

MINUTES OF THE SENATE WAYS AND MEANS COMMITTEE

The meeting was called to order by Chairman Dwayne Umbarger at 10:30 A.M. on March 15, 2005 in Room 123-S of the Capitol.

All members were present.

Committee staff present:

Norman Furse, Revisor of Statutes
Jill Wolters, Senior Assistant, Revisor of Statutes
Alan Conroy, Director, Kansas Legislative Research Department
J. G. Scott, Kansas Legislative Research Department
Julian Efird, Kansas Legislative Research Department
Susan Kannarr, Kansas Legislative Research Department
Matt Spurgin, Kansas Legislative Research Department
Judy Bromich, Administrative Analyst
Mary Shaw, Committee Secretary

Conferees appearing before the committee:

Glenn Deck, Executive Director, Kansas Public Employees Retirement System
Dave Kerr
Jim Edwards, Governmental Relations Specialist, Kansas Association of School Boards
Andy Sanchez, Executive Director, Kansas Association of Public Employees
Mark Desetti, Kansas National Education Association
Jan O. Sides, State Employees Association of Kansas

Others attending:

See attached list.

Bill Introductions

Senator Taddiken moved, with a second by Senator Schodorf, introduction of a bill requested by Senator Wysong concerning the Kansas partnership for faculty of distinction program; earnings equivalent awards that (5rs1031). Motion carried on a voice vote.

Copies of the Kansas Legislative Research Department Budget Analysis Report for FY 2005 and FY 2006 were available to the committee.

Subcommittee budget report on:

Kansas Public Employees Retirement System Issues (Attachment 1)

Subcommittee Chairman Stephen Morris reported on the Kansas Public Employees Retirement System Issues subcommittee Recommendations, Issues and bills.

Kansas Public Employees Retirement System Issues - SB 281 (Attachment 2)

Subcommittee Chairman Stephen Morris reported on the Kansas Public Employees Retirement System - **SB 281**.

Senator Morris moved, with a second by Senator Wysong, to adopt the Kansas Public Employees Retirement System Issues Subcommittee Report Recommendations, Issues, and the Subcommittee report on **SB 281**. Motion carried on a voice vote. The Chairman noted that at the time the Senate gets **HB 2037**, the KPERs bills will be worked.

CONTINUATION SHEET

MINUTES OF THE Senate Ways and Means Committee at 10:30 A.M. on March 15, 2005 in Room 123-S of the Capitol.

The Chairman opened the public hearing on:

SB 281--KPERS, retirement plan for members first hired on and after July 1, 2007

Staff briefed the committee on the bill.

Copies of a information from the Kansas Legislator Briefing Book regarding the Kansas Public Employees Retirement System were distributed (Attachment 3). Copies of a chart, Kansas Public Employees Retirement System, Estimate of Employer Contributions & Debt Service Payments, State/School Group (in millions) were distributed (Attachment 4).

Glenn Deck, Executive Director, Kansas Public Employees Retirement System, testified in support of **SB 281** (Attachment 5). Mr. Deck presented information on the alternative retirement plan design in **SB 281**. He explained that the alternative retirement plan design would be for employees hired on or after July 1, 2007, only; it would not impact retirement benefits of current employees. Detailed information is provided in Mr. Deck's written testimony.

Senator Dave Kerr testified in favor of **SB 281** (Attachment 6). He addressed the concerns that if the contributions laws in place some years ago had remained unchanged, the KPERS Fund would never have reached equilibrium and the unfunded liability would have grown to overwhelming proportions. The following steps that were taken to "put the bloom back in the cheeks" of the KPERS Fund are:

- **HB 2014** was passed - over the next 33 years, it will increase employer contributions to KPERS almost \$6 million.
- One-half billion dollars in pension obligation bonds were sold.
- **SB 281** is the last bit step in the sequence of repairs to the KPERS Fund.

Senator Kerr urged support for **SB 281**, the last major step to fix a quiet but massive problem in the funding of employee pensions. He noted that the bill emerged from the Joint Committee on Pensions and Investments with a unanimous vote.

Jim Edwards, Governmental Relations Specialist, Kansas Association of School Boards (KASB), spoke in support of **SB 281** (Attachment 7). Mr. Edwards explained that KASB believes that **SB 281** is a step in the right direction to solve the long-term, unfunded actuarial liability issues surrounding KPERS for the majority of state, school and local employees. In closing, Mr. Edwards noted that these are major changes and they should strengthen the viability of the State General Fund and in the long run strengthen the actuarial liability of KPERS, but as with anything, major changes should be viewed cautiously.

Andy Sanchez, Executive Director, Kansas Association of Public Employees (KAPE), testified in opposition to **SB 281** (Attachment 8). Mr. Sanchez mentioned that KAPE cannot support **SB 281** because it brings about a monumental change in the retirement system for future public employees and future KAPE members. He also addressed a number of concerns detailed in his written testimony. In closing, Mr. Sanchez explained a survey taken of their members in 2001 revealed an unsatisfactory feeling toward a change to a defined benefit plan. He noted on another question, 56 percent expressed their displeasure with the funding the legislature has provided toward KPERS.

Mark Desetti, Kansas National Education Association (KNEA), spoke in opposition to **SB 281** (Attachment 9). Mr. Desetti noted that specifically, the KNEA opposes the following changes:

- the reduction of the multiplier to 1.5,
- the recommended mandatory defined contribution, and
- the expansion of retirement points from 85 to 90 and the higher retirement age.

Mr. Desetti expressed concern of being faced with a bill that would require people to work longer with less

CONTINUATION SHEET

MINUTES OF THE Senate Ways and Means Committee at 10:30 A.M. on March 15, 2005 in Room 123-S of the Capitol.

take-home pay for a smaller benefit in a system that has no provision for cost of living adjustments and the difficulty of the KNEA to support such a plan.

Jan O. Sides, representing the State Employees Association of Kansas (SEAK), testified in opposition to **SB 281** (Attachment 10). Ms. Sides mentioned that while SEAK commends the attempt to help future public servants, without a guaranteed COLA, they cannot support the bill. She noted that the bill does not help future employees face retirement issues and urged inclusion of a COLA in the plan.

There being no further conferees to come before the meeting, the Chairman closed the public hearing on **SB 281**.

The meeting adjourned at 12:10 p.m. The next meeting is scheduled for March 16, 2005.

SENATE WAYS AND MEANS
GUEST LIST

Date March 15, 2005

NAME	REPRESENTING
Julie Muench	SOB
Erik Sartorius	City of Overland Park
MIKE RUSSO	CITY OF OVERLAND PARK
Rob Woodard	KPERS
Don Willson	WSA
Charles Eaton	Wichita STATE Univ
Garret B. Moore	wichita state UNIVERSTY
Kim Fowler	Judicial Branch
Mike Muller	KGC
Jeff Bottenborg	Kansas Sheriffs Ass'n
Jan Siss	SEAK
Don Rezac	SEAK
Keith Haxton	SEAK
Dennis Phillips	KSCFF
Kp Peterson	KBOR
Mark Desetti	KNEA
Terry Forsyth	KNEA
Mary Pruitt	KBOR
Ellen Abbey	WSU Classified Employees
LEO HARR	" " "
Debra Brooks	" " "
Karen Watney	DeftA
Andrew Gaska	Senate Minority leader
Mark Tomb	LKM

SENATE SUBCOMMITTEE REPORT


Kansas Public Employees Retirement System (KPERs)

Recommendations on Issues and Bills

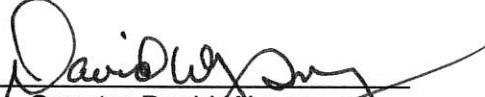
March 15, 2005



Senator Steve Morris, Chairperson



Senator Laura Kelly



Senator David Wysong

Senate Ways and Means
3-15-05
Attachment 1

SENATE SUBCOMMITTEE REPORT ON KPERS BILLS AND ISSUES

A. Review of Bills:

The Subcommittee reviewed the following bills and held hearings on March 8, 2005:

SB 20 would clarify the determination of KPERS State Group and School Group employer contribution rates by specifying that the rates will be calculated as if the two groups were combined in any year when the State rate is less than the combined rate.

Background: This bill was requested by the KPERS Board of Trustees and recommended by the Joint Committee on Pensions, Investments and Benefits. The fiscal note indicates that according to KPERS, without the clarifying language in SB 20, the state would contribute approximately \$1.0 billion more in employer contributions through the end of the amortization period in FY 2033. This projection is based on the KPERS current actuarial valuation adjusted for actual investment performance during calendar year 2004.

Recommendation: *The Subcommittee recommends SB 20 as introduced be passed.*

SB 21 would authorize the Director of Accounts and Reports to reissue outlawed KPERS warrants using a warrant reduction equal to administrative costs of reissuing the warrant, and authorizes the KPERS Board of Trustees to establish the administrative fee.

Background: This bill was requested by the KPERS Board of Trustees and recommended by the Joint Committee on Pensions, Investments and Benefits. Similar provisions are found in SB 46 that passed the Senate, but remains in the House Appropriations Committee. KPERS estimates administrative costs of \$1,000 to \$2,000 per year.

Recommendation: *The Subcommittee recommends SB 21 be amended to include the provisions of SB 46 as passed by the Senate that had a slight different maximum payment.*

SB 22 would allow participating employers to affiliate for optional group life insurance either on January 1 or on July 1.

Background: This bill was requested by the KPERS Board of Trustees and recommended by the Joint Committee on Pensions, Investments and Benefits. Affiliation under current law is limited to only once per year. KPERS does not anticipate any additional costs associated with this bill.

Recommendation: *The Subcommittee recommends SB 22 be amended to allow spouses and dependents of the KPERS members to purchase optional life insurance.*

SB 95. Reduces the length of service required for a surviving spouse to be eligible for retirement benefits when a member of KPERS or the Retirement System for Judges dies before reaching retirement age from 15 to 10 years of service.

Background: The bill was sponsored by Senator Lee and cosponsored by the other 39 members of the Senate. KPERS estimates additional unfunded actuarial liability would result from this bill totaling \$951,000, of which the State portion would be \$621,000 and the Local portion would be

\$330,000. In order to pay the additional costs over time, the additional first year contributions for the State would be \$41,100 and the Local would be \$21,800.

Recommendation: *The Subcommittee recommends SB 95 as introduced be passed.*

SB 99 would update current law regarding the Regents retirement plan for faculty and other unclassified employees of the State Board of Regents and the Regents institutions. The bill would allow the use of mutual funds offered by a bank or approved non-bank custodian under section 401(a) of the Internal Revenue Code as a financial instrument for investing retirement funds. The other changes in the bill would be technical compliance revisions in order to conform with federal requirements.

Background: This bill was requested by the State Board of Regents and recommended by the Legislative Educational Planning Committees. The bill resulted from comprehensive reviews by outside consultants to update the operation of the Regents retirement plan. The Board of Regents states that SB 99 would not have a fiscal effect on the state or any of its employees in the Regents system.

Recommendation: *The Subcommittee recommends SB 99 as introduced be passed.*

SB 279 would provide an additional long-term disability benefit to faculty and other unclassified employees of the State Board of Regents. In addition, the bill would modify current law regarding contributions that the Board makes in paying both the employer and employee amounts into the employee's retirement account if a staff member becomes disabled. The bill would address the contractual rights of current Regents retirement plan participants and would divide those disabled into four categories, depending upon length of service and benefits accrued. Current and future employees who do not fall into one of the new groups with accrued benefits would receive the pre-tax treatment for five years and thereafter receive the Regents employer and employee contribution payment as a post-tax disability benefit.

Background: This bill was requested by the State Board of Regents. Regents unclassified employees participate in the KPERS death and long-term disability benefits plan that is available to all other state employees who participate in the KPERS plan for retirement. The Regents make available an additional benefit to Regents unclassified employees since some retirement calculations only apply to other employees who participate in the regular KPERS retirement plan and not to members of the Regents retirement plan. Under current law, members of the Regents retirement plan who become disabled will have both the employee and employer contributions paid by their employer while disabled. Federal law passed in 2001 limits these additional contributions to disabled participants to a maximum of five years, depending upon their length of service and other accrued benefits. This bill was recommended by the Board of Regents two outside consultants who also reviewed the Regents retirement plan and suggested other amendments contained in SB 99. No fiscal note was available for this bill.

Recommendation: *The Subcommittee recommends SB 279 as introduced be passed.*

SB 291 would increase the current 0.6 percent employer contribution for the KPERS death and long-term disability benefits plan to 1.0 percent, effective July 1, 2005. The rate increase would raise employer payments for the State, school, and local groups that participate in the death and long-term disability benefits plan offered by KPERS.

Background: The bill was requested by the Governor and supported by the Secretary of Administration and Budget Director. The fiscal note addresses both the State and local governments that would be impacted by the rate increase.

This bill implements the Governor's FY 2006 budget recommendation to increase employer contributions to the KPERS death and long-term disability benefits plan. The fiscal note includes \$16.8 million, with \$13.6 million financed from the State General Fund, included in the *Governor's Budget Report* for FY 2006, and \$3.2 million for local units of government and other KPERS participating employers that are not part of the State and School groups.

The Subcommittee also reviewed the provisions of HB 2075 that was recommended by the Joint Committee on Pensions, Investments and Benefits to address the funding increase for the KPERS death and long-term disability benefits plan. HB 2075 as introduced would modify funding and benefits for active employees by increasing employer contributions from 0.6 percent to 0.8 percent of payroll effective July 1, 2005 and giving the KPERS Board of Trustees authority to make additional program adjustments in the plan. The bill would reduce the death benefit from 150 to 100 percent of salary for active or disabled employees and would allow employees to purchase the additional life insurance equal to 50 percent of salary.

The Subcommittee was concerned about the short-term fiscal solution in the bill as introduced and the reduction in benefits that also would be imposed by the bill as introduced. A longer term solution that would not have to be revisited with either another rate increase or benefits reduction would be a more practical solution. The Subcommittee was concerned by the reduction in life insurance from 150 percent to 100 percent. Although the industry standard for disability benefits is 60 percent, not 66 2/3 percent under current law, the Subcommittee agrees with that disability benefit reduction, but makes other recommendations to provide funding to hold the death benefit at 150 percent and to keep the program with a positive ending balance.

Recommendation: *The Subcommittee recommends SB 291 be amended and be passed. The amended bill concerning the KPERS death and long-term disability benefits plan would:*

increase employer contributions from 0.6 percent to 1.0 percent of payroll effective July 1, 2005, as recommended by the Governor;

expand the KPERS Board of Trustees' authority to administer the program within available funds and to adjust the plan design as needed, with the understanding that the disability benefit would be lowered from 66 2/3 percent to 60 percent;

provide that benefits for employees disabled prior to the effective date would remain unchanged, if the KPERS Board modifies the plan; and

maintain employer-provided basic life insurance at 150 percent of annual compensation.

B. Review of Other Issues:

The Subcommittee also reviewed the following issues at its meeting of March 9, 2005:

Federal Compliance Amendment. HB 2037 as introduced would adjust the maximum duration of KPERS long-term disability benefit payments for employees disabled after age 65 to ensure compliance with the federal requirements.

Background: This bill was requested by the KPERS Board of Trustees and recommended by the Joint Committee on Pensions, Investments and Benefits. The bill is on House General Orders and contains technical amendments that would need to be made in SB 291 which amends the same statutes as HB 2037. There is an increasing fiscal impact over time for this change, with estimate costs in FY 2006 - \$8,000; FY 2007 - \$30,000; and FY 2008 - \$57,000. Fully implemented the cost impact could reach \$250,000 in 15 to 20 years, according to the KPERS actuarial estimates.

Recommendation: *The Subcommittee recommends provisions from HB 2037 to be incorporated into SB 291 that modifies the KPERS death and long-term disability plan.*

Working After Retirement (Nurses at State Institutions). Under current law, state employees who return to work after retirement and are employed by any state agency would be subject to an earnings cap of \$15,000 in any calendar year. When a retired state employee reaches the \$15,000 threshold, then the employee either must stop working for the remainder of that calendar year or KPERS will cease paying the monthly retirement benefits for the remainder of that calendar year. The Subcommittee on SRS Institutions referred this issue for review as it pertains to nurses at SRS institutions.

Background: KPERS reports that the fiscal note would not be significant, according to the actuary, since there would be relatively few employees eligible if the proposal is to address only nurses at state institutions.

Recommendation: *The Subcommittee recommends that a three-year trial plan be implemented to allow nurses who retire or are retired from a state agency to be allowed to return to work after retirement without the \$15,000 cap if working for one of the following state institutions:*

Larned State Hospital, Osawatomie State Hospital, Rainbow Mental Facility, Kansas Neurological Institute, Parsons State Hospital and Training Center, the Kansas Soldiers Home at Fort Dodge, and the Kansas Veterans Home at Winfield.

The participating institutions would pay the actuarially calculated employer contribution rate to KPERS for each retired employee who is hired under this plan after retiring from KPERS.

Long-Term Funding of KPERS. Members discussed several other issues, including cost-of-living adjustments (COLAs) and health insurance costs for retired members and their beneficiaries.

Background: The Subcommittee reviewed the fiscal notes for SB 189, S 236, and SB 237.

The additional unfunded actuarial liability for SB 189 which would increase the KPERS death benefits from \$4,000 to \$5,000 for retired members: State - \$23.2 million; Local - \$7.7 million; additional first year contributions: State - \$2.2 million; Local - \$620,000.

Regarding SB 236 which would provide a one-time cost-of-living adjustment for KPERS retirees, their beneficiaries and disabled KPERS members: For retired members, additional unfunded actuarial liability of \$128.4 million for the State and \$39.9 million for local groups; additional first year contributions of \$13.6 million for the State and \$3.8 million for local employers; and for disability recipients: additional unfunded actuarial liability of \$3.4 million for the State and \$0.9 million for local groups; additional first year contributions of \$330,000 for the State and \$87,000 for local employers.

Regarding SB 237 which would pay a one-time monthly benefit equal to one-half of the monthly benefit payment for retired KPERS members, their beneficiaries and disabled KPERS members: For retired members: additional unfunded actuarial liability of \$20.5 million for the State and \$5.7 million for local groups; additional first year contributions of \$1.4 million for the State and \$0.5 million for local employers; and for disability recipients: additional contributions of \$950,000 for the State and \$250,000 for local employers.

Recommendation: *The Subcommittee recommends that the Joint Committee on Pensions, Investments and Benefits undertake an interim study during 2005 of the topic on long-term funding of KPERS as it relates to COLAs and health insurance costs for retired members and their beneficiaries.*

Consolidated Omnibus KPERS Bill. The Subcommittee considered whether individual bills or a combination of bills ought to be advanced.

Recommendation: *The Subcommittee recommends that all bills in this report receiving a favorable recommendation with the appropriate amendments should be consolidated into a substitute bill, preferable a House passed bill. Another bill (SB 281) is addressed separately in a different Subcommittee report and should not be included in the KPERS omnibus bill at this time.*

SENATE SUBCOMMITTEE REPORT

Kansas Public Employees Retirement System (KPERs)

SB 281

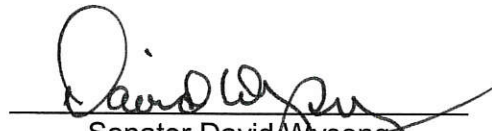
March 15, 2005



Senator Steve Morris, Chairperson



Senator Laura Kelly



Senator David Wysong

Senate Ways and Means
3-15-05
Attachment 2

SENATE SUBCOMMITTEE REPORT ON SB 281

SB 281 would establish a new retirement plan design for KPERS-covered employees who first would be employed after June 30, 2007. The plan design changes would not affect retirement benefits of employees who were first employed before July 1, 2007, by a KPERS participating employer. All of the current employees who are members of KPERS would continue in that plan. The current plan, however, would be closed to new employees hired after June 30, 2007, and they would be covered by the new retirement benefits plan instead of the KPERS plan currently in effect.

The proposed new plan would consist of a defined contribution component similar to the current plan and an optional defined contribution component which the current plan does not offer to KPERS members. By combining elements of two types of retirement contribution options, the new plan might be described as a hybrid plan. New plan features would include:

- Five year vesting;
- First day coverage;
- A retirement multiplier of 1.5 percent;
- Age 65 or 90 points normal retirement;
- A 4.0 percent employee contribution;
- An optional employee defined contribution plus employer match:
 - at 1.0 percent (employee) with a 0.25 percent match, or
 - at 2.0 percent (employee) with a 0.5 percent match (employer); and
- Additional optional employee contributions greater than 2.0 percent, without an employer match.

Background: The existing KPERS defined contribution plan requires 10 years for vesting; allows first day coverage only for members of the school group and a one-year waiting period of other state and local covered employees; provides a retirement multiplier of 1.75 percent; permits normal retirement at age 62 or 85 points; and requires employees to contribute 4.0 percent of salary. Salary deferral plans are available to most public employees as section 457 plans for state and local employees, or section 403(b) plans for school employees. Neither type of salary deferral plan is offered through KPERS, however.

SB 281 was recommended by Joint Committee on Pensions, Investments and Benefits at the conclusion of its 2004 interim study on KPERS long-term funding. The fiscal note from KPERS suggests that converting to the new plan would reduce long-term KPERS retirement funding for state and local units of government. KPERS estimates employer contribution savings through 2033 of \$1.8 billion for the state and \$728 million for local employers. There would be one-time implementation costs estimated by KPERS between \$520,000 and \$1.2 million, with \$260,000 to \$510,000 in FY 2006 and \$260,000 to \$510,000 in FY 2007. The annual on-going administrative costs are estimated by KPERS at \$56,200 beginning in FY 2007 and increasing to \$96,700 in FY 2008.

The Subcommittee was presented an overview by the KPERS Executive Director on March 9, 2005. During the briefing, potential issues and possible amendments to SB 291 were presented by KPERS. Some issues pertain to the new plan generally and plan design issues, other issues pertain to the defined benefit component of the plan, and still other issues pertain to the defined contribution component of the plan.

Hybrid Plan Design Issues. During drafting of the Joint Committee recommendations, the Revisor's of Statutes Office had concerns as to how the state correctional officers group was intended to be included in the new plan. Also during drafting, a question about interest rate earnings arose as to whether the current plan's 4.0 percent rate should be used, or some other rate used for person's who withdraw their contributions.

Recommendation: *The Subcommittee recommends that a group known as the state correctional officers should be included in the new plan, with normal retirement maintained at age 55 or age 60 for two subgroups, but that 90 points should be used for unreduced benefits instead of 85 points and that an actuarial reduction should be made in early retirements.*

Recommendation: *The Subcommittee recommends using an interest rate tied to the one-year Treasury bill rate, with a cap of 4.0 percent, for the new plan rather than using the 4.0 percent fixed rate used in the current plan.*

Defined Benefit Plan Design Issue. A question about retirement reduction factors was raised by KPERS. The Joint Committee's recommendation was for the new plan to include the full actuarial reduction if members retired prior to their earliest eligibility date for unreduced benefits. The current plan has a modified scale of actuarial reductions for early retirement that adjusts benefits. The KPERS actuarial reduction table for the new plan ranges from 10.0 percent at age 64 to 63.0 percent at age 55. The current plan's modified actuarial reductions ranged from 2.0 percent at age 61 to 41.0 percent at age 55. The current plan includes subsidies for early retirement since it allows for less than the full actuarial reductions that otherwise would have ranged from 10.0 percent at age 61 to 49.0 percent at age 55 had they not been modified by the Legislature in the current plan design.

Recommendation: *The Subcommittee recommends partial subsidies for early retirement, dependant upon length of credited services, with employees having 20 or more years of credited service when retiring to have a modified actuarial reduction in benefits. Employees with less than 20 years of credit service who retire early should be subjected to the full actuarial reduction in benefits. Several alternative tables will be provided by KPERS in guiding the consideration of this question as to implementation details.*

Defined Contribution Plan Design Issues. The Joint Committee recommended voluntary participation in the defined contribution component. The Subcommittee heard about problems with participation rates of younger employees in voluntary plans. The federal tax code also has limitations on the implementation of voluntary employee defined contributions which also might mitigate against voluntary participation and make a voluntary plan difficult to administer. Numerous issues would confront KPERS in implementing voluntary accounts. The Subcommittee examined mandatory employee participation in the defined contribution component and found it could address most of the issues that are found in voluntary plans.

Recommendation: *The Subcommittee recommends mandatory participation to replace voluntary participation in the defined contribution component design, with a 2.0 percent employee contribution rate for all participants in the new plan.*

General Recommendation Regarding SB 281. The Subcommittee was not able to spend adequate time reviewing the proposal and therefore does not make an overall recommendation about the bill.

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Retirement

Q-1

**Kansas Public
Employees
Retirement System**

Retirement

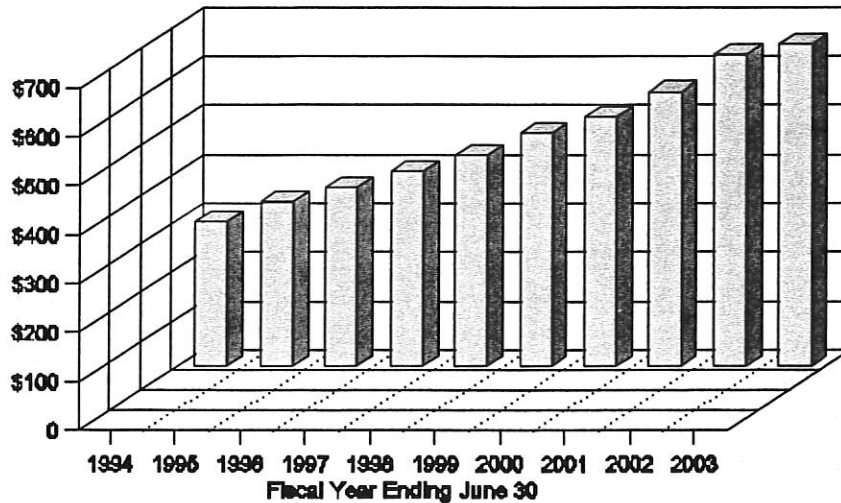
Q-1 Kansas Public Employees Retirement System

The Kansas Public Employees Retirement System (known as KPERS and referenced in this document as the Retirement System) administers three statewide plans: the State, School and Local Groups for regular state and local public employees, school and community college employees, Regents classified employees and certain Regents unclassified staff with pre-1962 service, and state correctional officers); the Kansas Police and Fireman's Retirement System (for certain designated state and local public safety employees), and the Kansas Retirement System for Judges (for the state's judicial system judges and justices). All coverage groups are defined benefit, contributory retirement plans and have as members most public employees in Kansas.

The primary purpose of the Retirement System is to accumulate sufficient resources in order to pay benefits. Retirement benefits paid by the Retirement System are considered off-budget and nonreportable expenses. The Governor recommended and the 2000 Legislature approved making retirement benefit payments nonreportable expenditures. Since the retirement benefit payments represent a substantial amount of money being distributed to retirees and their beneficiaries, the historical accounting of assistance paid is presented for informational purposes. Total benefits paid in FY 2000 exceeded \$500 million for the first time.

The number of retired members increased from 41,285 in FY 1994 to 57,597 in FY 2003. Benefits paid to retirants and their beneficiaries increased \$362 million over the same period. As increasing numbers of eligible employees retire, the average monthly benefit for new retirees also has increased, with 3,585 new retirants in FY 2003, with the average monthly benefit in excess of \$1,100 for new retirees.

Retirement Benefits Paid (In Millions)



The Retirement System also administers several other employee benefit and retirement programs: a public employee death and long-term disability benefits plan; an optional term life insurance program; and a legislative session-only employees retirement program. The Legislature also has assigned other duties to the agency in managing investments of moneys from three state funds: the Kansas Endowment for Youth Fund, the Senior Services Trust Fund, and the Treasurer's Unclaimed Property Fund.

A nine-member Board of Trustees is the governing body for the Retirement System. Four members are appointed by the Governor and confirmed by the Senate. One member is appointed by the President of the Senate. One member is appointed by the Speaker of the House. Two members are elected by System members. One member is the State Treasurer. The Board appoints the Executive Director who administers the agency operations for the Board.

The Retirement System manages assets in excess of \$10 billion. Annually, the Retirement System pays out more than \$750 million in total benefits and collects more than \$400 million in employer and employee contributions. The gap between current expenditures and current revenues is made up with funding from investments and earnings. The health of the Retirement System may be measured by its funded ratio, or the relationship between the promised benefits and the resources available to pay those promised benefits. In the most recent actuarial valuation, the funded ratio for the Retirement System was 75.2 percent. Due to strong investment returns, the status of the Retirement System generally improved in the last half of the 1990s. Recent changes in actuarial valuation procedures, coupled with lower investment returns, have reduced the funded ratio from a high of 88.6 percent in the 2000 actuarial valuation. With the decrease in funded ratio has been an increase in the unfunded actuarial liability, which was \$3.586 billion in the most recent actuarial valuation, compared with \$1.233 billion in 2000. This is the amount of shortfall when comparing the Retirement System assets with promised retirement benefits.

The Retirement System faces two challenges in terms of funding. The first challenge involves the retirement program and the second challenge involves the death and disability benefits program which also is administered by the agency. First, there is an annual gap between current revenue (contributions) and expenditure (benefits) that must be funded from investments. Second, there is a long-term shortfall in funding known as the unfunded actuarial liability, or the difference between assets and promised benefits. The Legislature has concentrated its attention on the retirement funding issue during recent sessions, but the death and disability funding issue will require attention during the 2005 Session because most of its reserves have been spent and revenue will be insufficient to maintain current benefits levels.

Retirement Funding

For the last several years, the Legislature, the Governor, and the Retirement System Board of Trustees have engaged in the development of a comprehensive plan to address the long-term retirement funding shortfall. Funding improvements made during the 2003 and 2004 legislative sessions represent key steps toward improving the Retirement System's financial condition and securing sufficient funds for future benefit payments. According to the Retirement System consulting actuary, as of December 31, 2003, "the System is in actuarial balance and the long-term funding of the System has improved dramatically."

Background of the Funding Shortfall

The 1993 Legislature authorized enhanced Retirement System benefits and adopted a 40-year payment plan that gradually increased employer contribution rates to pay for the enhancements. The incremental rate increases were designed so that the statutory contribution rates would converge with the actuarial rates required to fund the enhanced benefits. By 2000 and 2001, it became apparent that the incremental rate increases were insufficient. The Retirement System 2001 actuarial valuation showed that the unfunded actuarial liability (difference between the actuarial liabilities and the actuarial value of assets) had increased significantly, and future contribution rates were not projected to converge with actuarially required rates. At that time, the Retirement System actuary recommended that "action be taken to increase future contributions to a level which would restore the System to actuarial balance."

Funding Improvements

Following review of the 2001 valuation results, the Retirement System Board of Trustees, staff, and actuary began working closely with the Legislature's Joint Committee on Pensions, Investments and Benefits and the Governor's Office to develop a long-term funding plan. During the 2003 and 2004 legislative sessions, the following improvements were adopted as part of that comprehensive plan:

- The Legislature raised the statutory cap on annual employer contribution rate increases from 0.2% for the State and from 0.15% for local employers to 0.4% in 2006, 0.5% in 2007, and 0.6% in 2008.
- The Legislature authorized issuance of \$500 million in pension obligation bonds, and the Retirement System received net proceeds of \$440.2 million in March 2004.

- The Legislature split the Retirement System State and School group into two separate groups (the State employees group and the School employees group) for actuarial calculations and determination of employer contribution rates.
- The Retirement System Board of Trustees revised the actuarial components of the new funding plan by adopting the traditional Entry Age Normal actuarial cost method and a five-year asset valuation smoothing method.

Latest Actuarial Projections

The most recent actuarial valuation, dated December 31, 2003, found that the Retirement System's funded status has improved significantly. For example, the State employees group is projected to reach "equilibrium" in FY 2007. "Equilibrium" represents the point in time when the statutory employer contribution rate equals the required actuarial contribution rate. Also, given the higher statutory rate caps, the statutory and actuarial contribution rates are projected to converge in 2014 for the Local group and in 2025 for the School group.

As of December 31, 2003, the Retirement System funded ratio was 75 percent and the unfunded actuarial liability was \$3.6 billion for all groups (State, School and Local; KP&F; and Judges). As anticipated, the unfunded actuarial liability increased in 2003 primarily because the Entry Age Normal actuarial cost method was adopted. Unlike the previous method provided in state statute, employment age normal spreads benefit costs evenly over years of employment rather than backloading the costs.

Even with recent funding improvements, the dollar amount of the unfunded actuarial liability is projected to increase for a number of years before it begins to decline. This is due to the funding methodology selected in 1993, the gap between statutory and actuarial contribution rates for the School and Local groups, and the time-lag between the calculation and implementation of contribution rates. In addition, because of the asset smoothing methodology, investment losses deferred from 2001 and 2002 will be recognized in future actuarial valuations. Despite these projections, the Retirement System actuary states that "the System is expected to remain in actuarial balance if all actuarial assumptions are met going forward." Further, any future unfunded actuarial liability increases will be less substantial than they would have been absent the employer rate increases and issuance of the pension obligation bonds.

Future Steps

Significant challenges remain as employers begin budgeting for higher contribution rates that will increase payments for most units of Kansas government into the near future. Progress on the funding plan needs to be monitored closely and additional contributions or plan design changes may be necessary. All current and future Retirement System benefits are guaranteed by the State of Kansas, and any future shortfall in actual funding for benefits would have to be made up by direct state appropriations, if investment assets were not available. As long as investments provide the current funding needed to pay annual benefits, then the short-term issue does not pose a problem.

Kansas Public Employees Retirement System
Estimate of Employer Contributions & Debt Service Payments, State/School Group ^(a)
(in millions)

<u>Fiscal Year</u>	<u>Employer Contributions Pre HB 2014</u>	<u>Contributions HB 2014^(b)</u>	<u>Total Contributions</u>	<u>Debt Service Payments ^(c)</u>	<u>Total Payments</u>	<u>Annual Increase</u>
2005	\$ 168.13	\$ -	\$ 168.13	\$ -	\$ 168.13	
2006	\$ 180.26	\$ 7.11	\$ 187.37	\$ 10.00	\$ 197.37	\$ 29.24
2007	\$ 192.82	\$ 18.29	\$ 211.12	\$ 15.00	\$ 226.12	\$ 28.75
2008	\$ 204.27	\$ 33.61	\$ 237.87	\$ 26.08	\$ 263.95	\$ 37.83
2009	\$ 217.02	\$ 49.76	\$ 266.77	\$ 36.15	\$ 302.92	\$ 38.97
2010	\$ 230.26	\$ 66.69	\$ 296.95	\$ 36.15	\$ 333.10	\$ 30.18
2011	\$ 244.07	\$ 84.44	\$ 328.51	\$ 36.14	\$ 364.65	\$ 31.55
2012	\$ 258.50	\$ 103.07	\$ 361.57	\$ 36.14	\$ 397.71	\$ 33.06
2013	\$ 273.60	\$ 122.63	\$ 396.23	\$ 36.14	\$ 432.37	\$ 34.66
2014	\$ 289.48	\$ 143.22	\$ 432.70	\$ 36.14	\$ 468.84	\$ 36.47
2015	\$ 306.26	\$ 164.94	\$ 471.20	\$ 36.14	\$ 507.34	\$ 38.50
2016	\$ 324.03	\$ 187.91	\$ 511.93	\$ 36.13	\$ 548.07	\$ 40.73
2017	\$ 342.83	\$ 212.21	\$ 555.04	\$ 36.13	\$ 591.17	\$ 43.11
2018	\$ 362.75	\$ 237.95	\$ 600.71	\$ 36.13	\$ 636.84	\$ 45.66
2019	\$ 383.88	\$ 265.26	\$ 649.14	\$ 36.13	\$ 685.27	\$ 48.44
2020	\$ 406.32	\$ 294.29	\$ 700.61	\$ 36.13	\$ 736.73	\$ 51.46
2021	\$ 428.46	\$ 323.86	\$ 752.32	\$ 36.12	\$ 788.44	\$ 51.70
2022	\$ 453.07	\$ 344.05	\$ 797.12	\$ 36.11	\$ 833.24	\$ 44.80
2023	\$ 481.71	\$ 350.90	\$ 832.61	\$ 36.11	\$ 868.72	\$ 35.49
2024	\$ 509.95	\$ 353.50	\$ 863.45	\$ 36.11	\$ 899.56	\$ 30.83
2025	\$ 540.13	\$ 351.97	\$ 892.11	\$ 36.10	\$ 928.21	\$ 28.65
2026	\$ 572.40	\$ 346.47	\$ 918.86	\$ 36.09	\$ 954.96	\$ 26.75
2027	\$ 605.73	\$ 338.48	\$ 944.21	\$ 36.09	\$ 980.30	\$ 25.34
2028	\$ 641.65	\$ 325.91	\$ 967.55	\$ 36.08	\$ 1,003.63	\$ 23.33
2029	\$ 679.17	\$ 309.03	\$ 988.21	\$ 36.07	\$ 1,024.27	\$ 20.64
2030	\$ 718.65	\$ 286.15	\$ 1,004.80	\$ 36.05	\$ 1,040.85	\$ 16.58
2031	\$ 759.86	\$ 254.29	\$ 1,014.15	\$ 36.03	\$ 1,050.18	\$ 9.33
2032	\$ 802.25	\$ 207.79	\$ 1,010.04	\$ 36.02	\$ 1,046.05	\$ (4.13)
2033	\$ 842.35	\$ 135.16	\$ 977.51	\$ 36.00	\$ 1,013.51	\$ (32.54)
Totals	\$ 12,419.85	\$ 5,918.94	\$ 18,338.79	\$ 953.71	\$ 19,292.50	

^(a) Based on preliminary actuarial projections and calculations.

^(b) 2003 HB 2014 increased the statutory cap for state & school employer contribution increases from 0.2% annually to 0.4% in FY 2006, 0.5% in FY 2007 and 0.6% in FY 2008 and subsequent years.

^(c) State General Fund debt service payments on \$500 million pension obligation bonds issued in 2004.

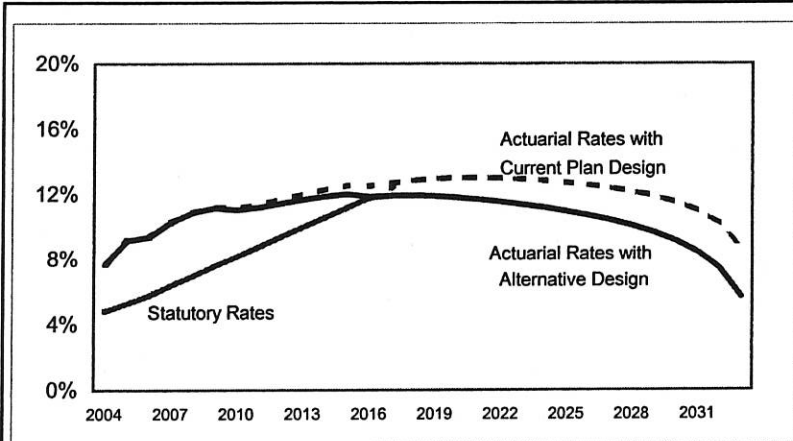
Senate Ways and Means
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Attachment 4

**Kansas Public Employees Retirement System
Cost Impact of Alternative Design (SB 281)**

	<u>State/School Group</u>		<u>Local Group</u>	
	<u>Current Plan</u>	<u>Alternative Plan</u>	<u>Current Plan</u>	<u>Alternative Plan</u>
Projected Equilibrium Rate	12.83%	11.90%	8.36%	7.98%
Projected Equilibrium Date	FY 2019	FY 2018	FY 2014	FY 2014
Total Employer Contributions (through 2033, estimated)	\$16.75 billion	\$14.9 billion	\$ 4.5 billion	\$ 3.7 billion
Savings versus Current Plan (through 2033, estimated)	n/a	\$ 1.8 billion	n/a	\$ 728 million
Present Value of Savings (through 2033, estimated)	n/a	\$ 377 million	n/a	\$ 140 million

Kansas Public Employees Retirement System Alternative Plan Design (SB 281)

Projected Employer Contributions & Contribution Rates for the KPERS State/School Group



Current Plan
Equilibrium = 12.83% in FY 2019

Alternative Plan Design
Equilibrium = 11.90% in FY 2018

	Employer Contributions (in millions)		
	Current	Alternative	Difference
2005	\$ 168.7	\$ 168.7	\$ -
2006	187.2	187.2	-
2007	210.1	210.1	-
2008	237.7	237.7	-
2009	266.6	266.6	-
2010	296.8	296.8	-
2015	471.0	471.0	-
2020	667.3	612.9	(54.4)
2025	780.9	680.5	(100.4)
2030	864.4	702.9	(161.5)
2033	827.1	604.8	(222.3)
Totals	\$ 16,750.5	\$ 14,944.1	\$ (1,806.4)

	Current Plan		Alternative Plan	
	Statutory	Actuarial	Statutory	Actuarial
2005	4.87%	7.78%	4.87%	7.78%
2006	5.27%	9.14%	5.27%	9.14%
2007	5.77%	9.36%	5.77%	9.36%
2008	6.37%	10.26%	6.37%	10.26%
2009	6.97%	10.87%	6.97%	10.87%
2010	7.57%	11.18%	7.57%	11.15%
2015	10.57%	12.29%	10.57%	11.85%
2020	12.93%	12.93%	11.88%	11.88%
2025	12.81%	12.81%	11.16%	11.16%
2030	11.85%	11.85%	9.64%	9.64%
2033	10.14%	10.14%	7.42%	7.42%

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Kansas Public Employees Retirement System

Alternative Retirement Plan Design – Senate Bill 281

Presented to the Senate Ways and Means Committee

•

March 15, 2005

Alternative Retirement Plan

Beginning in 2003, the Joint Committee on Pensions, Investments and Benefits requested that KPERS staff explore retirement plan alternatives that would help reduce long-term costs.

In response to this request, KPERS presented information to the Joint Committee during the 2004 interim.

In November 2004, the Joint Committee endorsed an alternative retirement plan designed to provide a basic defined benefit plan along with an optional defined contribution component (SB 281).

The alternative retirement plan design would be for employees hired on or after July 1, 2007 only; it would not impact retirement benefits of current employees.

Alternative Retirement Plan Design

	<u>Current Plan</u>	<u>Alternative Plan (SB 281)</u>
Defined Benefit Provisions		
▪ First Day Coverage (Immediate Membership)	School only	School, State and Local
▪ Vesting	10 years	5 years
▪ Retirement Multiplier	1.75%	1.50%
▪ Normal Retirement	Age 62 or 85 points	Age 65 or 90 points
▪ Early Retirement Reduction Factors	Subsidized for ages 55-61	No subsidy for ages 55-64
▪ Employee Contributions	4%	4%
▪ Employer Contributions	Based on actuarial valuation and statutory caps	Based on actuarial valuation and statutory caps
Defined Contribution Provisions		
▪ Employee Contribution	N/A	Optional contribution levels of 1%, 2%, and above 2% (to IRS limits)
▪ Employer Contribution (Match)	N/A	0.25% on employee 1% contribution 0.50% on employee 2% contribution No match for employee contributions above 2%
▪ Vesting	N/A	Employee vests in employer match at 5 years

Cost Impact of SB 281 Plan Design

	<u>State/School Group</u>		<u>Local Group</u>	
	<u>Current Plan</u>	<u>Alternative Plan (SB 281)</u>	<u>Current Plan</u>	<u>Alternative Plan (SB 281)</u>
Projected Equilibrium Rate	12.83%	11.90%	8.36%	7.98%
Projected Equilibrium Date	FY 2019	FY 2018	FY 2014	FY 2014
Total Employer Contributions (through 2033, estimated)	\$ 16.75 billion	\$14.9 billion	\$ 4.5 billion	\$ 3.7 billion
^(a) Savings versus Current Plan (through 2033, estimated)	n/a	\$ 1.8 billion	n/a	\$ 728 million
Present Value of Savings (through 2033, estimated)	n/a	\$377 million	n/a	\$140 million

^(a) Savings would continue after the current amortization period ends in 2033. For example, projected savings would be approximately \$260 million in FY 2034 and \$341 million in FY 2035.

Proposed Subcommittee Amendments

The Senate Ways and Means Subcommittee on KPERS Issues has recommended that SB 281 be amended as follows:

- Require employees hired on or after July 1, 2007, to participate in the defined contribution component of the alternative retirement plan. Under the voluntary defined contribution component currently provided in SB 281:
 - Due to federal tax code restrictions, employee contributions would be made to 457 and 403(b) plans with employer match deposited in a 401(a) plan.
 - Employer portion (401(a) plan) would be small for a number of years, affecting the ability to attract quality vendors, level of administrative expenses, and ability to offer low-cost investment options.
 - Based on other states' experiences, voluntary participation is low, particularly for younger employees.

Proposed Subcommittee Amendments (cont.)

The Senate Ways and Means Subcommittee on KPERS Issues also recommended the following amendments to SB 281:

- Establish interest earnings on employee contributions to the alternative plan's defined benefit component at the 1-year T-bill rate with a 4 percent cap.
- Apply the "90 point" rule and new early retirement rules for correctional officers who retire under the alternative plan.
- Modify the alternative plan's defined benefit early retirement rules to allow ongoing subsidization for employees with 20 or more years of service who elect to retire early. No subsidization would be provided for employees with less than 20 years of service who elect to retire early.

Alternative Retirement Plan Design

	<u>Current Plan</u>	<u>SB 281 Plan (with amendments)</u>
Defined Benefit Provisions		
▪ First Day Coverage (Immediate Membership)	School only	School, State and Local
▪ Vesting	10 years	5 years
▪ Retirement Multiplier	1.75%	1.50%
▪ Normal Retirement	Age 62 or 85 points	Age 65 or 90 points
▪ Early Retirement Reduction Factors	Subsidized for ages 55-61	Subsidized for ages 55-64 with 20 or more years of service only
▪ Employee Contributions	4%	4%
▪ Employer Contributions	Based on actuarial valuation and statutory caps	Based on actuarial valuation and statutory caps
Defined Contribution Provisions		
▪ Employee Contribution	N/A	Mandatory contribution level of 2%, Employees could elect to contribute more than 2% (up to IRS limits)
▪ Employer Contribution (Match)	N/A	0.50% on employee 2% contribution No match for employee contributions above 2%
▪ Vesting	N/A	Employee vests in employer match at 5 years

Cost Impact of Amended SB 281

	<u>State/School Group</u>		<u>Local Group</u>	
	<u>Current Plan</u>	<u>SB 281 Plan with Amendments</u>	<u>Current Plan</u>	<u>SB 281 Plan with Amendments</u>
Projected Equilibrium Rate	12.83%	12.05%	8.36%	8.07%
Projected Equilibrium Date	FY 2019	FY 2018	FY 2014	FY 2014
Total Employer Contributions (through 2033, estimated)	\$ 16.75 billion	\$15.2 billion	\$ 4.5 billion	\$ 3.9 billion
^(a) Savings versus Current Plan (through 2033, estimated)	n/a	\$ 1.5 billion	n/a	\$ 609 million
Present Value of Savings (through 2033, estimated)	n/a	\$319 million	n/a	\$ 115 million

(a) Savings would continue after the current amortization period ends in 2033. For example, projected savings would be approximately \$225 million in FY 2034 and \$300 million in FY 2035.

Appendices

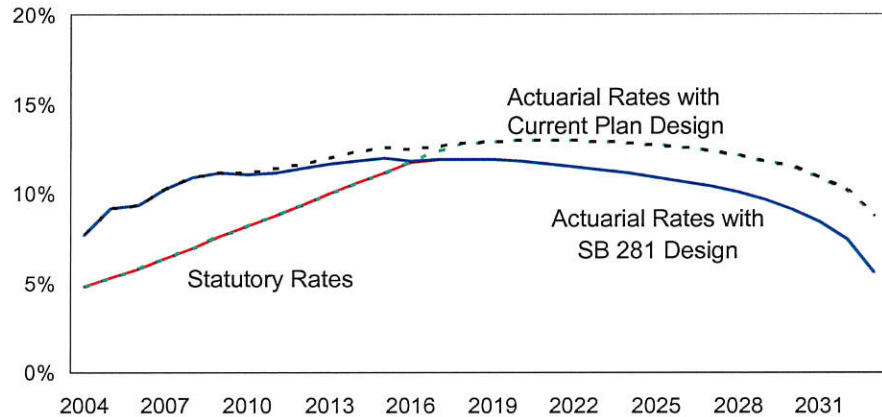
- Projected Employer Contributions & Contribution Rates
 - SB 281 Plan Design
 - Amended SB 281 Plan Design

- Early Retirement Reduction Factors
 - Early Retirement Reduction Factors for Alternative Plan

- Income Replacement Ratios
 - Retirement Plan Design Objectives
 - Comparison of Income Replacement Ratios
 - Income Replacement Ratios

SB 281 Plan Design

Projected Employer Contributions & Contribution Rates for the KPERS State/School Group



Current Plan
 Equilibrium = 12.83% in FY 2019

Alternative Plan Design (SB 281)
 Equilibrium = 11.90% in FY 2018

Employer Contributions (in millions)

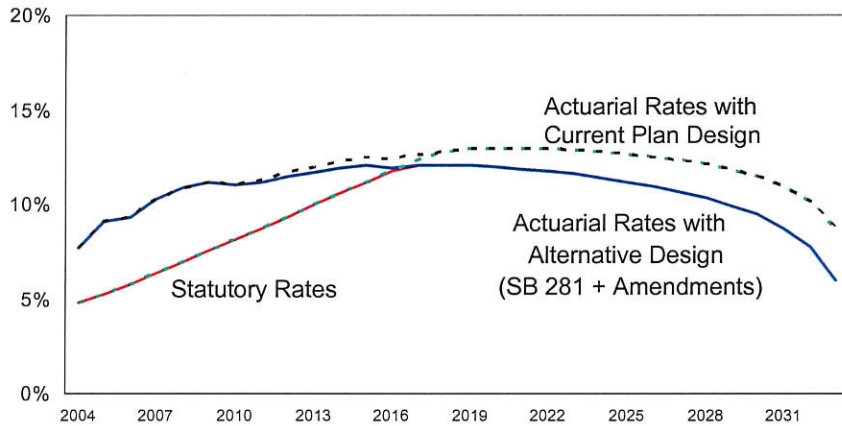
	Current	SB 281	Difference ^(a)
2005	\$ 168.7	\$ 168.7	-
2006	187.2	187.2	-
2007	210.1	210.1	-
2008	237.7	237.7	-
2009	266.6	266.6	-
2010	296.8	296.8	-
2015	471.0	471.0	-
2020	667.3	612.9	\$ (54.4)
2025	780.9	680.5	(100.4)
2030	864.4	702.9	(161.5)
2033	827.1	604.8	(222.3)
Totals	\$16,750.5	\$ 14,944.1	\$(1,806.4)

	Current Plan		SB 281 Plan	
	Statutory	Actuarial	Statutory	Actuarial
2005	4.87%	7.78%	4.87%	7.78%
2006	5.27%	9.14%	5.27%	9.14%
2007	5.77%	9.36%	5.77%	9.36%
2008	6.37%	10.26%	6.37%	10.26%
2009	6.97%	10.87%	6.97%	10.87%
2010	7.57%	11.18%	7.57%	11.15%
2015	10.57%	12.29%	10.57%	11.85%
2020	12.93%	12.93%	11.88%	11.88%
2025	12.81%	12.81%	11.16%	11.16%
2030	11.85%	11.85%	9.64%	9.64%
2033	10.14%	10.14%	7.42%	7.42%

(a) Savings would continue after the current amortization period ends in 2033. For example, projected savings would be approximately \$260 million in FY 2034 and \$341 million in FY 2035.

Amended SB 281 Plan Design

Projected Employer Contributions & Contribution Rates for the KPERS State/School Group



Current Plan
Equilibrium = 12.83% in FY 2019

Alternative Plan Design (SB 281 + Amendments)
Equilibrium = 12.05% in FY 2018

Employer Contributions (in millions)

	<u>Current</u>	<u>Alternative</u>	<u>Difference</u>
2005	\$ 168.7	\$ 168.7	-
2006	187.2	187.2	-
2007	210.1	210.1	-
2008	237.7	237.7	-
2009	266.6	266.6	-
2010	296.8	296.8	-
2015	471.0	471.0	-
2020	667.3	622.5	\$ (44.8)
2025	780.9	696.0	(84.9)
2030	864.4	726.1	(138.3)
2033	827.1	634.6	(192.5)
Totals	\$16,750.5	\$ 15,220.3	\$(1,530.2)

Current Plan

Alternative Plan

	<u>Statutory</u>	<u>Actuarial</u>	<u>Statutory</u>	<u>Actuarial</u>
2005	4.87%	7.78%	4.87%	7.78%
2006	5.27%	9.14%	5.27%	9.14%
2007	5.77%	9.36%	5.77%	9.36%
2008	6.37%	10.26%	6.37%	10.26%
2009	6.97%	10.87%	6.97%	10.87%
2010	7.57%	11.18%	7.57%	11.15%
2015	10.57%	12.29%	10.57%	11.94%
2020	12.93%	12.93%	12.06%	12.06%
2025	12.81%	12.81%	11.42%	11.42%
2030	11.85%	11.85%	9.95%	9.95%
2033	10.14%	10.14%	7.78%	7.78%

(a) Savings would continue after the current amortization period ends in 2033. For example, projected savings would be approximately \$225 million in FY 2034 and \$300 million in FY 2035.

Early Retirement Reduction Factors

Under current KPERS plan, members who retire early have their benefits reduced by 0.2% for each month between ages 60 and 62 plus 0.6% for each month between ages 55 and 60.

- These reductions are “subsidized” meaning that the reductions are less than they would be if benefits were actuarially reduced for early retirement.

The Senate Ways and Means KPERS Subcommittee has recommended amending SB 281 to continue to allow subsidization for those employees retiring with 20 or more years of service.

- Early retirement adjustments less than actuarially required but higher than current plan.

		<i>Monthly Benefit</i>
<i>Example:</i>	Employee retiring at age 60 with 20 years of service	\$ 780
	Employee retiring at age 60 with 19 years of service	\$ 589
	Difference	\$ 191
	\$ 50 attributable to difference of 1 year of service	
	\$141 attributable to early retirement reduction factor	

Example assumes final average salary of \$40,000

Alternative Plan's Early Retirement Factors

With the Senate Ways and Means KPERS Subcommittee's recommended amendments to SB 281, early retirement factors for defined benefit payments under the alternative retirement plan design would be reduced according to the following table assuming a monthly benefit of \$1,000 before the early retirement factor is applied.

<u>Age</u>	<u>Less Than 20 Years of Service</u>		<u>20 or More Years of Service</u>	
	<u>Reduction Factor</u>	<u>Monthly Benefit after Reduction</u>	<u>Reduction Factor</u>	<u>Monthly Benefit after Reduction</u>
55	62%	\$ 376	34%	\$ 664
56	58%	\$ 424	31%	\$ 688
57	55%	\$ 472	29%	\$ 712
58	48%	\$ 520	26%	\$ 736
59	43%	\$ 568	24%	\$ 760
60	38%	\$ 620	22%	\$ 780
61	34%	\$ 664	19%	\$ 810
62	25%	\$ 748	14%	\$ 856
63	17%	\$ 832	10%	\$ 904
64	8%	\$ 916	5%	\$ 952

Retirement Plan Design Objectives

Plan Design Objectives

- Provide benefits that, when combined with Social Security and personal savings, sustain the retiree's standard of living in retirement.
- Provide sufficient incentives to attract and retain high quality employees as part of total compensation and benefits package.

Sources of Retirement Income

- Social Security
- Employer-Sponsored Plans (KPERS defined benefit plan)
- Personal Savings

Income Replacement Target

- Generally recommend retirement income from all sources equal to 70 to 80 percent of pre-retirement income to permit retirees to maintain their lifestyle.
 - This percentage called “income replacement ratio.”

Comparison of Income Replacement Ratios

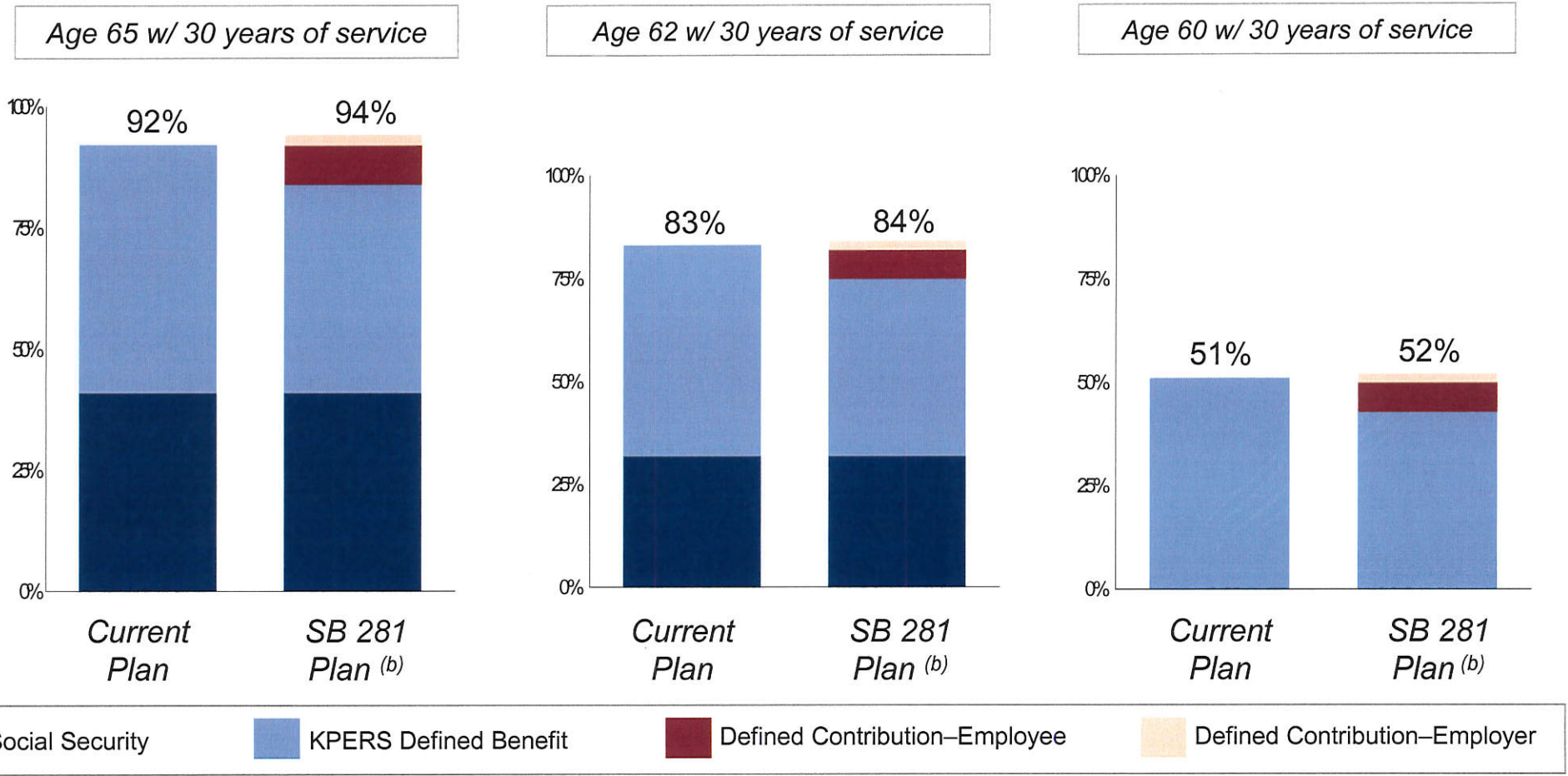
For employees who retire at age 62 or older with 25 to 30 years of service, replacement ratios under current and alternative plan designs are well within the 70 to 80 percent range with no additional personal savings.

- With 30 years of service and retirement at age 65, income replacement ratios of more than 90 percent.
- With 25 years of service and retirement at age 62, income replacement ratios of more than 70 percent.

With mandatory participation in SB 281's defined contribution component, alternative plan's income replacement ratios are comparable to ratios under the current plan.

Employees who retire before they are eligible for Social Security benefits (ages 55-61) have to fill a significant gap under both the current and alternative plans.

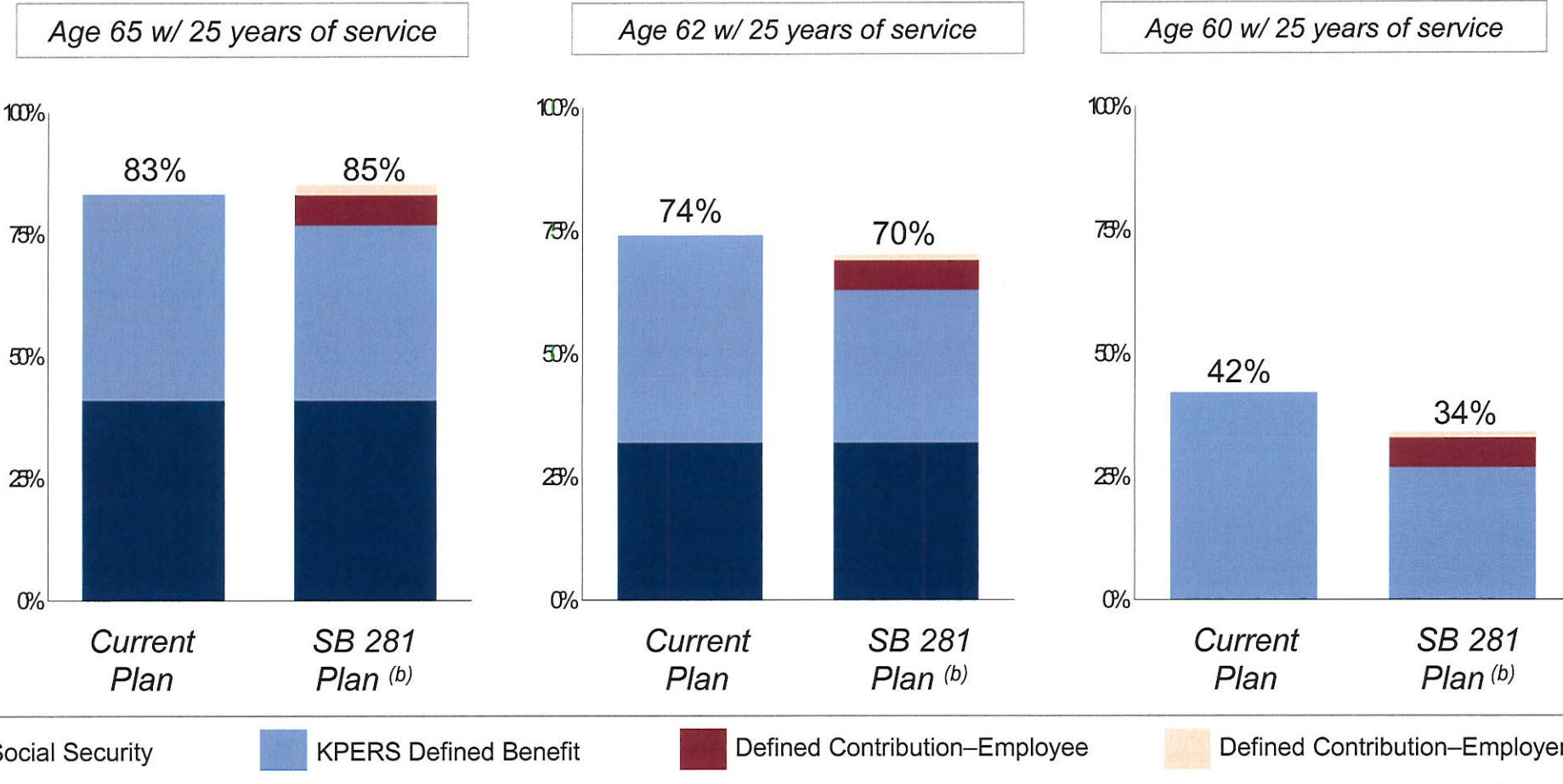
Income Replacement Ratios^(a)



(a) All projections assume final pre-retirement income = \$40,000

(b) All projections assume mandatory participation in SB 281 defined contribution plan.

Income Replacement Ratios^(a)



(a) All projections assume final pre-retirement income = \$40,000

(b) All projections assume mandatory participation in SB 281 defined contribution plan.

Testimony in Favor of SB 281

By Dave Kerr

March 15, 2005

Mr. Chairman and Members of the Senate Ways and Means Committee:

It is still a vivid memory that has us, your predecessors and I, sitting in this room reviewing charts which said that in as little as 4 to 6 years the Kansas Public Employees Retirement Fund would reach "equilibrium," a term usually defined as that point at which the contribution rate can remain stable and the fund will remain actuarially sound. That was in the late nineties and subsequent events proved those projections to be overly optimistic. In fact, if contribution laws in place at that time had remained unchanged, the fund would never have reached equilibrium and the unfunded liability would have grown to overwhelming proportions.

Some of the more important reasons those projections were not accurate are as follows:

- The major benefit improvements passed in the 1993 session proved to be far more expensive than anticipated. The 85 point full retirement option in particular was utilized more than expected by people only 54 to 57 years old which meant long and expensive retirements.
- After the previous KPERS actuary died and a new actuary took over, it was discovered that the Fund had liabilities to several thousand persons to whom no liability had been made a part of the projections.
- Advances in health care and nutrition meant people lived longer than previously projected so mortality tables were changed to reflect still longer retirements.
- The equity markets not only stopped going up for three years, they declined on a scale not seen since the Great Depression. (Last week was the fifth anniversary of the top in the Nasdaq Composite Average. It would still have to rise 150 percent to regain the lofty levels of March 2000.)
- Although infrequent, ad hoc benefit increases added to the problem because they were not a part of the original projections and when passed, they were not paired with a means to pay for them.

There were other, smaller reasons for the imbalance such as a group of unwise direct investments in the early nineties, but those were small in comparison to the ones noted above.

Three sessions ago we realized the situation had deteriorated to the point that corrective action had to be taken. True, the Fund had sufficient strength that it would be forty or fifty years before retiree checks would actually be endangered, but the longer we waited, the more it would cost.

So, we embarked on a bipartisan effort to put the bloom back in the cheeks of the KPERS Fund. First and most importantly, we passed HB2014. Over the next 33 years, it will increase employer contributions to KPERS almost \$6 billion. No longer will

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Attachment 6

contributions rise only two tenths of one percent of covered payroll as they have statutorily done since 1993. (This is not to imply that policy was inexpensive since it cost more than \$15 million more each year on top of increases due to salary increases.) Instead, payments will rise steeply until the State is paying over \$350 million per year more than it would have without the legislation.

Secondly, we sold one-half billion dollars in pension obligation bonds. Although generally misunderstood by the press, this measure was simply great for KPERS and their funded ratios and will probably save the State more than \$100 million over the next 33 years. Nonetheless, it does represent another \$36 million burden on the State General Fund each year.

As you can see, these first two steps were entirely in the form of additional financial commitments by the State and other employers. When each was passed, we made it clear that additional steps would be necessary and forthcoming. Even though they might take several years, they should be considered a connected series of "fixes."

Now before you is SB 281, the last big step in this sequence of repairs. Quite simply, it seeks some modest adjustments to benefits for those persons who will be hired July 1, 2007 and after. There are changes which are desirable from an employee's standpoint like a five year vesting period. And, there are changes to help the employer like an age 65 or 90 point normal retirement. On balance, the changes will save the State \$1.8 billion over the next 33 years and local government \$725 million. It also takes the first significant steps toward a partial defined benefit plan which I believe to be good for employees and employers alike.

In conclusion, I urge your support for SB 281, the third and last major step to fix a quiet but massive problem in the funding of employee pensions. Perhaps it is worthy of your notice that it emerged from the Joint Committee on Pensions and Investments with a unanimous vote.



Testimony on **SB 281**
before the
Senate Ways and Means Committee

by

Jim Edwards, Governmental Relations Specialist
Kansas Association of School Boards

March 15, 2005

Chairman Umbarger and Members of the Committee:

Thank you for the opportunity to appear today to support the efforts of the Kansas Public Employee Retirement System to solve the long-term, unfunded actuarial liability issues surrounding Kansas' retirement system for the majority of state, school and local employees. We believe that **SB 281** is a step in the right direction.

After the issue of the KPERS unfunded actuarial liability was presented to KASB's Legislative Committee in 2003, our organization adopted a policy at our Delegate Assembly which stated that the following goals should be addressed in any alternative plan: 1) the employers' cost of any retirement program or benefits mandated by the state should be fully and directly funded by the state; 2) KPERS should be a contributory system; and, 3) the Legislature should consider changes in the KPERS system to reduce the need for state general fund support provided that the benefits remain appropriate to attract and retain qualified employees.

We believe that **SB 281** meets most of these goals. Specifically, the proposed new plan would provide for:

- An optional employee defined contribution plus an employer match;
- A five-year vesting period;
- First-day coverage;
- A normal retirement at age 65 or 90 points;
- A retirement multiplier of 1.5 percent; and
- Implementation for those hired after July 1, 2007.

While these are major changes to the system, they should strengthen the viability of the State General Fund and in the long run strengthen the actuarial liability of KPERS. As with anything though, major changes should be viewed cautiously.

We would appreciate your favorable consideration of **SB 281**. I would stand for questions.

Senate Ways and Means
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Attachment 7

**The Kansas
Association of
Public Employees**

KAPE

Working to Protect Kansas Public
Employees since 1962

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**Working Together,
We Make A Difference!**



**Testimony
Before the Senate
Ways and Means Committee
SB 281**

March 15, 2005

Presented by Andy Sanchez

Executive Director, Kansas Association of Public Employees

Thank you Mr. Chairman and members of the committee, I appreciate the opportunity to participate and provide testimony against SB 281. KAPE can not support SB 281 because it brings about a monumental change in the retirement system for future public employees and future KAPE members.

KPERS has been under funded for years and lawmakers have taken commendable steps to shore up the system. Our organization was a supporter of the issuing of obligation bonds. However, it has been the feeling of members that such a project should have included some type of enhancement for retirees. This instance is no different.

Our members are encouraged that lawmakers are looking to member voluntary contributions into the retirement system. But as I stated, this is for future employees, and thus, no opportunity exists for future Cost of Living Adjustments (COLA's) of present employees.

We believe a defined contribution retirement plan is a step in the wrong direction for several other reasons. First, it deviates from the type of retirement plan that forty-eight states utilize, which is a defined benefit plan. Second, Workplace Economics, Inc. reports in their 2004 state employee benefits report that of the two states (Nebraska and Michigan) that adopted defined contribution plans as their primary retirement plan (in 1997), one has come back to add a cash balance option in 2002. This would provide for a guaranteed minimum benefit. This afterthought adjustment raises concerns.

Third, an extensive state survey to employees in 2001 asked two very direct questions about the retirement plan and the benefit package. Sixty-eight percent said they were satisfied with the benefits they receive.

Last, a survey of our members also in 2001 revealed an unsatisfactory feeling toward a change to a defined benefit plan. On another question fifty-six percent expressed their displeasure with the funding the legislature has provided towards KPERS.

Thank you

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Attachment 8



Mark Desetti, testimony
Senate Ways and Means Committee
March 15, 2005
SB 281

Thank you for the opportunity to share our concerns about **Senate Bill 281**, the proposal for a two-tiered KPERS system.

While we understand the impetus for this bill, we oppose the proposed changes to the retirement system it contains.

In the teaching profession, Kansas is at a crossroads. We have a very high percentage of our teachers over the age of fifty and rapidly approaching retirement, enrollment in teacher training programs has been declining for several years, our attrition rate is around 10% per year for the first three years of teaching, and teacher salaries sit at 41st in the nation and regionally are behind all of our neighbors except Oklahoma. Teacher compensation in Kansas trails Nebraska, Iowa, Colorado, Texas, and Arkansas and is about even with Missouri. Health care costs continue to skyrocket and 16 Kansas school districts either offer no health insurance plan at all or pay nothing towards the premium. So at a time when it is becoming more and more difficult to entice young people into the teaching profession, we are faced with a bill that tells them their retirement system will provide a smaller benefit for more years of service than their older colleagues receive.

Specifically, we oppose the following changes:

- the reduction of the multiplier to 1.5,
- the recommended mandatory defined contribution program, and
- the expansion of retirement points from 85 to 90 and the higher retirement age.

Collectively these three provisions show that new employees will take home a smaller percentage of their paychecks and work longer for a smaller benefit. We think that's wrong.

The reduction in the multiplier is very troubling. Back in November in a report to the Joint Committee on Pensions, Investments and Benefits, Glenn Deck said, "Current plan benefits (are) below average for peer state retirement benefits." Indeed, our current multiplier is on the low end of comparisons with peer systems. Reducing the multiplier puts us in the bottom.

Senate Bill 281 tries to offset this reduction with the defined contribution plan. As proposed in the bill, this is a voluntary plan but the subcommittee is recommending that this be a mandatory plan. It is my understanding that federal law does not allow a voluntary defined contribution plan within our system. In essence what this means is that the employee contribution will increase from 4% to either 5 or 6%. By withholding more of one's salary, the employee can pay for the reduction in the multiplier. Unfortunately, given low teacher salaries and the fact that many beginning teachers are indeed working paycheck to paycheck, this simply means less income.

KPERS has provided you with information on the income replacement levels under the current system and this proposed system. We should point out however that their estimates are based on three "ifs:" *an expected rate of return, no changes to the social security system, and full participation in the defined*

contribution plan. While switching to a mandatory defined contribution plan takes care of one of the assumptions, current proposals on social security being touted by President Bush will change the underlying assumptions and, while KPERS investments have done well historically, the assumption that these defined contributions will do as well is dependent on the skill of the investor.

We are faced then with a bill that will require people to work longer with less take-home pay for a smaller benefit in a system that has no provision for cost of living adjustments. I hope you understand our difficulty in supporting such a plan.

All this said, we understand the dilemma you are in. The challenge before you is indeed awesome. We applaud the attention you are giving to KPERS and hope that you will consider the impact of each individual change on the ability of the state and our schools to recruit and retain a highly qualified, skilled workforce.



STATE
EMPLOYEE
ASSOCIATION
KANSAS

**Testimony to the
Senate Ways & Means Committee
by
Jan O. Sides
State Employees Association of Kansas
March 15, 2005
Regarding
SB 281 – Retirement Plan for New Employees after July 1, 2007**

Mr. Chairman and members of the Committee, thank you for the opportunity to provide testimony on this bill regarding a retirement plan for new employees. My name is Jan O. Sides, and today I am representing the State Employees Association of Kansas (SEAK).

We continue to hear about retirees that have to go back to work to make ends meet due to inadequate increases in KPERS benefits, small increases in Social Security that is canceled out by increases in Medicare Part B premiums, retirants' escalating premium cost for the state Health Care Plan, and poor market returns over the past couple of years that have reduced some savings/retirement funds of retirants by as much as 50%. These retirement resources have been referred to as "a three legged stool" retirement approach – unfortunately all three legs are getting shorter each year and the approximately 60,000 retirees under KPERS still have to deal with inflation.

Since 1994, KPERS has had only one COLA and only one 50% monthly benefit check for retirees. We understand the problem with state finances, but the seniors that have worked for the taxpayers of Kansas for years are now struggling to keep up with the rising cost of living. Many are losing the battle each year!

We commend your attempt to help future public servants, but without a guaranteed annual COLA we can not support this bill. As presently proposed this bill only helps reduce the burden on the State General Fund. It does not help future employees face retirement issues. We sincerely appreciate your consideration on this issue and urge you to include a COLA in the plan.

Thank you for you time and I stand for questions.