Approved: March 2, 2011
Date

MINUTES OF THE SENATE WAYS AND MEANS COMMITTEE

The meeting was called to order by Chairperson Carolyn McGinn at 10:30 a.m. on January 18, 2011, in Room 548-S of the Capitol.

Senators Schmidt and Emler excused

Committee staff present:
Jill Wolters, Office of the Revisor of Statutes
Daniel Yoza, Office of the Revisor of Statutes
David Wiese, Office of the Revisor of Statutes
Alan Conroy, Director, Legislative Research Department
J. G. Scott, Chief Fiscal Analyst, Legislative Research Department
Aaron Klaassen, Senior Fiscal Analyst, Legislative Research Department
Dorothy Hughes, Fiscal Analyst, Legislative Research Department
Brea Short, Intern, Senator McGinn's Office
Jan Lunn, Committee Assistant
Josh Lewis, Chief of Staff

Conferees appearing before the Committee:
Glenn Deck, Executive Director, Kansas Public Employees Retirement System (KPERS)

Others attending:
See attached list.

Kansas Public Employees Retirement System (KPERS) Overview

Mr. Deck indicated the KPERS system partners with state and local government employers to provide retirement, disability and survivor benefits to members and beneficiaries. KPERS administers three statewide, defined benefit plans for public employees: public employees (state, local, and school), police and fire, as well as judges (Attachment 1).

Mr. Deck outlined plan basics, membership, contributions and benefits, assets, and investment returns. He provided a historical perspective on long-term funding and addressed previous funding actions. The key finding in the 12/31/09 valuation measurement indicates the funded ratio per group is:

- 78% for the state employee group
- 56% for the school employee group
- 64% for the local employee group
- 76% for the fire and police employee group
- 82% for the judges employee group

A funding ratio of 80% and rising is generally considered adequate funding for a public sector defined benefit plan. A plan with a funded ratio of 60% or below can be considered at significant risk and in need of remedial action to stabilize funding. Mr. Deck emphasized the significance of the unfunded actuarial liability (UAL) in the School Group with no projected change in employer contributions and an annual investment return of 8 percent. The total system actuarial funded status is 64%.

Senator McGinn asked what drove benefit plan enhancements in 1993. Mr. Deck explained many surrounding states' benefit plans included eligibility under the "85-point rule (when the sum of a member's age and years of service credit equals 85). In addition, there was an increase in the retirement formula factor and a 15 percent (one-time) cost-of-living (COLA) increase for retirees. He added that the funding plan mechanisms implemented have resulted in the issues seen today.

Senator Taddiken inquired what actuarial required contribution rate (ARC) is currently paid. Mr. Deck responded that the current rate is 8.17 percent for FY 2011.

Responding to questions from Senator Kelly, Mr. Deck explained the actuarial cost methodology used involves "smoothing or averaging" over a 5-year period. The

purpose is to stabilize the employer contribution rate. Therefore, investment gains or

losses change annually based on these calculations. Current market valuation basis compares liabilities to the current market value of the fund instead of the "smoothed or averaged" value.

Senator Lee inquired about the impact on the fund if interest rates begin to significantly increase. Mr. Deck indicated if that were to happen bond prices would likely decrease resulting in a compressed bond portfolio. Senator Lee wanted to know why the School Group is so much more out of actuarial balance than the others. Mr. Deck explained there were several factors involved: a.) the School Group came into KPERS without assets and b.) the systematic under-contribution rate in the last sixteen years.

Senator Teichman asked if all groups were combined, when actuarial balance would be achieved. Mr. Deck responded that it would be difficult to combine all the funds, but if the State, Local, and School Groups were combined, actuarial balance would be achieved in approximately 2031-2032.

Senator Huntington requested more information regarding the statutory cap. Mr. Deck reported a statutory cap of 0.1 percent was placed on annual increases to employer contribution rates in 1993; this decision was based on the concern relative to the benefit cost of the plan and the calculated contribution rate.

Mr. Deck described various funding solution options that were presented to the Joint Committee on Pensions, Investments and Benefits during the 2009 Interim. He outlined **SB 564** and **House Sub for HB 2400**; both bills had hearings (2010 Session) but neither passed out of its house of origin. **HB 2751** was introduced several days prior to adjournment during the 2010 Session; no action/hearing was taken on this bill. The Joint Committee again reviewed long-term funding issues during the 2010 Interim; they recommended updating and reintroducing **SB 564** and **HB 2400.** Committee members heard a brief synopsis of other states' responses to long-term funding.

Senator Teichman questioned why this potential legislation would not substantially improve KPERS' funded ratio for a number of years. Mr. Deck responded that while contributions are important in the long-term, the funded ratio is not raised immediately. The only way to raise the funded ratio quickly is through a bond issue or very strong investments.

Senator Kelly requested clarification on **HB 2751**; Mr. Deck indicated this bill would create a Tier 3 for future employees. Under **HB 2751**, Senator Kelly inquired whether calculations were made. Mr. Deck responded that fiscal notes were created for this bill, but he would furnish that information at a later time.

Mr. Deck indicated that while **HB 2751** created a Tier 3 KPERS defined contribution retirement plan for employees hired after June 30, 2012, it did not ramp up contributions. If a policy choice were to be made, legislation should address the unfunded liability by increasing the employer/employee contribution rates as well.

Senator Lee inquired whether it would be possible to commingle funds. Mr. Deck responded that it is impossible to commingle these funds; Internal Revenue Service (IRS) rules and regulations are followed in administering these funds. Mr. Deck discussed legal ramifications for revising or changing plan rules.

Senator Huntington asked what the cap would need to be for employer contributions to achieve actuarial balance. Mr. Deck explained that to be in actuarial balance would be the ideal; the shortest span of time between the statutory and ARC rates meeting is most desirable. Senator Huntington questioned whether revising the vesting period would be valuable to consider. Mr. Deck indicated that revision of the vesting period would not impact the issue significantly.

Mr. Deck further elaborated on the effect of COLAs. When funding problems began in the mid-90's, the decision was made not to award automatic COLAs to retirees. In the KPERS' materials, emphasis has been placed on saving through other investment

avenues.

Senator Masterson asked whether there is a plan to offer current employees an opportunity to "buy-out" their KPERs benefits and move it into a Tier 3 system. Mr. Deck indicated those types of projections had not been performed at this time, but a letter ruling from the IRS would be required.

Senator Taddiken questioned whether the Legislature had set a different contribution rate for various funds. Mr. Deck responded that a different statutory contribution rate is possible for different funds.

Senator Vratil asked if COLA calculations have been made the last several years; Mr. Deck replied that COLA calculations are routinely done. If an annual COLA of 3 percent were awarded, it would raise the UAL several billion dollars.

In summary, Mr. Deck indicated current benefits are safe for a period of time, ability to withstand future economic downturns is compromised, investment returns alone cannot correct the problem, legislative action is necessary to address the funding shortfall, and passing long-term funding legislation in 2011 is essential.

The meeting was adjourned at 12:02 p.m.