

MINUTES OF THE APPROPRIATIONS COMMITTEE.

The meeting was called to order by Chairperson Phill Kline at 10:00 a.m. to 11:00 a.m. on January 19, 1999 in Room 514-S of the Capitol.

All members were present except: Rep. McKechnie  
Rep. Shari Weber  
Rep. Phil Kline  
Rep. George Dean

Committee staff present: Legislative Research - Alan Conroy, Julian Efird, Stuart Little, Robert Waller  
Revisor of Statutes - Jim Willson, Mike Corrigan  
Secretary - Ann McMorris

Conferees appearing before the committee:

Julian Efird, Principal Analyst, KLRD  
Pat Beckham, KPERS Actuary, Milliman & Robertson, Inc., Omaha, NE  
Meredith Williams, Executive Secretary, KPERS

Others attending: See attached list

Chair opened meeting at 10:00 a.m. and called on the first conferee.

**Kansas Public Employees Retirement System - Unfunded Liability**

Julian Efird, Principal Analyst, Kansas Legislative Research, briefed the committee on the conclusions and recommendations of the Joint Committee on Pensions, Investments and Benefits. After reviewing the background of the committee, he moved to information on KPERS investments and unfunded liability. The chart on benefits paid, litigation report, membership on board and the studies made during the interim were reviewed. The joint committee recommended continued study on defined contribution plans as they felt more research was needed before making a final recommendation. The joint committee has been appointed and will have its first meeting to hear the consultants report. (Attachment 1)

Meredith Williams, executive secretary, KPERS, addressed the committee. He said that KPERS is different than most agencies, it makes money. In 1998 KPERS had investment earnings of about \$1.25 billion and after paying out \$512 million in benefits to 51,000 members, and had a net of revenues over expenditures of \$1.75 billion. KPERS takes contributions from members and employers and invests them prudently. At the end of fiscal year 1998, the KPERS fund had \$8.8 billion which is held in trust. As of a week ago that had grown to \$9.23 billion. The return for the first six months appears to be around 5%. KPERS makes projections for many years in the future on all employees and depend heavily on actuaries and complex formulas. He introduced Pat Beckham who is a fellow of the Society of Actuaries and a member of American Academy of Actuaries.

Patrice A. Beckham, F.S.A., Milliman & Robertson, Inc., visited with the committee about KPERS and the actuarial funded status of the system. She reviewed the Triennial Experience Study which was conducted and reported to the Board and the June 1998 actuarial evaluation which was presented to the Board in October. (Attachment 2) She reviewed the definitions of actuarial terms. In particular she noted that unfunded actuarial liability is often compared to a mortgage. The amortization is calculated at a level percent of pay, not a level dollar amount. Economic assumptions and demographic assumptions were discussed. Source of contributions and their impact on the system were analyzed.

Next meeting will be held on January 20, 1999.

Adjournment.

Respectfully submitted,  
Ann McMorris

Attachments - 2



# JOINT COMMITTEE ON PENSIONS, INVESTMENTS, AND BENEFITS

## RETIREMENT ISSUES AFFECTING PUBLIC EMPLOYEES AND RETIREES\*

### CONCLUSIONS AND RECOMMENDATIONS

The Committee recommends to continue studying defined contribution plans; develop a KP&F definition during the 1998 interim; introduce a bill for special local contribution rates; and confirm the Governor's nominee to the Board of Trustees.

### BACKGROUND

The Joint Committee on Pensions, Investments, and Benefits historically has been charged by statute to monitor, review, and make recommendations relative to investment policies and objectives formulated by the Kansas Public Employees Retirement System (KPERs) Board of Trustees; to review and make recommendations related to benefits for members under KPERs; and to consider and make recommendations on the confirmation of members nominated by the Governor to serve on the KPERs Board of Trustees.

Other topics are assigned by the Legislature or Legislative Coordinating Council (LCC). The 1998 Legislature added a statutory requirement to study local correctional officers and membership in the Kansas Police and Fireman (KP&F) Retirement System. The LCC assigned the topic of studying certain groups of state employees and possible inclusion in KP&F. Also, the LCC authorized the Committee to hire an actuarial consultant for assistance in studying defined contribution plans.

### COMMITTEE ACTIVITIES

In reviewing the interim study topics, the Joint Committee held regular meetings in Topeka on July 1-2, July 8, September 10-11, October 15, and November 9-10, 1998. The minutes and attachments for all meetings are available in the Division of Legislative Administrative Services. The following topics were studied by the Joint Committee during the 1998 interim.

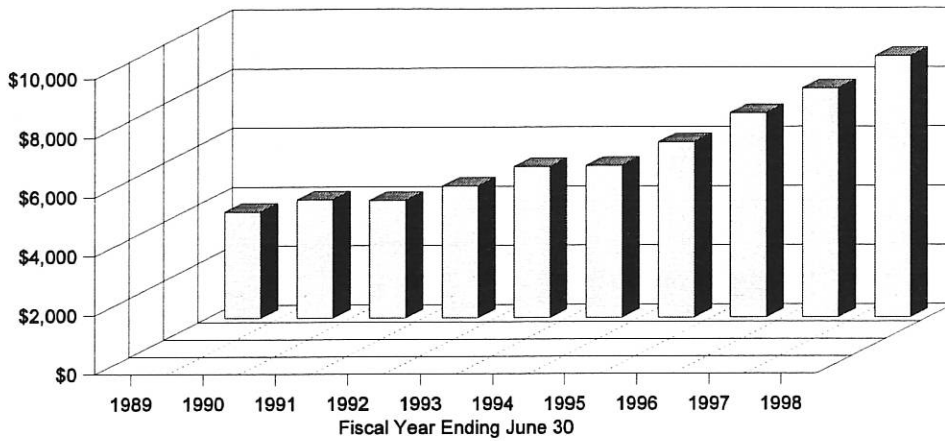
#### **KPERs Investments**

News from the KPERs administrators for the plan year that ended June 30, 1998, has been good. Earnings reported in FY 1998 indicate that investments had an overall annual rate of return equal to 16.5 percent. The investment portfolio grew in value to \$8.8 billion on June 30, 1998, compared with a year earlier when the Fund's investments were valued at \$7.7 billion. Investment performance for the last ten fiscal years has helped increase the KPERs net asset value from \$3.6 billion in FY 1989. Growth in the past four fiscal years is notable in the table below when double digit growth took place.

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\* S.B. 41 accompanies this report.

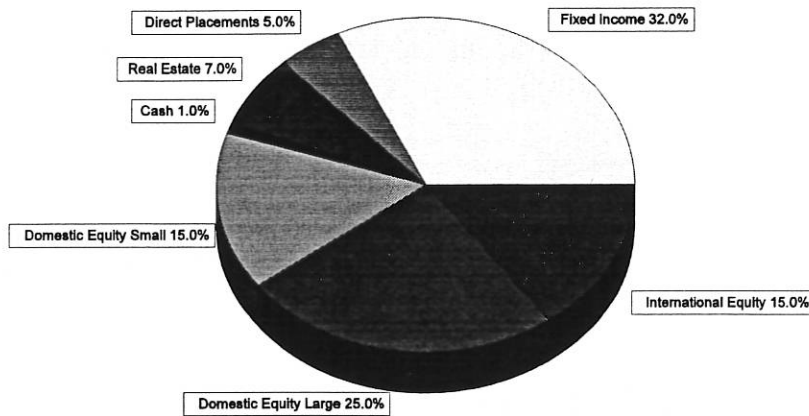
**KPERS Net Asset Value of Investments**  
(In Millions)



The KPERS Board of Trustees adopted a new investment policy to guide the relative proportion of the portfolio that is allocated to different types of investments. Previously, the allocation of KPERS assets was based on a policy adopted

January 28, 1994, and continued until July 16, 1998. The new target allocation policy adopted by the KPERS Board of Trustees on July 17, 1998, is shown in the following chart.

**KPERS Target Asset Allocation**  
As of July 17, 1998



**Unfunded Liability**

The KPERS actuary presented the results of

the FY 1998 actuarial valuation, which included an adjustment in actuarial assumptions. The report reflected favorable investment experience

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over the past plan year that ended June 30, 1998. However, the unfunded actuarial liability increased by \$215 million, primarily due to the change in actuarial assumptions approved by the KPERS Board of Trustees. The following table shows a summary of the actuarial calculations that resulted in an increase of the unfunded actuarial liabilities for the Fund.

	In Millions
Unfunded actuarial liability as of June 30, 1997	\$ 1,376
Investment gain	(413)
Change in actuarial assumptions	350
Liability loss from actual experience	104
1998 ad hoc COLA	88
Effect of employer contribution/time lag	54
Expected increase due to amortization method	32
Unfunded actuarial liability as of June 30, 1998	\$ 1,591

An asset valuation method, approved by the KPERS Board of Trustees, is used by the KPERS actuary to smooth the effect of market fluctuations in order to lessen the year-to-year changes in employer contribution rates. The actuarial value of assets is equal to the expected asset value based on an assumed earnings rate of 8.0 percent, plus one-third of the difference between the actual market value and the expected asset value. Unrecognized gains or losses from prior years also are considered. The other two-thirds of the current difference are taken into account in subsequent years when future valuations are performed. This asset valuation method tends to influence the amount of investment gain reported by the actuary.

For the FY 1998 valuation done on June 30, 1998, there was an actuarial gain of \$413 million based on the investment gain using the market

smoothing method. There was a liability loss of \$104 million due to actual experience which was calculated by the KPERS actuary. An actuarial loss due to poor experience was recognized in last year's valuation, and was addressed by this year's three-year experience study which resulted in a change of actuarial assumptions. The changes in actuarial assumptions, which were approved by the KPERS Board of Trustees, have an immediate negative impact on the unfunded liability resulting in an additional \$350 of liability. However, by addressing these long-term adjustments, the liability loss from actual experience for future valuations should be minimized in the subsequent years.

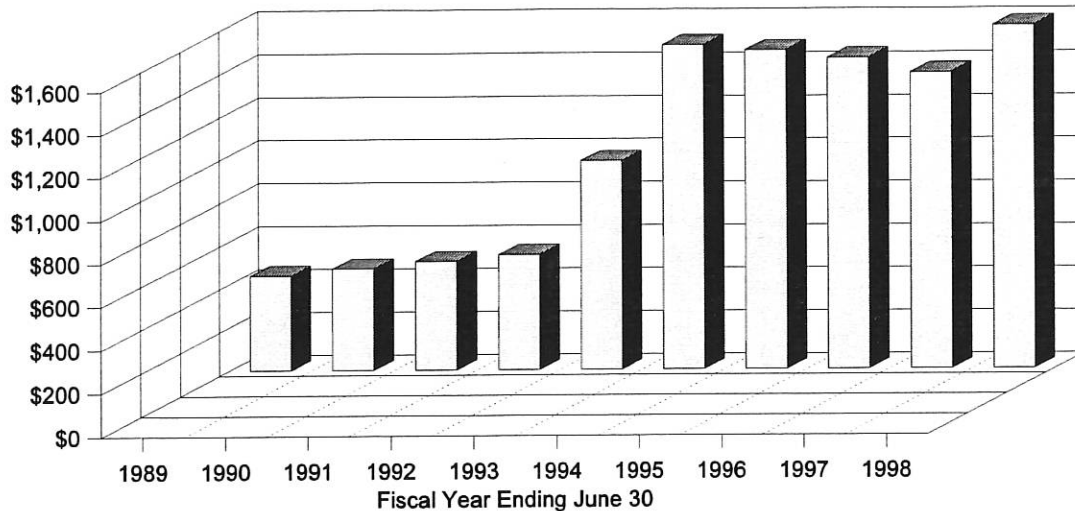
Among the final factors cited by the KPERS actuary as impacting the unfunded liability was the 1998 COLA. The original actuarial cost estimate of \$108 million was reduced to \$88 million by prepaying \$20 million of the state's cost. Other factors having negative impact on the unfunded liability are the expected increase due to the amortization method with negative impact (calculated at \$35 million) and the lag in employer contributions reaching the actuarially required amounts (which result in a negative impact of \$54 million).

The net impact of changes in this year's actuarial valuation results in an increase of unfunded liability to almost \$1.6 billion at the end of FY 1998. Unfortunately, the improvements in the unfunded liability recognized over the past three years are reversed this year as shown in the following bar chart.

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## KPERS Unfunded Liability

(In Millions)



### Actuarial Projections

There has been anticipation that continued good investment performance would reduce significantly the unfunded liability and accelerate the "equilibrium" point when the statutorily defined KPERS rate of employer contributions will equal the actuarially required rate. Currently, the full actuarial contribution is not made by all employers. Statutes provide that the employer rates of contribution for KPERS state/school and local units may not increase over the prior year by more than 0.20 percent for state/school and 0.15 percent for local employers. Since the actual contribution rates have been less than the actuarially required rates for the past several years, this shortfall has the effect of increasing the unfunded liability and thus is one factor in that calculation. Until "equilibrium" is reached, this condition will continue to have a negative impact on the unfunded liability.

The KPERS actuary presented new projections of the employer contribution rates for future years and the estimated year of "equilibrium" for rates. The convergence of projected and actuarial rates may change based on factors evaluated annually by the KPERS actuary. However, once equilibrium is achieved, govern-

mental payments for KPERS contributions should have reached the maximum rate required in order to pay for the unfunded liability during the remaining years of the plan period. A November 1998 projection, based on the most recent actuarial valuation, shows that the state's employer contribution rate will peak in FY 2005 at 5.32 percent for the state/school payments. Last year's 1997 projection indicated equilibrium in FY 2003 at 4.71 percent for the state/school rate. The local employer's contribution rate was accelerated by one year and remains at 3.4 percent for equilibrium.

### Convergence of Employer Rates

	1998	1997
State/School	5.32%	4.71%
Fiscal Year	2005	2003
Local	3.4%	3.41%
Calendar Year	2002	2003

### Post-Retirement Benefits

The number of retired members increased from 38,243 in FY 1989 to 50,071 on July 1, 1998. Benefits paid to retirants and their beneficiaries

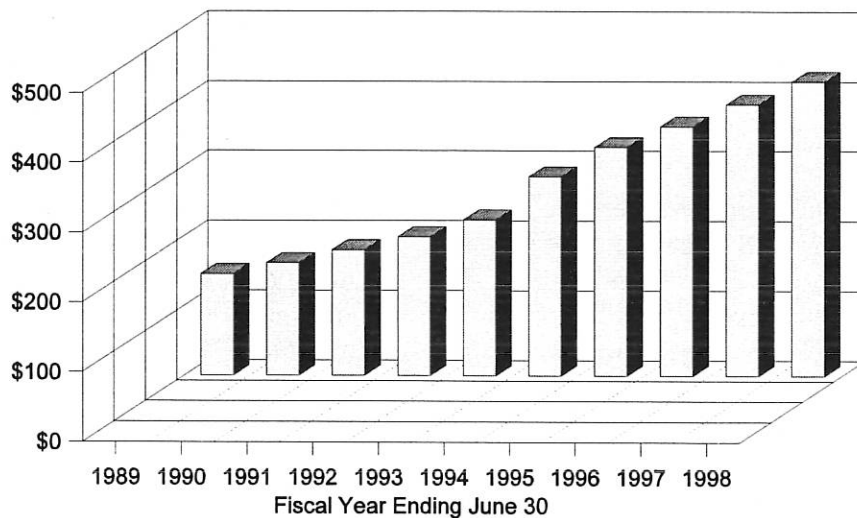
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increased from \$145.2 million in FY 1989 to \$421.8 million in FY 1998. The average monthly benefit amount increased from \$316 to \$701 between FY 1989 and FY 1998. The increase in the number of retired members and the higher average monthly post-retirement benefits resulted in the growth in annual payments over the FY 1989 to FY 1998 period as shown in the following chart. Of particular note is the increase reflected

first in FY 1994 following substantial enhancement in benefit calculations for retirees after July 1, 1993, and post-retirement adjustments for members retired prior to that date. An almost \$52 million jump occurred in annual payments after the 1993 Legislature provided enhancement retirement benefits for both retirees and those eligible to retire beginning in FY 1994.

**KPERS Retirement Benefits Paid**  
(In Millions)



**Post-Retirement Benefit Adjustments**

One of the factors influencing the FY 1998 actuarial valuation was a COLA. The 1998 Legislature enacted legislation providing post-retirement benefit adjustments for all members of KPERS who retired prior to July 1, 1997, to all disabled members, and to certain members of the old Kansas School Retirement System (KSRS). These were the first adjustments since 1994 when the last cost-of-living increase for retired public employees was passed by the Legislature.

One provision granted KSRS members with 25 or more years of service a monthly benefit increase of \$100, effective July 1, 1998, for anyone who had retired under KSRS prior to January 1,

1971. This increase provided enhanced benefits for 299 KSRS retirants. Because this is an older group that is closed and relatively small, the KPERS actuary indicated there will be a negligible actuarial impact.

The 1998 benefit adjustments include an ad hoc 3.0 percent COLA that was authorized for all persons who retired or started receiving disability benefits prior to July 1, 1997. This COLA is permanent in the sense that it increases the base monthly retirement benefit payment by 3.0 percent and continues throughout the lifetime of the member, as well as any disabled member or beneficiary that shares in the member's benefit.

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The average KPERS monthly benefit payment for the pre-1997 group was increased an average of \$20 per month.

The actuarial cost for this benefit adjustment is \$108.0 million. The actuarial state cost is estimated at \$83.6 million all funds. The actuarial local cost is estimated at \$24.4 million. A portion of the state's actuarial cost was paid in FY 1999 with an appropriation of \$20 million from the State General Fund. The remaining liability was added to the System's unfunded liability and will be paid over 15 years. An adjustment of a 0.19 percent increase in the state/school employer contribution rate is calculated by the KPERS actuary in FY 2001 for benefit enhancements, bringing the total rate to 4.58 percent. The FY 2000 state/school rate is 4.19 percent.

### **Litigation Report**

The Committee received periodic status reports about the KPERS litigation. As of August 31, 1998, KPERS has received settlements of \$27,656,811 and after expenses and fees to attorneys, the net recoveries totaled \$12,062,783 for the Fund. The reimbursable expenses to KPERS totaled \$7,471,777 and the contingent fees paid to attorneys totaled \$8,122,252. At the September meeting, Robert F. Coleman, KPERS Special Counsel, Kansas Litigation Group, presented a brief history of the litigation for members.

### **New KPERS Board Member**

The Joint Committee is authorized by statute to make a recommendation to the Senate about confirmation of the Governor's appointments to the KPERS Board of Trustees. Frank Gaines was nominated by the Governor as a member of the KPERS Board of Trustees. Following an interview with the nominee, the Joint Committee affirmed the Governor's nomination of Frank Gaines to the KPERS Board of Trustees as part of its 1998 interim. A recommendation will be forwarded to the 1999 Legislature.

### **Membership in KP&F**

Two topics were considered under this interim study item: one was directed by a legislative entity and the other by the 1998 legislation.

**KP&F Membership of State Employees.** The LCC assigned as a topic for interim study the question concerning state employees who wish membership in KP&F. The Secretary of Administration presented a joint request from representatives of the Division of Personnel Services and the Kansas Association of Public Employees (KAPE) regarding the inclusion of members from a Statewide Law Enforcement Unit into KP&F.

The joint request is the result of a successfully concluded Memorandum of Agreement involving employees from six state agencies seeking membership in KP&F: enforcement agents from the State Gaming Agency, State Racing Commission, Kansas Lottery, and Alcoholic Beverage Control Division in the Department of Revenue; fire investigators in the State Fire Marshal's Office; and special investigators in the Securities Commission's Office. Also members of the unit, but presently members of KP&F, are agents from the Kansas Bureau of Investigation (KBI).

Other agencies with similar positions, but not included in the Secretary's presentation, are conservation officers and park rangers in the Department of Wildlife and Parks and police officers in the Capitol Area Security Patrol. Separate meet and confer sessions involve those groups. An Attorney General's opinion has been requested in a matter involving the police officers who contend that membership in KP&F should be retroactive to 1976 when the agency was placed under the Kansas Highway Patrol. Other potential eligible groups include parole officers in the Department of Corrections, motor carrier inspectors in the Highway Patrol, and fire protection officers of the Adjutant General. In addition, the Secretary of Corrections has submitted a budget request in FY 2000 to place corrections officers in KP&F.

Actuarial studies were performed for each of the six agencies in the Statewide Law Enforce-



ment Unit to determine the cost for past service credit. The estimated cost, if employees were awarded prior service credit in KP&F, would total \$2,481,350. The cost in FY 2000 for prior service is estimated at \$236,147. Future service only would result in an increase in annual cost, beginning in FY 2000, and estimated at \$64,176.

The Executive Director of KAPE provided information regarding the KAPE position relative to including the state agency personnel in KP&F. It was noted that all of these state employees carry firearms and have authority to make arrests. The job descriptions of each position require certification as a law enforcement officer. KAPE also represents the KBI agents and university police officers who are members of KP&F, and who have similar official duties and job requirements.

#### **KP&F Membership of Local Employees.**

The other topic concerned local correctional officers and jailers under KP&F per 1998 S.B. 11. A new provision in 1998 S.B. 11 defines a policeman and fireman. The provision changes the definition of a policeman to require that certification by the Kansas Law Enforcement Training Commission which initially takes 320 hours of accredited instruction at the Training Center and 40 hours of instruction annually thereafter. As firemen currently do not receive the same type of training, their definition is being changed to require that their principal duties are engagement in the fighting and extinguishment of fires. This amendment would not affect anyone who is already a KP&F member. The old definition of "policeman and fireman" in the KP&F statutes had included language that a person who is ". . . in support thereof and who is specifically designated, appointed, commissioned or styled as such by the governing body or city manager of the participating employer . . ." would be considered a KP&F member.

An amendment in the proposed new definition added a proviso that allows city or county corrections officers to be certified as eligible for KP&F if so designated by a city or county governmental unit or official from July 1, 1998 to June 30, 1999. In addition, a study by the Joint

Committee on Pensions, Investments and Benefits is mandated in statute to review and make recommendations relating to inclusion of city and county correctional officers as eligible members of KP&F. A representative of the Shawnee County jail employees asked for a continued opportunity for local jailers to join KP&F. The Shawnee County officers currently are members of KPERS, and are negotiating with the County Commission on changing to KP&F.

#### **Impact of 15 Percent Cap**

The Executive Director of the League of Kansas Municipalities asked for consideration of an item affecting several Kansas governments, namely the new 15 percent cap on inflating final average salary which has had an adverse financial impact on local units of government. The Personnel Director, United Government of Wyandotte County/Kansas City, Kansas, reported that Price, Waterhouse, Coopers had calculated the potential liability of the change to be \$1,839,811 in 1998 if all 74 eligible employees retired, and \$338,114 in 1999 if all 25 employees retired.

The KPERS Executive Secretary provided information that only four individuals in four different jurisdictions had retired and received lump-sum payments that increased members' final average salary by more than 15 percent. However, the new law has been in effect since July 1, 1998 and as additional employees retire, the impact may be greater.

#### **Retirement Options Reviewed by Consultants**

K.S.A. 46-2201(d) provides that in accordance with K.S.A. 46-1204, the LCC may authorize such professional services as may be requested by the Joint Committee on Pensions, Investments and Benefits. A provision in 1998 legislation appropriates funding to the LCC for an evaluation and study of the KPERS defined benefit plans and the topic of defined contribution plans. According to the conference committee recommendation in the 1998 omnibus bill explanation, funding would provide independent actuarial

services and consultant evaluation of the alternatives and costs of modifying the current defined benefits plans administered by the KPERS Board and adding a defined contribution plan for public employees that either would supplement or replace the present plans.

The LCC delegated selection of a consultant to the Committee. Following distribution of a request for proposals (RFP), two firms submitted proposals, including Deloitte & Touche of Kansas City, Missouri, and Gabriel, Roeder, Smith & Company (GRS) of Southfield, Michigan. The Committee selected GRS as its consultant and transmitted that recommendation to the LCC. A contract between the LCC and GRS was approved by each party to the agreement.

The GRS actuaries were directed by the Committee to focus on the following five alternatives as each would apply to members of KPERS. The first three represent modifications in the present plans, while the last two may be added to the present plans or may be used in combination with other plans.

**Combination DB/DC Plan.** Washington Teachers' Plan 3 created a DC plan funded solely with employee contributions, and a reduced benefit formula DB plan funded solely with employer contributions. Applying this approach to Kansas produces a DC plan funded by 4.0 percent employee contributions under KPERS and 7 percent employee contributions under KP&F. Under the DB plan, the basic benefit accrual rate would be reduced from 1.75 percent to 0.75 percent for KPERS, and from 2.5 percent to 1.25 percent for KP&F.

**Pure DC Plan.** Michigan's DC plan calls for a basic employer contribution plus a match. For Kansas, this would mean a mandatory employee contribution of 4.0 percent of salary for KPERS and 7.0 percent of salary for KP&F. Additional elective employee contributions of as much as 3.0 percent of salary would be permitted. For cost-neutrality, the employer contributions under KPERS would be 4.0 percent of salary plus a 100 percent match of employee contributions above 4.0 percent. For KP&F, the basic employer

contribution rate would be 7 percent, with a 100 percent match of employee contributions above 7 percent. Employer contributions and investment earnings thereon would be vested according to the following schedule: 25 percent after two years of service, 50 percent after three years, and 100 percent after four years.

**Hybrid Plan.** Wichita's Plan 3 provides a DC plan for the first seven years of employment. At the seven-year point, employees must make a one-time election to remain in the DC plan, or transfer their account balances and receive full service credit in the DB plan. The seven-year time frame was selected because it is the vesting period under the Plan 3 DB structure in Wichita. For Kansas, the suggested break point would be ten years. During that period of time, employee contributions (4.0 percent-KPERS; 7.0 percent-KP&F) would be credited to individual accounts, as would employer contributions of 5.0 percent under KPERS and 8.5 percent under KP&F. The funds would be invested with all other system assets and receive the same investment return. Employer contributions and investment earnings would be vested according to the following schedule: 25 percent after three years of service, 50 percent after seven years, and 100 percent after 10 years.

**Section 457 Deferred Compensation Plan with Employer Match.** The Committee expressed an interest in exploring an employer match on employee deferrals to the Section 457 Deferred Compensation Plan. A similar approach is currently used in Missouri. The state's match is \$25 per month for any participant contributing \$25 per month or more to the 457 plan. The match is contributed to a separate 401(a) qualified plan to maximize tax benefits.

Missouri's match was implemented July 1, 1995 and participation increased over 75 percent when comparing June 30, 1994 participation levels with June 30, 1996 levels. Currently, almost 25 percent of participants contribute the minimum of \$25 per month needed to receive the state's match.

There are approximately 9,500 participants in

the State of Kansas Deferred Compensation Plan. Assuming these are all state employees (*i.e.*, none are school district or municipal employees) and that the plan experiences the same results as Missouri in implementing a match, then the participation level would grow to about 16,600 participants, and the cost of the match to the state would be \$4,980,000 per year. If this program were extended to school districts and/or municipalities, they would also incur additional annual costs.

**Deferred Retirement Option Plans (DROPs).** These plans can be added to DB plans as a means of providing orderly transitions at retirement, and partial lump sum payouts to retirees. The following provides additional details, and issues that need to be addressed. Upon becoming eligible for normal retirement, a retirement system member satisfying DROP eligibility conditions is permitted to either retire or continue working and retire at a future date with a pension based on credited service and final average salary (FAS) at date of termination of employment, or elect to participate in the DROP and retire at a future date with a pension based on FAS and service at date of election to participate in the DROP.

Participation in the DROP is generally subject to the following conditions: satisfaction of eligibility conditions which may be more stringent than normal retirement eligibility (*e.g.* completion of 30 years of service). The amount of the member's pension is determined as of the date of DROP participation, based on credited service, FAS, and retirement plan benefit provisions on that date. A DROP account is established in the name of the member. The account is credited with a percentage of the frozen monthly pension payments during the member's continued period of employment. The percentage may be 100 percent or some lower percentage selected so that DROP can be offered by the plan sponsor on a cost-neutral basis. The DROP account established for a given member is credited with payments for up to a maximum number of years (*e.g.*, five) after the date of election to participate in the DROP. Payments beyond the maximum DROP period, but prior to termination of

employment, are forfeited. During the period of employment following election of DROP participation the member does not contribute to the retirement system. Interest is generally credited to the member's DROP account at a fixed rate (*e.g.*, 8.0 percent).

Upon termination of employment the frozen monthly pension begins (adjusted for COLA increases if applicable) and the member can elect one of the following alternatives for the DROP account: lump sum distribution of the account balance, paying the appropriate taxes; roll the account balance into an eligible plan such as an IRA; convert the account balance to a monthly benefit to enhance the regular pension payments; or leave the account balance in the retirement system and draw down a portion either monthly or less frequently, depending on personal financial needs and DROP distribution rules. **Note:** other options may be feasible, but in all cases – including those listed above—there are a number of issues to be considered. For example: tax implications (including amounts to be withheld), required distributions, and administration.

Either or both the DROP and the Section 457 employer-match feature can be added to (1) the existing KPERS program or (2) any of the alternatives studied in this report, with one exception. The DROP feature is not used with a pure DC plan. In developing the benefit structures to apply in Kansas, an effort was made by the actuarial consultants to design plans that would be cost-neutral, *i.e.*, plans whose long-term costs would be approximately the same as the current KPERS benefit structures.

## CONCLUSIONS AND RECOMMENDATIONS

For the 1998 interim period, the Committee makes the following recommendations.

### Retirement Options Reviewed by Consultants

The Joint Committee concludes that the conferees were not able to identify employment problems that need correction through some

adjustment in retirement benefits. Also, there were no compelling arguments for moving to defined contribution plans. However, since the Committee could not finish studying this topic and believes that further analysis is needed in order to learn more about defined contribution plans, no specific recommendations on this topic are offered.

The Committee recommends that the defined contribution study topic be carried over to next interim and that possible continuation with the present consultants be considered if terms mutually agreeable can be reached. The subcommittee of the Chairperson, Vice Chairperson, and Ranking Minority Member will perform any financial negotiating function with regard to the consultant's contract and cost of future work.

The Committee asked the consultant for cost analysis on a DROP plan and a DC plan for new employees only. The consultant's report will be provided to the Joint Committee during the 1999 Legislature in partial fulfillment of the present contract.

#### **KP&F Membership of State Employees**

The Committee considered development of a definition of exactly who should qualify for KP&F membership. The discussion centered on who should be eligible and based on what criteria. Information from the Division of Personnel Services on potential state employee additions to KP&F indicates a number of employees may be eligible who are not members of the Statewide Law Enforcement Unit. Because this topic requires additional study in order to develop a workable definition and to consider other state employees who may qualify for membership, the Joint Committee defers any action on the proposed membership of specific state employees in KP&F.

The Committee recommends that a morato-

rium be placed on all new groups coming into KP&F until a definition can be developed not later than the 1999 interim

#### **KP&F Membership of Local Employees**

The 1998 legislation only provides a window until June 30, 1999, for new local correctional officers to enter KP&F if they do not meet qualifications effective July 1, 1998, regarding membership for all new members of KP&F. A change in definition will preclude new officers from membership in KP&F in the future if they fail to meet the statutory requirements relative to certification as law enforcement officers.

The Committee declines to recommend that a committee bill be introduced to permit local correctional officers to become special members of KP&F.

#### **Impact of 15 Percent Cap**

The Committee considered the KPERS actuary's recommendations of several methods for paying the liability in a manner other than the present lump sum method which places a budget burden on some local units of government. The preferred method would involve the local units of government which incur a cost to pay the liability over 15 years as an increase in the actuarial contribution rate, according to the KPERS actuary.

The Committee recommends introduction of a Committee bill to allow a special local employer contribution rate to be established when the 15 percent cap is exceeded and for the amortization period to be 15 years.

#### **Nomination of KPERS Board Member**

The Joint Committee concurs with the nomination by the Governor of Frank Gaines and recommends during the 1999 Legislature that the Senate confirm the Governor's appointment.

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By Joint Committee on Pensions, Investments and Benefits

AN ACT concerning retirement and pensions; relating to the Kansas public employees retirement system; employer contributions; amending K.S.A. 1998 Supp. 74-49,126 and repealing the existing section.

Be it enacted by the Legislature of the State of Kansas:

Section 1. K.S.A. 1998 Supp. 74-49,126 is hereby amended to read as follows: 74-49,126. (1) Notwithstanding the provisions of subsection (9) of K.S.A. 74-4902 and amendments thereto, any payment for accumulated sick leave, vacation or annual leave, severance pay or any other payments to the member which, when upon retirement, increases the member's final average salary by more than 15%, shall require the participating employer to pay the system a lump-sum amount equal to the system's actuarial liability for benefits attributable to and payable on account of such excess over the 15% or require the participating employer to pay the system as provided in subsection (2).

(2) In lieu of a lump-sum amount as provided in subsection (1), such participating employer may elect to pay the system in an amount sufficient to amortize over a period of no more than 15 years commencing January 1, 2000, the system's actuarial liability for such benefits attributable to and payable on account of such excess over the 15%. The board shall determine for each such participating employer the amount sufficient for amortization. On the basis of such determination the board shall annually certify to each such participating employer separately an actuarially determined rate of contribution which shall be required to be paid by that participating employer. Such rate shall be termed the participating employer's excess liability contribution.

(2) (3) As used in this section, "system" means the Kansas public employees retirement system, the Kansas police and firemen's retirement system and the retirement system for judges.

Sec. 2. K.S.A. 1998 Supp. 74-49,126 is hereby repealed.

Sec. 3. This act shall take effect and be in force from and after its publication in the statute book.



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## Presentation to The Kansas Legislative Committees

January 19, 1999

Presented By:  
Patrice A. Beckham, F.S.A.  
Milliman & Robertson, Inc.

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## Discussion Topics

- Review Triennial Experience Study
- Review 6/30/98 Valuation Results



2





## Actuaries

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- ⦿ **What we do**
  - Advise on how to prefund benefits before they become payable
  
- ⦿ **What we don't do**
  - Impact whether or not a promised benefit is payable

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## Key Terms

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- ⦿ **Present Value**
- ⦿ **Actuarial Cost Method**
  - Normal Cost
  - Actuarial Liability
- ⦿ **Actuarial Value of Assets**
- ⦿ **Unfunded Actuarial Liability (UAL)**
- ⦿ **Experience Gain/Loss**

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## **Actuarial Present Value**

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- **The amount of funds currently required to provide a payment or series of payments in the future.**
- **Determine by discounting future payments at actuarial interest rate and by probabilities of payment.**

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## **Actuarial Cost Method**

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**Mathematical technique which assigns costs to specific years.**

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## **Actuarial Cost Method**

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**Normal Cost: Cost assigned to current year by actuarial cost method.**

**Actuarial Liability (AL): Portion of actuarial present value of benefits attributable to prior service under the actuarial cost method.**

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## **Actuarial Value of Assets**

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**Methodology used to assign a value to the current assets in the Fund for valuation purposes.**

8

2-4



## **Unfunded Actuarial Liability (UAL)**

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**Difference between Actuarial Liability and Actuarial Value of Assets**

**Impacted by:**

**Experience Gains/Losses**

**Change in Assumptions**

**Changes in Benefit Structure**

**Contributions Actually Made**

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## **Amortization of UAL**

- 
- ⊗ **Pay off current present value amount with periodic payments of interest & principal .**
  
  - ⊗ **KPERS payment calculated as level % payroll so dollar amount of payment increases 4% each year.**
  
  - ⊗ **KPERS amortization period set statutorily at 40 years, measured from 1993.**

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2-5



## Experience Gain/Loss

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- Difference between actual experience and that anticipated by the actuarial assumptions during the period between two valuation dates.
- Measured as difference between actual UAL and expected UAL.

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## Purpose of an Experience Study

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- Evaluate actual experience vs. expected
- Future expectations
- Input from System, Advisors, Board
- Outcome: Keep/change assumptions



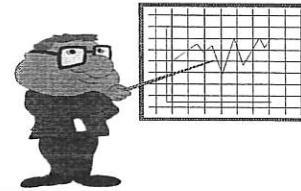
12



## Actuarial Assumptions

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- No “correct” assumptions
- Range of reasonableness
- Economic and Demographic



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## Economic Assumptions

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- Inflation: 3.5%
- Payroll Growth: 4.0%
- Rate of Return: 8.0%

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## Demographic Assumptions

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- **Mortality - Update to 1994 GAM Table**
- **Retirement - New rates by group reflect earlier retirement under Rule of 85, especially for school**
- **Disability - Overall good fit but fine tuned assumption for each group**
- **Termination - Separate rates based on service for first 4 years; age based factors thereafter**
- **Probability of Vesting - age based by Group**

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## June 30, 1998 Actuarial Valuation

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- **Determine actuarial contribution rates**
- **Disclose asset/liability measures**
- **Analyze experience**
- **Report on trends**



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2-8



## Changes from 1997 Valuation

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- New membership and asset information
- New actuarial assumptions
- July 1998 Ad-hoc COLA

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## Change in Unfunded Actuarial Liability

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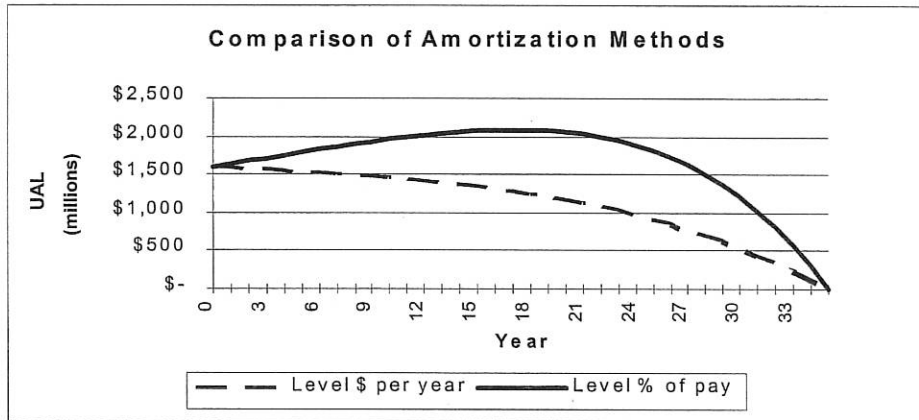
(Unfunded) Actuarial Liability 6/30/97	(1,376)
• Effect contribution cap and time lag	(54)
• Expected increase due to amortization method	(32)
• Investment gain	413
• Change in assumption	(350)
• 1998 Ad-hoc COLA	(88)
• Liability loss from actual experience	(104)
(Unfunded) Actuarial Liability 6/30/98	(1,591)

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## Amortization of UAL



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## Change in State /School Rate

Actuarial Contribution Rate, 6/30/97 5.27%

Change in amortization of UAL:

• Effect of contribution cap/time lag	0.07%
• Amortization method	0.00%
• 1998 COLA	0.18%
• Investment gain	(0.61)%
• Change in assumption	0.64%
• Liability loss from experience	0.13%

Change in normal cost rate 0.47%

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Actuarial Contribution Rate, 6/30/98 6.15%

2-10



## Convergence of Rates

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	<u>1998</u>	<u>1997</u>
State/School	2004	2002
	5.32%	4.70%
Local	2002	2003
	3.40%	3.41%

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## Actuarial Contribution Rates

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<u>System</u>	<u>1998</u>	<u>1997</u>
State/School	6.15%	5.27%
Local	3.89%	3.86%
TIAA	1.81%	1.59%
KP & F	7.35%	7.36%
Judges	16.14%	14.38%
Combined	5.45%	4.83%

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## Recommended Contribution Rates

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<u>System</u>	<u>1998</u>	<u>1997</u>
State/School	4.58%	4.19%
Local	3.22%	2.93%
TIAA	1.81%	1.59%
KP & F	7.35%	7.36%
Judges	16.14%	14.38%
Combined	4.28%	3.94%

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## Shortfall

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<u>System</u>	<u>1998</u>	<u>1997</u>
State/School	1.57%	1.08%
Local	0.67%	0.93%
TIAA	0%	0%
KP & F	0%	0%
Judges	0%	0%
Combined	1.17%	0.89%

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