Approved: April 26, 2011

(Date)

MINUTES OF THE SENATE WAYS AND MEANS COMMITTEE

The meeting was called to order by Chairperson Carolyn McGinn at 10:30 AM on Tuesday, January 31, 2012 in 548-S of the Capitol.

All members were present.

Committee staff present:

Jan Lunn, Committee Assistant
Melinda Gaul, Chief of Staff, Senator McGinn's Office
Eli Johns, Intern, Senator McGinn's Office
Alan Conroy, Director, Legislative Research Department
J. G. Scott, Chief Fiscal Analyst, Legislative Research Department
Michael Steiner, Senior Analyst, Legislative Research Department
Bobbi Mariani, Fiscal Analyst, Legislative Research Department
Jill Wolters, Office of the Revisor of Statutes
David Wiese, Office of the Revisor of Statutes
Daniel Yoza, Office of the Revisor of Statutes

Conferees appearing before the Committee:

Senator Jeff King
Rebecca Proctor, Member of KPERS Study Commission

Others attending:

See attached list

Upon the request of Senator Kelsey, *Senator Vratil moved introduction of 12rs1692 concerning reduction of sales tax and income tax rates; Senator Huntington seconded the motion, which carried on a voice.*

Senator Huntington moved introduction of 12rs2004 concerning reporting of abuse and neglect of children; Senator Kelly seconded the motion, which carried on a voice vote.

Staff overview on **SB 338—Enacting the Kansas public employees retirement system act of 2014**

David Wiese, Office of the Revisor of Statutes Office, briefed committee members on the new retirement plan design recommended by the Kansas Public Employees Retirement System (KPERS) Study Commission (Attachment 1). The plan is a two-part design with:

1. An employee directed account with a mandatory contribution of 6 percent of the employee's compensation, and
2. An employer annuity account in which the employer contribution would be placed.

Other key components of the bill were reviewed.

Mr. Wiese noted that in new Section 18, subsection b, the bill contains language describing how vested legislators' retirement benefit would be calculated under **SB 338**. Non-vested legislators would come under the new plan on January 1, 2014.

Report on KPERS Study Commission by Senator Jeff King, Chairman:

Senator Jeff King, Chairperson of the KPERS Subcommittee, reviewed the reform proposals (Attachment 2):

- Employees who will be vested by January 1, 2014 (with five years of KPERS-eligible service);
- New hires and non-vested employees as of January 1, 2014;
- State funding of KPERS; and
- Legislative KPERS

Senator King noted that for vested employees, the study commission made no recommended changes other than those passed last year in **Senate Substitute for HB 2194**. **HB 2194** would not become effective unless both chambers consider and vote on the bill. **HB 2194** requires vested employees to choose between paying 2 percent more of their salary into KPERS for a 6 percent benefit increase for future years of service or accept a 20 percent reduction in benefits earned for future years of service.

He described the retirement plan for new hires and non-vested employees; state funding of the KPERS unfunded liability; and changes proposed for vested and non-vested legislators. Senator King indicated that with the passage of **HB 2194** and **SB 338**, the state will save approximately $4.5 billion over the next 20 years.

Senator King reported that testimony was heard from an actuary (during the committee meetings) concerning the closing of defined-contribution accounts, which could result in billions of dollars in "plan closure costs." By structuring the annuity in the manner contained in the bill, plan closure costs are avoided. He indicated the bill does not contain language referencing "plan closure costs" since the system has been structured as an annuity. New Section 10 and New Section 11 (page 7 of the bill) contain the required annuity component language. Senator King confirmed the design of the bill has been reviewed by the KPERS attorney.

Senator King distributed a letter from Acting Executive Director, Elizabeth Miller, with addenda reflecting updated versions of the present value analysis of the State/School group and the Local Group. (Attachment 3a) Senator King pointed out the report distributed uses "present value calculation" that reflects an actual plan cost of $20-$21 million annually over a fifty year period. He recognized that with the current unfunded liability, costs could be greater up front (as seen in the first four years of the reports).

With regard to a question concerning the State/School Group analysis (Attachment 3) and with the implementation of **HB 2194**, Senator King indicated the cost over 50 years is $8.3 billion using a "present value calculation." If a "present value calculation" is not used, the cost reflected is $22 billion. If the Study Commission's plan is adopted, the "present value calculation" is $9 billion. Senator King clarified that using the assumption that KPERS returns 8 percent on its investments yearly, it would cost the state $21 million more yearly (present value calculation) to implement the Study Commission's recommendations than implementing **HB 2194** alone.

Senator King emphasized the importance of the state paying the actuarial required contribution (ARC); the Study Commission creates a system requiring that the state pay what is required for the fund's stability. A committee member asked what federal government consequences exist if the state does not make the statutory-required contributions; Senator King was unable to answer the question.

Senator King discussed the benefits to state employees under the plan. In response to a question, Senator King clarified that under **HB 2194** alone, Kansas will make the lowest contribution to any state pension plan in the country. Discussion was also heard concerning the vested and non-vested legislator payments as well as the potential amendment to create parity between legislator and non-legislator payments. Senator King commented that non-legislators, who are vested as of January 1, 2014, would have the same plan as before except they would have a choice to pay 2 percent (from 4 percent to 6 percent) more of their salary to get a 6 percent retirement benefit increase in future years or they can choose to pay the current 4 percent contribution and get a 20 percent decrease in future retirement benefits. For vested legislators, as of December 31, 2013, an actuary will calculate the present value of his/her pension plan. That amount is paid out as a lump sum to be transferred into the new system.

A committee member inquired whether the KPERS return on investment (ROI) of 8 percent is generous. Senator King replied that historically KPERS has returned over 8 percent; however, over the last 10 years they have not met the 8 percent ROI target. Another question was heard whether a cost of living adjustment (COLA) is contained within the Study Commission's plan. Senator King indicated "Tier 2" employees, which are defined as individuals starting employment on July 1, 2009, have a COLA. **HB 2194** reforms contain allowances for repealing that COLA for Tier 2 employees. He explained that if the Study Commission plan becomes effective, that COLA will be removed because there will be no "Tier 2" employee.

Senate Minority Report on KPERS Study Commission:

Rebecca Proctor, a member of the KPERS Study Commission, discussed the Minority Report with Committee members (Attachment 4). Ms. Proctor indicated that those individuals signing the Minority Report do not feel the plan recommended by the majority of the study commission meets the charge, which was to develop a viable plan to ensure the long-term sustainability of the KPERS system.

She commented that state and local government plans are not subject to the Employee Retirement Income Security Act (ERISA), which is part of the reason for Kansas' unfunded liability. Had the plan come under ERISA requirements, the state would have been required to fund the actuarially required contribution. She clarified that a vested legislator cannot take the lump sum payout; it is a buyout from the current KPERS that is required to be reinvested into either the KPERS cash balance plan or defined-contribution plan. Ms. Proctor discussed the Study Commission Plan, how it was presented to the members of the Commission, described how the defined contribution plan and cash balance plan works, the differences in Kansas' plan compared to typical cash balance plans, and how the plan affects new employees (non-vested). Ms. Proctor indicated that when the bill was published it was different than what was presented to the Commission members. The bill contains an additional defined contribution plan available only to employees of public school systems and employees of certain community colleges (a 403b plan), which is in New Section 5 of the bill. The bill now contains a 403b plan (only for employees of public school systems and employees of certain community colleges), a 401k or 404k plan, and a cash balance plan. Ms. Proctor asserted this was not discussed in Commission meetings. Senator King responded that when listening to the audio recording of Commission meetings, a motion was offered conceptually that included language of "offering a wide array of investment options." The Revisors Office working on drafting the bill discussed with Senator King that a 403b plan is part of a wide array of investment options available to teachers and community colleges; in order reflect the spirit of a wide array of investment options, it seemed unnecessary to foreclose on the investment option (403b) available to a percentage of KPERS participants. That was the rationale for its inclusion. Ms. Proctor indicated her concern is that the inclusion of the 403b option is not just an additional investment option, but that it is an additional plan with additional code requirements. There was discussion about treating state employees equally, not about separating a group of individuals under a separate plan.

Ms. Proctor indicated that KPERS Plan Actuary, Pat Beckham, has estimated the cost of Senator King's plan at $33.04 billion for years 2012 through 2060; the cost of **HB 2194** is

$22.14 billion for the same time period. Ms. Proctor concluded the Study Commission plan increases costs, reduces employee benefits while not addressing the State's unfunded actuarial liability.

In response to a committee member's question, Ms. Proctor could not estimate the value of the cash balance plan upon retirement based on the assumptions provided.

Chairperson McGinn adjourned the meeting adjourned at 11:30 a.m.