MINUTES

JOINT COMMITTEE ON PENSIONS, INVESTMENTS, AND BENEFITS

October 14, 2008
Room 545-N—Statehouse

Members Present

Senator Steven Morris, Chairperson
Representative Richard Carlson, Vice-Chairperson
Representative Geraldine Flaharty, Ranking Minority Member
Senator Anthony Hensley
Senator Laura Kelly
Senator Ruth Teichman
Senator Dwayne Umbarger
Representative Margaret Long
Representative Sharon Schwartz
Representative Arlen Siegfreid

Staff

Alan Conroy, Kansas Legislative Research Department
Julian Efird, Kansas Legislative Research Department
J. G. Scott, Kansas Legislative Research Department
Mike Steiner, Kansas Legislative Research Department
Gordon Self, Office of the Revisor of Statutes
Melissa Doeblin, Office of the Revisor of Statutes
Gary Deeter, Committee Secretary

Conferees

Glenn Deck, Executive Director, Kansas Public Employees Retirement System (KPERS)
Vince Smith, Chief Investment Officer, KPERS
Patrice Beckham, KPERS Actuary, Milliman USA
Ed Klumpp, Kansas Coalition of Public Retirees

Morning Session

Glenn Deck, Executive Director, Kansas Public Employees Retirement System (KPERS), provided follow-up information from previous meetings (June and September) regarding working after retirement (Attachment 1). He outlined three areas to be considered: re-employment of retirees through third-party contractors; options for modifying the earnings limitations; and incentives to retain employees eligible to retire.

Regarding a district hiring a teacher through a third-party contractor, Mr. Deck said that if the contractor is truly independent under Internal Revenue Service (IRS) rules, then the KPERS working-after-retirement restrictions do not apply. He noted that 638 retired teachers were reemployed with salaries over $20,000 and that 33 were hired through a private contractor. He said that he is not aware of any other state prohibiting third-party contracts for teachers or school administrators. Responding to a question, Mr. Deck referenced information about restrictions by teacher retirement systems in Texas, Georgia, and Montana.

Mr. Deck summarized three different options that have been suggested for addressing the earnings limitation issue: remove the $20,000 earnings limitation and revise the break-in-service requirement; remove the earnings limitation for certain retirees meeting specific requirements of age and points; or lift the earnings limitation for critical teaching positions that meet certain criteria (Attachment 1, page 7).

Because of the IRS code governing retirement systems, Mr. Deck said that KPERS must stipulate a break-in-service requirement for retirees who wish to be reemployed. He said the present 30-day KPERS requirement is a minimum recognized by the IRS. If the issue is to be addressed by legislation, he suggested lifting the $20,000 earnings cap and stipulating a six-month break in service for members who retire before age 62 and a 30-day break for those retiring after age 65. He provided relevant information regarding Nebraska, North Carolina, and Georgia policies.

Mr. Deck addressed one option suggested by the United School Administrators: lift the $20,000 earnings limitation for any rehired retiree who is re-employed by the same employer if, at the time of retirement, the member is age 62 or older and has accumulated 95 points (age plus years of service). The employer would be required to pay both the employee and employer contributions. He referenced estimates that show, depending on permutations of the plan, the total annual cost would range from $1.7 million to $5.4 million. Responding to a member's question, Mr. Deck said if legislation were proposed for this option, he would recommend a sunset provision of five years.

Explaining the effect of lifting the earnings limitation to alleviate teacher shortages with the school district paying both the employer and employee contribution, Mr. Deck said the Unfunded Actuarial Liability (UAL) would increase between $17.6 and $33.4 million; the cost to school districts would range from $1.55 to $2.79 million annually. Responding to a question, Mr. Deck said KPERS does not keep data on districts that provide incentives for early retirement, and pointed out that the Department of Education does collect such data.

Commenting on incentives proposed by conferees to retain retirement-eligible employees who are retirement eligible, Mr. Deck provided preliminary analysis of two approaches. The first would apply a multiplier of 1.90 percent to years beyond 90 points; the plan would cost about $700,000. The second would apply a multiplier of 1.85 percent to all years of service if the member retires with 90 points or a multiplier of 1.90 percent for a member with 95 points. He said the cost would be in the $20-plus million range. Answering a question, Mr. Deck said both options would remove the $20,000 earnings cap.

Vince Smith, KPERS Chief Investment Officer, addressed the current financial crisis by referring members to page 7 of Attachment 2, saying that the market experiences periodic downturns from which previously it has always recovered. He said the present situation represents a crisis of confidence and credit freeze.

The KPERS investment portfolio on September 30, 2008, had an unaudited estimated market value of $11.8 billion. Total return for calendar year 2008 to that date was a negative 14.6 percent. A historical chart of KPERS investment returns (Attachment 2, page 7) demonstrates how the

KPERS net asset value has increased over the same time period (Attachment 2, page 8), even when suffering period decreases, as in the present situation.

Noting that because of the KPERS long-term investment strategy, the portfolio is diversified in order to reduce risk while maximizing returns. He said that about 55.0 percent of KPERS investments is in the equity markets, while fixed income comprises another 22.0 percent. Responding to questions, Mr. Smith said he anticipated at least another three to four months of volatility before the markets hopefully stabilize. Mr. Deck noted that if the downturn persists into calendar year 2009, then the issue of addressing the contribution rate of increase should be considered during the 2010 Legislative Session.

Mr. Deck continued by addressing the current statutory cap on the KPERS employer contribution rate increases, illustrating the interaction of the rate of return and the actuarial contribution rate to reach equilibrium under different assumptions, including examples based on a positive 8.0 percent return, a negative 8.0 percent return, and a negative 14.5 percent rate of return on investments (Attachment 3). The negative 14.5 percent investment return example, which parallels the year-to-date figure of a negative14.6 percent return, indicates that the statutorily capped increases in employer contribution rates for state and school groups will never reach the Actuarial Required Contribution (ARC) during the period through 2033. Other examples show the impact of increasing the employer contribution rates to bring the ARC into balance before 2021.

In following up a question from a previous meeting, Patrice Beckham, KPERS Actuary, Milliman USA, reviewed an evaluation of salary increases for state employees (Attachment 4). She said that projections of salary increases are made by taking the increases of the previous year and estimating a percentage increase for the coming year. The estimate for 2007 was 6.1 percent. The actual increase in 2007 was 8.7 percent. However, if the unanticipated bonus of $860 is excluded, the increase in salaries is 6.4 percent. Ms. Beckham concluded that projections were nearly aligned with actual increases and confirmed the initial assumptions regarding salary increases.

Next, the Committee topic focused on cost-of-living increases. Ed Klumpp, representing the Kansas Coalition of Public Retirees, addressed cost-of-living adjustments (COLA) for KPERS retirees (Attachment 5). He stated that the Coalition supports a 3.0 percent annual COLA. He acknowledged constraints impinging on such a recommendation: a tight state budget and the current economic crisis, but urged members to consider the needs of retirees. He recommended that the COLA be formulated within an integrated plan based on consistency rather than fairness, that the plan be inclusive, and that the plan begin at whatever percentage funds can support but move toward a 3.0 percent annual COLA. He noted that after bonds are paid from the Expanded Lottery Act Revenue Fund, there would be available an estimated $36 million, which could be funneled into a permanent COLA.

The minutes for the September 15-16 meeting were approved. (Motion by Representative Siegfreid; seconded by Representative Schwartz).

The next meeting is scheduled for Tuesday and Wednesday, December 2-3, 2008.

Prepared by Gary Deeter
Edited by Julian Efird

Approved by Committee on:

December 2, 2008
(Date)

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