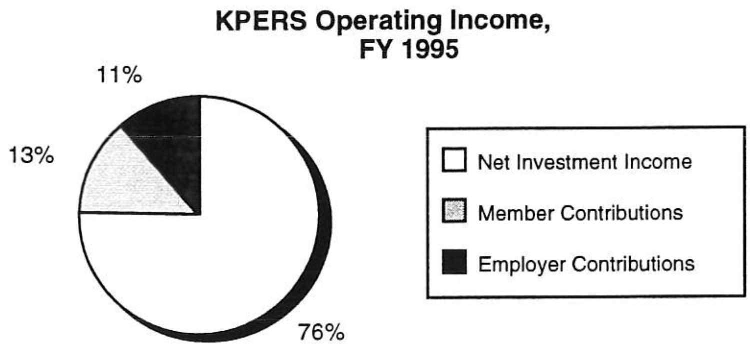
On July 1, 1993, a new Board of Trustees was established in accordance with K.S.A. 74-4905. Four members of the nine-member Board of Trustees are appointed by the Governor subject to confirmation by the Senate, and two are appointed by legislative leadership. Two members of the Board are elected by members and retirees of the System—one school member and one non-school member. The State Treasurer is an ex officio member of the Board. The Board appoints an Executive Secretary to manage the daily operations of the System. In fiscal year 1996, the System employed approximately 77 full-time staff members. An organizational chart of the Retirement System's structure is presented below.

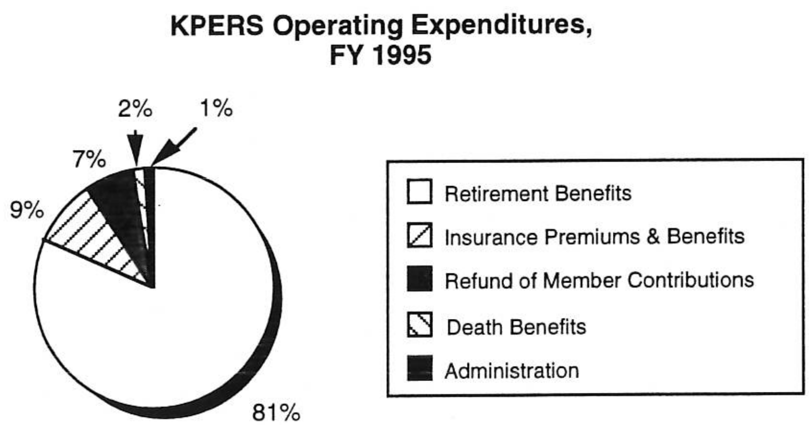


The retirement plans the Retirement System administers are defined-benefit plans. Under a defined-benefit plan, benefit levels are pre-determined and the employer contribution rates are periodically adjusted based on retirement system earnings to make sure enough money will be available to pay those benefits.

The System's administrative expenses, including employees' salaries and wages, are paid from earnings on investments. In fiscal year 1995, the Retirement System's total expenditures were about \$355 million. Almost \$334 million of that amount was for benefit payments, and about \$17 million was spent on investment costs. In that year, the Retirement System had 76 employees and spent about \$4 million on operating costs.

The following charts show the relative sources and uses of operating funds for fiscal year 1995.





As the chart shows, most income for benefits comes from investment income. The member contributions come from employees contributing 4% of their salary to the plan. The employer contributes an amount that varies each year. In fiscal year 1996, the State contribution was 3.3% of employee salaries. Nearly all of operating expenditures are for benefits.

1-8

How Does The Kansas Public Employees Retirement System Compare To Other Public and Private Pension Systems With Respect To Contributions, Vesting Provisions, and Benefit Levels?

In a number of areas, Kansas' Retirement System compared favorably to the other state systems we examined. Kansas' retirement benefit and 4% employee contribution rate are about average, and Kansas also offers many of the same benefits other states do—such as disability and group life insurance, and death benefits. Kansas' Retirement System compared less favorably in a few areas. Most states provide automatic cost-of-living increases to retirees, while Kansas provides only occasional increases at the Legislature's discretion. In all, 12 states provide free or highly subsidized health insurance to retirees, while Kansas subsidizes rates by only 15%. Finally, Kansas' vesting period is 10 years, while many other states allow their employees to become vested in five years or less.

The cost of Kansas' employee retirement benefits is very low. Its employer contribution rates of 3.1% in fiscal year 1994 was the second lowest of the other states. Retirement System officials told us this rate is low because of the System's good investment performance. The contribution rate is held artificially low to some extent because of a law passed in 1993. The Retirement System has a somewhat larger unfunded liability than most other State systems, but it appears that the Legislature is handling it reasonably. These and related findings are discussed in more detail in the sections that follow.

The Retirement System's Cash Benefits Generally Compared Favorably With Other States, but Health Insurance and Cost-of-Living Provisions Were Somewhat Less Generous Than Many Other States Provide

To compare the Retirement System's benefits to other retirement plans, we obtained a database of information from the Government Finance Officers Association. That database contains information from a survey of state and local government retirement systems conducted by the Association. The data in the most recent survey contains information from fiscal year 1994. We contacted 15 of the states to verify the accuracy of the information contained in the database, and to gather more current information. In addition, we contacted four large private-sector employers in Kansas—Blue Cross and Blue Shield, Cessna, Goodyear, and Security Benefit Group.

In making our comparisons we eliminated plans covering judges, police and fire, and school employees. We did this partly because there aren't comparable programs in the private sector, and partly to limit the number of comparisons. We also eliminated states that don't participate in Social Security, because they generally offer higher benefits and provide higher employer contributions to compensate for the lack of Social Security benefits. In all, we compared the Retirement System with 38 other state retirement plans and four private-sector plans. Appendix A contains complete data for each of the state plans we reviewed.

The Retirement System's cash benefits ranked just below average compared with other states. The following table shows the annual cash retirement benefits paid for two workers with a final average salary of $30,000—one who worked for 20 years, and one who worked for 30 years. The table compares Kansas' benefits to the high, low, and average benefits paid by other states' retirement systems. (Rankings in all tables are high to low. The number of plans in the rankings varies because some states didn't answer all questions.)

Annual Benefit for Employee With $30,000 Final Average Salary

Years Of Service	Other States High	Other States Low	Other States Average	KPERS	KPERS' Ranking
30	$24,000	$10,200	$16,197	$15,750	20th of 37
20	$18,000	$6,300	$10,676	$10,500	17th of 34

Another way to express the cash benefit is as a percent of final average salary. This percentage varies with the number of years of service. The following table shows the percent of final average salary paid by the Retirement System and other states for an employee who worked for 30 years. The profile box on the facing page shows the 30 year annual benefit for all the states in our sample.

Annual Retirement Benefit as Percent of Final Average Salary For 30 Years of Service

Other States High	Other States Low	Other States Average	KPERS	KPERS' Ranking
80%	34%	54.7%	52.5%	20th of 37

As these tables show, KPERS' cash benefit is slightly below the average of the other states. New Mexico paid the highest percentage of salary, and Illinois paid the lowest.

Factoring-in the paid health insurance premiums provided by some other state retirement systems didn't significantly change how Kansas' benefits ranked. Paid health insurance premiums must be considered in determining how a retirement system ranks in terms of retirement benefits provided.

Although paid health insurance is a non-cash benefit, it significantly reduces a retiree's living expenses. For example, one retirement system may provide a retiree with a monthly cash benefit of $800, but provide no health insurance. A second system may provide only $700 a month, but may fully pay its retirees' health insurance premiums. If cash benefits alone are considered, it appears the first system has the better benefits. But if the value of the health insurance premium paid by the second system is $200 a month, it's clear the second system offers the better value.

We found that 31 states made health insurance available to retirees at the State's group rates, but only 13—including Kansas—paid all or part of the cost of the retiree's premium, as follows:

- 4 states paid the entire premium
- 8 states paid premium amounts ranging from 45% to 95% of the cost
- Kansas subsidizes the medical portion of health insurance rates for State retirees by 15%. (Health insurance in Kansas costs a State retiree an average of about $2,900.) However, officials with the State Health Care Commission told us the Commission expects to gradually phase-out this subsidy.

When we made adjustments to retirement cash benefits to reflect the amount paid for health insurance premiums and reranked the states, it made little difference in the overall results. Kansas ranked 21st, and was still somewhat below average. The average benefit adjusted for health care was $16,835, and the Kansas adjusted benefit was $16,184.

Kansas gives cost-of-living increases less often than many states. Another issue that can affect how well off a system's retirees are is cost-of-living increases. For example, two retirement systems may provide identical benefits at the retirement date, but if one system provides annual cost-of-living adjustments and the other doesn't, within a few years, the retiree from the first system will be substantially better off than the retiree from the system that provides no cost-of-living increases.

Nearly two-thirds of the 39 states we reviewed had provisions for automatic cost-of-living adjustments for their retirees. That information breaks down as follows:

Annual Retirement Benefit For Employees With 30 Years of Service And $30,000 Final Average Salary

Rank	State	Annual Benefit
1	New Mexico	$24,000
2	Alaska	20,250
3	Rhode Island	19,800
4	Iowa	19,500
5	Alabama	18,114
6	Texas	18,000
7	Washington	18,000
8	Wyoming	18,000
9	Utah	18,000
10	Oklahoma	18,000
11	Pennsylvania	18,000
12	Hawaii	18,000
13	Arizona	18,000
14	Kentucky	17,700
15	Idaho	17,253
16	Mississippi	17,064
17	South Carolina	16,380
18	Montana	16,071
19	New York	15,960
20	**Kansas**	**15,750**
21	North Dakota	15,660
22	Oregon	15,030
23	New Jersey	15,000
24	Delaware	15,000
25	New Hampshire	15,000
26	Virginia	14,850
27	Georgia	14,700
28	Tennessee	14,458
29	Wisconsin	14,400
30	Missouri	14,400
31	Florida	14,400
32	Arkansas	13,950
33	Michigan	13,500
34	Minnesota	13,500
35	South Dakota	12,150
36	California	11,250
37	Illinois	$10,200

Of the states we reviewed, Kansas ranked 20th of the 37 states. Kansas' ranking is just below the median. An annual benefit can't be calculated for Nebraska because it has a defined-contribution plan which promises no particular benefit.

- 24 states had automatic cost-of-living increases every year
- nine states—including Kansas—provided occasional increases
- two states didn't offer any cost-of-living increases
- four states didn't provide this information

The Retirement System generally offered the same types of non-cash benefits other systems offered. Most of the systems we reviewed offered a variety of additional benefits, such as disability insurance, group life insurance, and death benefits. We didn't compare these benefits because of the complexity and wide variety of the different types of plans.

Employee Contribution Rates in Kansas Were About Average, And Employer Contribution Rates Were Among the Lowest Of the States We Reviewed

State employees generally pay for a portion of their retirement benefits during the years they work through a mandatory contribution of a certain percentage of their salaries. The table below shows the ranges of employee contribution rates among the states we reviewed for fiscal year 1994.

Employee Contribution Rates

Other States				KPERS'
High	Low	Average	KPERS	Ranking
8.7%	0.0%	3.9%	4.0%	22nd of 37

As the table shows, the percentage of salaries employees from different states are required to contribute varies widely. In eight states, employees don't have to contribute anything toward their retirement. Most of these states pay lower annual retirement benefits than states that require employee contributions. However, because they don't have to contribute toward their defined-benefit plan employees have more income to invest on their own for retirement in deferred compensation plans or IRAs.

Kansas employees must contribute 4% of their salaries, which the table shows is slightly above average. If only those states requiring employee contributions are included in the calculations, the average raises to 5.1%. By this measure, Kansas employees' contribution rate is lower.

Kansas' employer contribution rate was among the lowest of the states we reviewed. In fiscal year 1994, Kansas contributed 3.1% of employee salaries to fund the retirement system—a very low rate compared with other states. The table below shows the range of employer contribution rates for the states we compared.

Employer Contribution Rates

Other States				KPERS'
High	Low	Average	KPERS	Ranking
17.7%	0.7% (a)	8.5%	3.1	34th of 37

(a) New York had the lowest contribution rate in 1994. Between 1990 and 1995 they were under court order to keep their rates near 0% because the system had built up a surplus of funds. Their rates began increasing in 1996.

As the table shows, the average employer contribution rate of 8.5% was more than double the rate Kansas paid. More discussion about why employer contribution

1-12

rates in Kansas are low is contained in the following section about the Retirement System's funding.

The Retirement System Wasn't as Well Funded as Many of the Other State Retirement Systems We Reviewed

How well-funded a retirement system is has to do with the assets it has available to invest so that it can pay retirement benefits to employees who are currently retired, or who will retire in the future. If a retirement system is 100% funded, that means that its assets meet the present value of all its current and future liabilities for retirement benefits. If a system is only 75% funded its assets meet 75% of its liabilities. Some systems are more than 100% funded. That means that the system has more than enough assets to cover its current and future liabilities. In systems that are far greater than 100% funded, the system generally lowers the employer contribution rate until the system's assets decline and come more in line with liabilities.

Our comparisons showed that for fiscal year 1994 (the most recent year for which comparative information was available), Kansas' Retirement System was about 78% funded, compared with an average of about 88% for the other systems we reviewed. Since 1994, the System's level of funding has increased to about 81%.

Percent that Retirement Systems' Current and Future Retirement Benefits Are Funded

Other States			KPERS	KPERS'
High	Low	Average		Ranking
249.3%	53.8%	87.8% (a)	78.2%	29th of 36

(a) This average excludes the state shown as the highest. That state was excluded because it was so far out of the range of the other states. The next highest state had a funding rate of 111%.

The Retirement System's lower level of funding can be attributed in part to the relatively low employer contribution rate in Kansas The assets a retirement system has to fund benefit payments owed to current and future retirees is a function of the employer contribution rate, the employee contribution rate, and the investment performance of the retirement system. Of these three factors, Kansas' employer contribution rate was the only one that appeared to be significantly lower than in other states. As noted above, for fiscal year 1994 Kansas' employer contribution rate was only 3.1%, compared with an average of 8.5% for the other state retirement systems.

Retirement System officials point to good investment performance as the main reason the employer contribution rate in Kansas is low. In addition, officials said that the State has funded the System consistently, allowing the size of the investment portfolio to grow.

Actions taken by the 1993 Legislature affected the Retirement System's unfunded liability. Before 1993, the Retirement System had been about 88% funded, or about average compared to other state systems. That year, the Legislature increased retirement benefits and spread out contribution increases needed to fund those benefits over future years. It set the employer contribution rate at a level lower than the actuary said would be needed to fully fund the increase in benefits, and also passed legislation limiting increases in the employer contribution rate to .2% a year.

For fiscal year 1997, Kansas' employer contribution rate is set at 3.59% compared with the 5.17% the system's actuary determined should be contributed. Assuming the State continues increasing the contribution rate .2% a year, it's estimated the System will be fully funded by the year 2033. However, if the State doesn't continue increasing the rate, the unfunded liability will grow rapidly.

Estimates of the System's level of funding also had to be adjusted when it changed actuaries in 1994. Based on the new actuary's calculations, the current and future retirement benefits the Retirement System needed to pay were much larger than the previous actuary estimated. These differences were caused by mistakes allegedly made by the previous actuary, by projections made at the start of the year not being met, and by changes in the computation methods used by the new and the old actuarial firms. Nonetheless, with the increase in its estimated liabilities, the System's funding level wasn't as good as was estimated by the previous actuary.

Officials from the Government Finance Officers Association told us the Retirement System's funding level shouldn't be of particular concern as long as the employer contributions are actuarially determined and the Legislature appropriates enough money to make those contributions. They told us many factors can cause increases in unfunded liabilities, such as increases in benefits and poor investment returns. Based on what they knew, they said the Retirement System's funding level didn't appear to be problematic. They told us the key factors were whether the contribution rates were based on sound actuarial determinations, and whether the employer had historically made the money available to make those contributions. Kansas is doing both of these things.

Compared With the Majority of Other States We Reviewed, Kansas Requires Its Employees To Be Members of the Retirement System a Relatively Long Time Before Becoming Vested

Vesting is the number of years employees must have been members of a retirement plan before they are eligible to receive a future retirement benefit. Federal law limits private-sector retirement systems to a maximum vesting period of five years, although companies can use seven year vesting if they phase-in vesting over that period. Public retirement systems aren't required to follow this federal law.

The following table shows the number of years the states in our sample required their employees to work before they became vested in their retirement plans.

Length of Time Before Employees Can Become Vested

Number of Years To Vesting	Number of States
< 5 Years	6
5 Years	17
8 Years	1
10 Years	12

As the table shows, most states vest employees in either five or 10 years. Kansas and 11 other states require a 10-year vesting period. This longer vesting period prevents shorter-term employees from receiving retirement benefits. This topic will be discussed further in question two.

The ages at which employees are allowed to retire with full benefits are so variable within and between states that they're very difficult to compare. The Retirement System allows employees to retire with full benefits at age 65, at age 62 with 10 years of service, or at any age when their combined age and years of service equal 85. Some states have a large number of specific combinations of age and years of service at which employees can retire. Ages for early retirement are equally variable. However, Kansas' requirements appear to be fairly typical.

Private Pension Systems May Provide Greater Benefits Than Public Systems

Large private employers generally offer employees combined defined-benefit and defined-contribution plans. Defined-benefit plans offer a set retirement benefit based on years of service and final average salary. Defined-contribution plans are based on specific levels of employer contributions. The employer, and sometimes the employee, put money into an account for the employee, and the employee controls how the money is invested. Defined-contribution plans don't offer any specific amount of retirement benefit.

Hewitt Associates, a large pension consulting firm, conducted a study of 1,034 private plans and found that employers often add defined-contribution plans to "sweeten" their retirement packages, and to limit the role of the defined-benefit plans. They report that about 80% of major employers offer both plans. In private retirement plans, employees generally don't contribute to their defined-benefit plans, but must contribute to the defined-contribution plans in order to receive matching employer contributions.

Research comparing private and public pension plans tends to show that <u>public</u> defined-benefit plans are more generous than large <u>private</u> employers' defined-benefit plans. However, this difference is more than made up by the additional retirement benefits provided by private employers' defined-contribution plans.

The Wyatt Company, another large pension system consulting firm, conducted a study comparing benefits from private and public pensions, <u>including</u> benefits from Social Security, defined-benefit plans, and defined-contribution plans. They estimated the following for an employee retiring at age 65 with 30 years of service, and a final average salary of $35,000:

- a public employee would receive a benefit equal to 71% of his or her salary
- a private employee would receive a benefit equal to 87% of his or her salary

To see how the Retirement System compares to large private employers, we gathered information from four large Kansas corporations—Blue Cross Blue Shield of Kansas, Goodyear Tire and Rubber Company, Security Benefit Life, and Cessna Aircraft Company.

Summary of Retirement Plans Of Selected Kansas Private Employers

	Blue Cross Blue Shield	Cessna	Goodyear	Security Benefit	KPERS
Defined-Benefit Plans					
Benefit for 30 yrs svs & $30,000 FAS	$18,000	$16,245 (a)	$13,320	$12,600	$15,750
Employee Contributions	0%	0%	0%	0%	4%
Defined-Contribution Plans					
Employee Contribution	Up to 15%	Up to 10%	Up to 16%	Up to 10%	NA
Employer Match	$.50 per $1 up to 10% of Salary	$.50 per $1 up to 5% of Salary	$.50 per $1 up to 6% of Salary	$.50 per $1 up to 6% of Salary	NA
Company Contribution In Stock or Cash?	Cash	Stock	Stock	Cash	NA
Profit Sharing	No	No	No	Yes	No

(a) Cessna employees hired after 1990 will have a benefit of $11,997

We found that each company provides both a defined-benefit plan and a defined-contribution plan for their employees. Cessna also provides a profit sharing plan. All the companies provide the defined-benefit plan free to their employees, meaning their employees don't contribute any of their own salaries to their plans. To receive any benefits from the defined-contribution plans, employees must make contributions to the plans first, then the companies match the employee contributions to a varying extent. The table above summarizes these companies' benefits.

As the table shows, two companies offer better defined-benefit plans than the State does. They also provide this benefit at no cost to the employee. All the companies also provide a defined-contribution plan with an employer match. It's difficult to estimate a benefit that would result from a defined-contribution plan because employee contributions aren't mandatory, employees can invest in several different types of funds, and investment returns vary widely. However, they are benefits the Retirement System doesn't offer.

How Can Kansas Provide More Flexibility and Options For State Employees to Invest Their Retirement Moneys?

Defined-Benefit retirement plans like the Retirement System's generally aren't portable and tend to penalize workers who change jobs. Although nearly all states still provide traditional defined-benefit plans for their employees, a few states have begun to make it easier for employees to take retirement moneys with them when they change jobs. Some states also are giving employees options for how their retirement moneys can be invested, and providing alternative methods for computing retirement benefits that can be to the employee's advantage. Large private employers commonly offer both defined-benefit plans and defined-contribution plans to their employees to give some of the benefits of each. Kansas also could increase flexibility by building aspects of defined contribution retirement plans into its current plan. However, most alternatives have potential costs to the State or to employees. These and related findings will be discussed in more detail in the sections that follow.

Defined-Benefit Retirement Plans Like the Retirement System's, Lack Portability and Tend to Penalize Workers Who Change Jobs

Generally speaking, there are two major types of retirement plans—defined-benefit plans, and defined-contribution plans. The Kansas Public Employees Retirement System is a defined benefit plan, which generally has the following characteristics:

- the retirement benefit is assured because it is fixed by a formula (years of service multiplied by final average salary multiplied by a percentage adopted by the employer)
- the employee contribution rate is a fixed percentage of the employee's salary
- the employer contribution rate is variable depending on how much is needed to fund the pre-determined retirement benefit, after the plan's investment earnings have been taken into account
- the employer bears the investment risk—employers pay more when investments don't perform well, and less when they do
- The plan isn't portable—if employees change jobs before retiring, they can't take their retirement benefits with them. Their options are either to leave the benefits with their employers until they reach retirement age and can begin withdrawing them, or to withdraw their contributions—plus interest—and invest that money *in their own retirement account.* The employee generally forfeits any moneys the employer has contributed to the retirement plan on his or her behalf.

In contrast, a defined-contribution retirement plan has the following characteristics:

- the retirement benefit amount isn't assured
- the employee contribution rate is fixed
- the employer contribution rate is a fixed percentage of the employee's salary

Advantages and Disadvantages of Defined-Contribution Plans and Defined-Benefit Plans

Advantages for Employees

Defined-Contribution Plans

- Investment Benefits - Employees can benefit from good investment performance
- Control over Investments - Employees can make choices about how their contributions are invested
- Portability of Benefits - When people change employers they can generally take the employer share of their account with them.
- Easier to Understand - These plans have no complicated benefit formulas

Defined-Benefit Plans

- Certainty of Benefit Amount - Employees have some certainty about the amount of the benefits that will be available at retirement. This allows better planning for retirement.
- Cost-Of-Living Adjustments Are Possible
- No Investment Risk - The employer promises a set benefit, and must pay it no matter what the investment performance is.
- Higher Benefits - Long-term employees generally get a better benefit than they do under most defined contribution plans

Advantages for Employers

Defined-Contribution Plans

- Ease of Administration - Costs are predictable. There is no actuarial calculations, and the cost of benefits are paid each pay period. There also is no possibility of an unfunded liability.
- No Investment Risk - Employees make their own investment decisions and bear all the risks.

Defined-Benefit Plans

- Costs Are Reduced When Employees Leave Before Retirement - Employer contributions and earnings are kept in the System when non-vested employees quit, or when vested employees withdraw their contributions.
- The State Benefits from Favorable Investment Returns - Investment returns reduce the amount the state must contribute.

Disadvantages for Employees

Defined-Contribution Plans

- Uncertain Retirement Benefits - The amount of the benefits that will be available at retirement is uncertain. This makes retirement planning difficult.
- The Employee Assumes Investment Risk - Benefits can be reduced because of poor investment performance. If the employee makes high risk investments and the stock market declines, he or she could loose much of their retirement money.
- Investment Knowledge is Required - Many employees lack investment knowledge and choose investments that are too conservative. Such employees may end up with an insufficient retirement benefit.
- No Cost-Of-Living Adjustments

Defined-Benefit Plans

- Benefits Aren't Portable. - When employees leave, they can't take the employer contributions with them, and the interest they receive on their contributions may be minimal.
- Penalties for Short-Term Employees - Switching employers results in lowered annual benefits upon retirement.
- No Control over Investments

Disadvantages for Employers

Defined-Contribution Plans

- Costs Aren't Reduced When Employees Leave Before Retirement - When employees withdraw their contributions they generally can take the employer's contribution with them.
- Contributions Aren't Reduced by Investment Returns - The employer has no investment portfolio, and can't use investment returns to reduce its financial burden.

Defined-Benefit Plans

- Employers Assume the Investment Risk - Employers have to pay a specific benefit, no matter what the investment income is.
- Contribution Rates Change Every Year - The employer's contribution changes from year to year to meet the funding needs of the System.
- Administration Is More Difficult - The system must do things such as manage the investment portfolio, make actuarial calculations, and distribute monthly benefits.
- Unfunded Liability Can Develop - Unfunded liabilities create funding obligations for future generations

- the employee bears the investment risk and makes his or her own investment decisions, which may produce a larger or smaller benefit at retirement depending on how the investments perform
- The plan is portable—if employees change jobs before retiring, they can take their retirement benefits with them, which generally consist of their contributions, the employer's contributions, and any interest earned. To aid in this, most defined-contribution plans have shorter vesting.

More information about the advantages and disadvantages of the two types of retirement plans can be found in the boxes on the facing page. An illustration of how a defined-contribution plan works can be found in Appendix B.

In the past, when employment patterns were different than they are today, both public and private retirement plans were almost all defined-benefit plans. Job markets tended to be stable, and it wasn't uncommon for a person to work for one employer his or her entire career. In more recent years, employees frequently are forced to find other jobs because of corporate or governmental downsizing. With a more transient job force, it has become increasingly important for workers to be able to take their pension benefits with them when changing jobs.

Besides lacking portability, defined-benefit plans tend to penalize employees who change jobs. This occurs even if they work for their employers long enough to become "vested" in each plan (eligible to receive a retirement benefit when they reach a certain age), and leave their moneys in those plans until they begin drawing them out at retirement. The accompanying table illustrates this point. This table shows the total retirement benefit for three employees who all had the same salary histories during their career. They all started out with a salary of $7,800 and ended with a final average salary of $30,000. However, each worked for a different number of employers.

Annual Retirement Benefits for Three Employees With Similar Salary Histories

Retirement Benefit From:	Employee A: 1 Employer for 30 Years (Vested)	Employee B: 3 Employers, 10 Years Each (Vested at Each)	Employee C: 5 Employers, 6 Years Each (Never Vested)
1st Employer	$15,750	$1,979	$0
2nd Employer	--	$3,223	$0
3rd Employer	--	$5,250	$0
4th Employer	--	--	$0
5th Employer	--	--	$0
Total At Retirement	$15,750	$11,696	$0 (a)

(a) If employee C withdrew his or her contributions from each employer when they left, and rolled it over into a tax-deferred account such as an IRA or a 401(k) plan, they would have enough money in the account to purchase an annual annuity of about $3,500. This assumes they received an average annual interest rate of 5% in their tax-deferred account during their career.

As the table shows, the retirement benefit for the employee who switched jobs every 10 years is only two-thirds of the benefit of the employee who stayed with the same employer, even though the employee worked the same number of years at the same salary.

Employees are further penalized when they don't work for each employer long enough to become vested in that employer's retirement plan. When this happens, the employee receives no retirement benefit, and generally forfeits any money the employer has contributed to the retirement plan on his or her behalf. Employee C in the table above illustrates this point.

A Few States Have Taken Steps to Make It Easier for Employees To Take Their Retirement Benefits With Them When They Change Jobs, Or to Have More Control Over Investment Decisions

Most states already offer a defined-contribution retirement plan for selected educational employees. In Kansas, for example, university faculty and other unclassified staff are in a defined-contribution plan sponsored by TIAA-CREF. Employees contribute 5.5% percent of their salaries to the plan and the State contributes an additional 8.5% percent. This plan is portable because the employees can take both employer and employee contributions with them if they change jobs. The plans also provides the employees with wide choice over where those funds are invested. The Legislature also has provided a similar plan to a small number of executive and legislative branch employees who are in positions that are potentially short-term.

To find out what alternatives other states had developed that offered more flexibility or portability for other State employees, we interviewed officials from the National Conference of State Legislatures and the Government Finance Officers Association, and reviewed several states' retirement plans. Generally, aside from making deferred compensation programs available to employees who wish to—and can afford to—set aside additional moneys for retirement, most states haven't done much to increase portability or flexibility in investing retirement moneys.

A few states have taken steps to make retirement moneys more transportable when employees change jobs. The following listing summarizes those steps; it's followed by more detail about each option.

- giving employees more access to retirement contributions when they change jobs
- offering employees a defined-contribution plan
- offering employees a combination of a defined-benefit plan and a defined-contribution plan
- providing more flexibility in how an employee's retirement benefits are determined

Two states have adopted retirement plans that increase employees' access to retirement contributions when they change jobs. In Colorado, even employees who aren't vested in the state's defined-benefit plan can take some of the employer contributions with them when they change jobs. Non-vested employees can take the contributions they made plus interest, and the retirement system adds an additional

25% to that amount. If non-vested members leave their money in the system until they retire, the retirement system increases the amount it will kick-in to 50% of the amount of the employee contributions plus interest. A health care subsidy and cost-of-living adjustments are also included for employees who leave their money in the system until they retire.

South Dakota has a similar plan, except it's more generous. Employees can choose to be covered by the traditional defined-benefit plan, under which they can't withdraw employer contributions, or by a portable pension program. Under the portable plan, employees who leave with less than three years of service can take the contributions they made, 75% of the employer contributions, and interest. With three or more years of service, employees can take 100% of the employer contributions made on their behalf, in addition to their own contributions plus interest.

One state has offers a non-traditional defined-contribution plan that lets employees invest their retirement funds, but doesn't let them take employer contributions with them if they leave. Nebraska is the only state we contacted that uses a defined-contribution plan instead of a defined-benefit plan. Its plan lets employees choose between three types of funds to invest their moneys. However, unlike most traditional defined-contribution plans, Nebraska's plan isn't portable. Employees who leave before they retire can't take the employer contributions with them.

One state offers a combined defined-benefit and defined-contribution plan that provides employees with a retirement benefit even if they change jobs and withdraw their employee contributions. The State of Washington developed a plan for its teachers so that their benefits could be more portable. Under this plan, the employer contributions are paid into the defined-benefit plan. (The retirement benefit from this portion of the plan is half the amount other state employees would receive.) Employee contributions all are paid into a defined-contribution plan. If employees leave before they retire, they can take the money in the defined-contribution account with them. In some ways, this isn't too different from any defined-benefit plan, because employees can always take their contributions with them when they leave. However, in other plans, if employees withdraw their contributions, they give up their right to a benefit upon retirement. In contrast, with this plan employees can withdraw their contributions and receive their future defined-benefit. In addition, they get to choose how their contributions are invested.

Four states have added features to their defined-benefit retirement plans that give employees more flexibility in how their retirement benefits are determined. In Oregon and Wisconsin, retirees can choose between two methods in computing their annual retirement benefits. First, the state calculates how much of an annual annuity could be purchased based on the employee's contributions, plus interest, plus a 100% employer match. It then calculates how much the employee would receive under the traditional formula. The annuity method may give employees higher benefits, especially if they leave early in their careers.

The Colorado plan mentioned earlier has a similar option. In Colorado's case, the alternative method of calculating the benefit is to determine the annual annuity that could be purchased based on the employee's contributions, plus interest, plus a 50% employer match. The member gets the higher amount.

Although this feature can increase the amount of money an employee receives upon retirement, it doesn't necessarily make benefits any more portable. The employee can't take the employer contributions with them if they leave before retirement.

In a somewhat related variation, South Dakota provides an option for employees who elect to participate in the portable pension plan described earlier. When employees who participate in that plan retire, they can choose to receive a benefit based on the amount in their account—including the employer contributions—or to have their benefit calculated under the defined-benefit formula. This option in essence protects the employee from the investment risks in a defined-contribution plan.

Decreasing the Vesting Period Could Give Employees Greater Flexibility to Build Retirement "Nest Eggs" With Multiple Employers

With a 10-year vesting period, such as the Retirement System has, employees could change jobs every nine years and end up with no retirement benefits. Shorter vesting allows employees who change jobs frequently to accrue retirement benefits with several employers. Even with the built-in penalty associated with defined-benefit retirement plans, as described earlier, employees who become vested in their employers' retirement plans could at least build some retirement benefit as they go from job to job. A reduced benefit is much better than no benefit at all.

Federal law recognizes this drawback, and requires private companies to allow their employees to become vested in five years, or in seven years if they phase-in vesting over the seven-year period. As mentioned in Question One, Kansas' retirement system is among a group of states that has one of the longest vesting periods. A total of 23 states we reviewed had vesting periods of five or fewer years for their retirement systems.

Private Employers Appear to Frequently Offer Both Defined-Benefit and Defined-Contribution Plans For Their Employees

As discussed in Question One, Hewitt Associates, a large pension consulting firm, reported that about 80% of major employers offer both defined-benefit and defined contribution plans for their employees. This trend appears to be true with large Kansas Employers as well.

Based on our contacts with Blue Cross and Blue Shield, Cessna, Goodyear, and Security Benefit Group, we found that all four companies provided both types of plans for their employees. The defined-benefit plans offered by these employers don't offer any more portability or flexibility than the Retirement System does. But, the defined-contribution portion gives vested members access to both the employee and the employer portion of the contributions, and the employees have a choice of several different funds they can invest in.

Although Defined Contribution Plans Can Create More Portability And Investment Choices for Employees, These Plans Don't Necessarily Guarantee a Larger Retirement Benefit

The table on page 15 showed the benefits three employees would receive from a defined-benefit plan. To compare defined-benefit and defined-contribution plans, we estimated the size of the benefit that those employees might receive from two different defined-contribution plans. This is shown in the table below. Plan I in the table below has a contribution rate of 4% from both employee and employer. This is close to the contribution rates in the current the Retirement System defined-benefit plan. Plan II has a contribution rate of 5.5% for employees and 8.5% for the employer. The latter plan is based on the TIAA-CREF plan available to Kansas' unclassified university employees.

The benefits from defined-contribution plans vary greatly, depending on how employees invest the money. To illustrate this, we estimated a range of annual benefits these plans might yield for the three employees. To get the range, we estimated how much money would've accumulated if accounts earned average annual returns of 5% and 8% respectively. After determining how much money would've accumulated, we determined the size of the annual annuity that could be purchased with that money. Actual results could be higher or lower than either of these two assumptions, depending on actual investment results. (Appendix B shows the annual contributions and ending balances of the hypothetical accounts shown in the table.)

Comparison of Three Employee's Benefits From Defined-Benefit Plans and Defined-Contribution Plans

	Annual Retirement Benefit		
	Employee A Same Employer 30 Years	Employee B Three Employers 10 Yrs Each	Employee C Five Employers 6 Yrs Each
Defined-Benefit Plan			
(10-Year Vesting)	$15,750	$11,696	$0
Defined-Contribution Plan			
(5-Year Vesting)			
Plan I (a)	$7,173 to $11,424	$7,173 to $11,424	$7,173 to $11,424
Plan II (b)	$12,567 to $19,988	$12,567 to $19,988	$12,567 to $19,988

(a) Plan I is a plan with 4% employer and 4% employee contributions
(b) Plan II is a plan with 8.5% employer and 5.5% employee contributions

Defined-Contribution plans are more portable than defined-benefit plans, but may give lower benefits. The defined-contribution plans are totally portable. As the table above shows, each of the employees received the same final annu-

1-23

al benefit no matter how many times they changed jobs, and with no penalty. However, the table shows that portability can come at a cost to the employee if the plan's contribution rates are low.

As the table shows, a defined-contribution plan with contribution rates similar to those currently used to fund the Retirement System (Plan 1 in the table) wouldn't produce as good a retirement benefit for employees A and B as does the current defined-benefit plan offered by the Retirement System. It's only when contribution rates are increased substantially, as in Plan II, that the defined-contribution plan begins to produce a better benefit. On the other hand, the most transient of the three employees (Employee C) gets a better benefit from the defined-contribution plan under both scenarios because he didn't work for any employer long enough to vest under the defined-benefit plan.

Conclusion

It is clear that defined-benefit retirement plans aren't as beneficial to short-term employees as they are to long-term employees. This report mentions a number of ways to increase portability or flexibility for State employees. However, most of the alternatives have some actual or potential cost to the State or to the employee. For example, allowing employees to take employer contributions with them when they change jobs would likely increase the employer contribution rate needed to fund the system in the future. Likewise, having a shorter vesting period would increase the number of employees who are eligible for retirement, thus increasing the costs of the System. Converting to a defined-contribution plan might give more portability and choices, but could result in smaller benefits for many employees. Also, the Retirement System would have to continue to administer the defined-benefit plan for those employees who didn't choose to transfer to the defined-contribution plan.

APPENDIX A

Benefits Offered By a Sample of State Retirement Systems

The following tables give details about retirement benefits offered by a sample of state retirement systems. Most of this information is taken from a recent survey of state retirement systems conducted by the Government Finance Officers Association. Information from that survey was for fiscal year 1994. We updated the information for states shown in bold face type to fiscal year 1996.

State	Type of Plan	Benefit as % of Salary 30 Yrs Service	20 Yrs Service	10 Yrs Service	Annual Benefit For Employee With Final Average Salary = $30,000 30 yrs Service	20 yrs Service	Provide Cost of Living Increases?	Automatic or Ad Hoc?
Alabama	Defined-Benefit	60.4	40.2	20.1	$18,114	$12,060	Yes	Ad Hoc
Alaska	Defined-Benefit	67.5	42.5	20.0	$20,250	$12,750	Yes	Automatic
Arizona	Defined-Benefit	60.0			$18,000		Yes	
Arkansas	Defined-Benefit	46.5	31.0	15.5	$13,950	$9,300	Yes	Automatic
California	Defined-Benefit	37.5	25.0	12.5	$11,250	$7,500	Yes	Automatic
Connecticut	Defined-Benefit						Yes	
Delaware	Defined-Benefit	50.0	33.0	17.0	$15,000	$9,900	Yes	Ad Hoc
Florida	Defined-Benefit	48.0	32.0	16.0	$14,400	$9,600	Yes	Automatic
Georgia	Defined-Benefit	49.0	33.0	16.0	$14,700	$9,900	Yes	Ad Hoc
Hawaii	Defined-Benefit	60.0			$18,000			
Idaho	Defined-Benefit	57.5	38.3	19.2	$17,253	$11,502	Yes	Both
Illinois	Defined-Benefit	34.0	21.0	10.0	$10,200	$6,300	Yes	Automatic
Iowa	Defined-Benefit	65.0	43.3	21.7	$19,500	$13,002	Yes	Ad Hoc
Kansas	**Defined-Benefit**	**52.5**	**35.0**	**17.5**	**$15,750**	**$10,500**	**Yes**	**Ad Hoc**
Kentucky	Defined-Benefit	59.0	39.0	20.0	$17,700	$11,700	Yes	Automatic
Michigan	Defined-Benefit	45.0	30.0		$13,500	$9,000	Yes	Automatic
Minnessota	Defined-Benefit	45.0	30.0	15.0	$13,500	$9,000	Yes	Both
Mississippi	Defined-Benefit	56.9	37.5	18.8	$17,064	$11,250	Yes	Both
Missouri	Defined-Benefit	48.0	32.0	16.0	$14,400	$9,600	Yes	Automatic
Montana	Defined-Benefit	53.6	35.7	17.9	$16,071	$10,713	Yes	Automatic
Nebraska	Def. Contribution	NA	NA	NA	NA	NA	No	NA
New Hampshire	Defined-Benefit	50.0			$15,000		Yes	
New Jersey	Defined-Benefit	50.0	33.3	16.7	$15,000	$10,002	Yes	Automatic
New Mexico	Defined-Benefit	80.0	60.0	30.0	$24,000	$18,000	Yes	Automatic
New York	Defined-Benefit	53.2	33.3	16.7	$15,960	$9,990	Yes	Ad Hoc
North Dakota	Defined-Benefit	52.2	34.8	17.4	$15,660	$10,440	Yes	Ad Hoc
Oklahoma	Defined-Benefit	60.0	40.0	20.0	$18,000	$12,000	Yes	Ad Hoc
Oregon	Combination	50.1	33.4	16.7	$15,030	$10,020	Yes	Automatic
Pennsylvania	Defined-Benefit	60.0	40.0	20.0	$18,000	$12,000	Yes	Ad Hoc
Rhode Island	Defined-Benefit	66.0	36.0	17.0	$19,800	$10,800	Yes	Automatic
South Carolina	Defined-Benefit	54.6	36.4	18.2	$16,380	$10,920	Yes	Automatic
South Dakota	Defined-Benefit	40.5	27.0	13.5	$12,150	$8,100	Yes	Automatic
Tennessee	Defined-Benefit	45.0	30.0	15.0	$14,458	$9,639	Yes	Automatic
Texas	Defined-Benefit	60.0	40.0	20.0	$18,000	$12,000	No	NA
Utah	Combination	60.0	40.0	20.0	$18,000	$12,000	Yes	Automatic
Virginia	Defined-Benefit	49.5	33.0	16.5	$14,850	$9,900	Yes	Automatic
Washington	Defined-Benefit	60.0	40.0	20.0	$18,000	$12,000	Yes	Automatic
Wisconsin	Combination	48.0	32.0	16.0	$14,400	$9,600	Yes	Automatic
Wyoming	Defined-Benefit	60.0	40.0	20.0	$18,000	$12,000	Yes	Automatic

States That Don't Participate In Social Security

Louisiana	Defined-Benefit	75.0			$22,500			
Nevada	Defined-Benefit	75.0	50.0	25.0	$22,500	$15,000	Yes	Automatic
Colorado	Defined-Benefit	65.0	50.0	25.0	$19,500	$15,000	Yes	Automatic
Ohio	Defined-Benefit	63.0	42.0	21.0	$18,900	$12,600	Yes	Automatic
West Virginia	Defined-Benefit	60.0	40.0	20.0	$18,000	$12,000		

Notes:

Information for states whose names are shown in bold face type has been updated to Fiscal Year 1996. Information for all other states is from Fiscal Year 1994.

Blank spaces indicate the state made no answer.

NA means not applicable.

State	1994 Contribution Rate (%) Employer	Employee	Years To Vest	% The System Is Funded	Health Care Available?	% Health Care Premium Paid By State
Alabama	6.99	5.00	10	91.3	Yes	0
Alaska	13.00	6.75	5	94.8	Yes	62
Arizona	3.14			109.0		No Answer
Arkansas	10.00	0.00	10	108.8	Yes	No Answer
California	11.01	7.00	10	96.4	Yes	92.5
Connecticut	14.72	0.00	10	53.8	Yes	100
Delaware	6.10	3.00	5	100.0	Yes	80
Florida	17.66	0.00	10	69.4	No	NA
Georgia	13.49	1.25	10	84.4	Yes	No Answer
Hawaii	14.72			92.3		No Answer
Idaho	11.63	6.97	5	70.7	Yes	No Answer
Illinois	4.86	4.00	5	57.2	Yes	80
Iowa	5.75	3.70	4	100.0	No	NA
Kansas	**3.10**	**4.00**	**10**	**78.2**	**Yes**	**15**
Kentucky	7.65	5.00	1 month	93.7	Yes	0-100
Michigan	11.33	0.00	10	83.5	Yes	95
Minnesota	4.20	4.07	3	81.5	Yes	0
Mississippi	9.75	7.25	4	64.0	Yes	0
Missouri	9.48	0.00	5	83.1	Yes	45
Montana	6.70	6.42	5	84.1	Yes	No Answer
Nebraska	varies	3.60	5	NA	Yes	No Answer
New Hampshire	3.34	0.00		58.1		No Answer
New Jersey		5-8.7	10	99.0	Yes	100
New Mexico	16.59	7.42	5			No Answer
New York	0.70	3.00	10	100.0	Yes	No Answer
North Dakota	4.12	4.00	5	98.9	Yes	0
Oklahoma	12.00	2.50	8	79.1	Yes	No Answer
Oregon	9.15	6.00	5	92.4	Yes	0
Pennsylvania	10.27	5.00	10	101.8	Yes	No Answer
Rhode Island	11.84	7.75	10		Yes	0
South Carolina	7.55	6.00	5	79.9	Yes	
South Dakota	5.00	5.00	5	70.5	Yes	100
Tennessee	5.00	0.00	5	95.6	Yes	0
Texas	6.45	6.00	5	106.9	Yes	100
Utah	11.66	0.00	4	88.4	Yes	No Answer
Virginia	5.40	5.00	5	98.1	Yes	No Answer
Washington	7.41	5.00	5	249.3	No	NA
Wisconsin	6.40	0-6.2	5	93.1	Yes	47
Wyoming	5.68	5.57	2	111.2	No	NA
Louisiana	11.87			61.3		
Nevada	9.31	9.31	5	73.9	Yes	
Colorado	10.80	8.00	5	87.0	Yes	Varies
Ohio	13.31	8.50	5	87.6	Yes	100
West Virginia	9.23		5	86.0		

1-27

APPENDIX B

Estimates of the Annual Benefits Resulting From Two Defined-Contribution Retirement Plans

The first table in this appendix is an example of a defined-contribution plan with a contribution rate of 4% from both employee and employer. This is close to the contribution rates in the current the Retirement System defined-benefit plan. The second table is an example of a defined-contribution plan with a contribution rate of 5.5% for employees, and 8.5% for the employer. The latter plan is based on the TIAA-CREF plan available to Kansas' unclassified university employees.

We calculated ending balances for the accounts under two interest rate assumptions. For a more conservative investor, we assumed an average annual interest rate of 5% over the 30-year period. For a less conservative investor, we assumed average annual interest of 8%. After calculating the ending account balances, we determined the size of the annual annuity that could be purchased with each.

Estimate of the Annual Benefit From a Defined-Contribution Account With 4% Employer Contributions and 4% Employee Contributions

Year	Salary	Employee Contribution 4.0%	Employer Contribution 4.0%	Account Ending Balance 5% Interest	Account Ending Balance 8% Interest
1	$7,830	$313	$313	$626	$626
2	8,222	329	329	1,348	1,387
3	8,633	345	345	2,141	2,244
4	9,064	363	363	3,009	3,206
5	9,518	381	381	3,959	4,285
6	9,993	400	400	4,997	5,491
7	10,493	420	420	6,128	6,837
8	11,018	441	441	7,360	8,336
9	11,569	463	463	8,700	10,003
10	12,147	486	486	10,155	11,852
11	12,754	510	510	11,734	13,903
12	13,392	536	536	13,446	16,172
13	14,062	562	562	15,299	18,681
14	14,765	591	591	17,304	21,451
15	15,503	620	620	19,472	24,506
16	16,278	651	651	21,813	27,873
17	17,092	684	684	24,339	31,580
18	17,947	718	718	27,064	35,657
19	18,844	754	754	30,000	40,138
20	19,786	791	791	33,162	45,058
21	20,776	831	831	36,565	50,458
22	21,814	873	873	40,226	56,379
23	22,905	916	916	44,161	62,868
24	24,050	962	962	48,390	69,976
25	25,253	1,010	1,010	52,930	77,756
26	26,516	1,061	1,061	57,804	86,267
27	27,841	1,114	1,114	63,033	95,574
28	29,233	1,169	1,169	68,640	105,746
29	30,695	1,228	1,228	74,651	116,858
30	$32,230	$1,289	$1,289	$81,090	$128,991
Account Balance at Retirement =				**$ 81,090**	**$ 128,991**
Amount of Lifetime Annual Annuity =				**$7,173**	**$11,424**

1-29

Estimate of the Annual Benefit From a Defined-Contribution Account With 8.5% Employer Contributions and 5.5% Employee Contributions

Year	Salary	Employee Contribution 5.5%	Employer Contribution 8.5%	Account EndingBalance 5% Interest	Account EndingBalance 8% Interest
1	$7,830	$431	$666	$1,096	$1,096
2	8,222	452	699	2,360	2,427
3	8,633	475	734	3,747	3,926
4	9,064	499	770	5,266	5,611
5	9,518	523	809	6,929	7,499
6	9,993	550	849	8,744	9,610
7	10,493	577	892	10,724	11,965
8	11,018	606	937	12,880	14,588
9	11,569	636	983	15,224	17,505
10	12,147	668	1,033	17,771	20,742
11	12,754	701	1,084	20,535	24,330
12	13,392	737	1,138	23,530	28,301
13	14,062	773	1,195	26,774	32,691
14	14,765	812	1,255	30,283	37,539
15	15,503	853	1,318	34,076	42,886
16	16,278	895	1,384	38,173	48,778
17	17,092	940	1,453	42,594	55,265
18	17,947	987	1,525	47,362	62,399
19	18,844	1,036	1,602	52,500	70,241
20	19,786	1,088	1,682	58,033	78,852
21	20,776	1,143	1,766	63,989	88,301
22	21,814	1,200	1,854	70,395	98,663
23	22,905	1,260	1,947	77,282	110,020
24	24,050	1,323	2,044	84,682	122,458
25	25,253	1,389	2,147	92,628	136,073
26	26,516	1,458	2,254	101,157	150,968
27	27,841	1,531	2,367	110,308	167,255
28	29,233	1,608	2,485	120,120	185,055
29	30,695	1,688	2,609	130,639	204,501
30	$32,230	$1,773	$2,740	$141,908	$225,734
Account Balance at Retirement =				**$141,908**	**$225,734**
Amount of Lifetime Annual Annuity =				**$12,567**	**$19,988**

1-30

APPENDIX C

Agency Response

On October 17, 1996, we provided copies of the draft audit report to the Kansas Public Employees Retirement System. Their response is included as this appendix.

Kansas Public Employees Retirement System

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LEGISLATIVE POST AUDIT

October 23, 1996

Barbara J. Hinton, Legislative Post Auditor
Legislative Division of Post Audit
800 Southwest Jackson Street, Suite 1200
Topeka, Kansas 66612-2212

Dear Ms. ~~Hinton~~ Barb:

Thank you for the opportunity to formally respond to the draft copy of your completed performance audit, Reviewing Benefits Provided by the Kansas Public Employees Retirement System: A K-GOAL Audit.

The audit report indicates that the Retirement System's benefits are slightly below the average of a large sample of other statewide pension systems while the employer contribution rate in Kansas is among the lowest in the country. We are pleased that the audit findings mirror the results we reported to the House Appropriations and Senate Ways & Means Committees last Spring. Our review, based on the same Public Pension Coordinating Council data base, utilized a universe of similarly-sized public pension systems.

Three factors have enabled KPERS to be a low cost provider of pension benefits as measured by the level of taxpayer paid employer contributions: (1) consistent investment performance at or above market returns; (2) consistent use of prudent and reasonable actuarial assumptions by the Board of Trustees; and (3) consistent funding of required employer contributions by the State and other participating units of government.

I look forward to sharing a few, brief comments with the Legislative Post Audit Committee at its meeting next week. As always, we will also be prepared to answer any other questions that members may have about the Retirement System's operations.

Our standing practice is to invite you to present all completed audits to the Board of Trustees and its Audit Subcommittee. Accordingly, this audit report will appear on agendas for the November 15, 1996 meetings of both bodies.

Sincerely,

Meredith Williams
Executive Secretary

Capitol Tower ■ Suite 200 ■ 400 S.W. 8th Ave. ■ Topeka, Kansas 66603-3925 ■ Phone (913) 296-6666
KPERS Telephone Facsimile (913) 296-2422
Call Toll Free 1-800-228-0366