

MEMORANDUM

To: Senate Financial Institutions and Insurance Committee

From: Alan D. Conroy, Executive Director

Date: February 15, 2018

Subject: SB 395; Final Average Salary cap

SB 395 as introduced would add a maximum cap on the final average salary for members hired on or after July 1, 2018 and for existing members who have participating service under a contract entered into with an affiliated employer on or after April 1, 2018. The maximum final average salary applies to the Judges' Retirement System, Kansas Police and Firemen's Retirement System (KP&F) and to KPERS members, including legislators.

As introduced, SB 395 affects final average salary calculations, which is a component of a traditional defined benefit plan like KPERS 1, KPERS 2, KP&F and Judges. However, KPERS 3 is a cash balance plan and final average salary is not used in calculating KPERS 3 benefits. Therefore, as written, there is no cap on allowable salary for KPERS 3 members. All new KPERS members are participants of KPERS 3.

One distinction that may not be clear is that the bill does not cap actual salary of employees, just the amount that can be counted for KPERS final average salary purposes. Based on the valuation date from the 12/31/2016, approximately 1.7% of KPERS members have salary above the cap in SB 395 (\$99,636). Attachment A has a breakdown of members by group who were above the cap.

Final Average Salary Calculations

Final average salary is one piece of the benefit formula used for KPERS 1, KPERS 2, KP&F and Judges (final average salary x years of service x a multiplier). Final average salary is calculated differently for each group:

- KPERS 1 (including legislators)
 - Pre-1993 members: average of highest 3 years of salary without add-ons (e.g. sick and annual leave) or highest 4 years of salary with add-ons, whichever is greater
 - Members since 1993: average of highest 3 years of salary
- KPERS 2 (including legislators)
 - Average of highest 5 years of salary
- KP&F
 - Average of highest 3 years of salary out of the last 5 years of service
- Judges
 - Average of highest 3 years of salary out of the last 10 years of service



SB 395 places a maximum final average salary for the Judges and legislators. However, for KPERS and KP&F, SB 395 caps the amount of compensation allowed to be used in the final average salary calculation. The effect of the two approaches is similar, but the method of calculation does differ slightly.

Projected Actuarial Costs

In order to complete a cost projection for SB 395, several assumptions had to be applied to project future member salary. The assumptions include:

- The salary limitation would apply to all groups, including KPERS 3 members;
- No employee or employer contributions would be collected on salary above the maximum cap;

While the bill would apply to existing members who enter into an employment contract after April 1, 2018, the cost estimate does not include any changes for existing members. Some existing members will be affected by SB 395, but KPERS does not have information on the number of members who are working under a contract so no assumption was included in the cost estimate.

Applying a cap on the allowable salary for final average salary calculations would change both the amount of contributions and the projected costs of future benefits. However, the number of members that are projected to reach the salary limitation is relatively small (currently about 1.7% of members) so the overall cost impact is limited.

The projected impact of SB 395 on FY 2019 employer contributions is summarized in the following table:

Estimated FY 2019 Employer Contributions				
	State/School	Local	KP&F	Judges
Current FY 2019 employer contribution estimate	\$408.75	\$147.38	\$99.07	\$4.10
Projected FY 2019 employer contributions under SB 395	\$408.60	\$147.28	\$99.06	\$4.04
Difference	\$(0.15)	\$(0.09)	\$(0.00)	\$(0.06)

Over the 30-year projection period ending in FY 2048, the total projected employer contributions decrease by \$5.0 million for the State/School group, \$7.8 million for the Local group, \$42.2 million for KP&F and \$33.8 million for Judges.

The largest impact, in terms of proportion, is on the Judges group. Judges' salaries are set statutory and currently about 70% of judges' salaries are above the initial \$99,636 cap.

Administrative Considerations

In order to administer a cap on final average salary, KPERS will need to upgrade our information technology system and internal business flow to accommodate the changes. There will be some costs associated with the upgrades to the information technology system. KPERS is currently studying the necessary changes and developing a cost estimate.

As currently written, SB 395 applies to the calculation of final average salary, which is not a feature of the KPERS 3 cash balance plan. If the intent is to include KPERS 3 members, the bill will need to be amended to include a cap on allowed compensation for this group. In addition, it is not clear in the bill if employee and employer contributions are to continue being made after a member reaches the cap on salary. It would be helpful, from an administrative standpoint, if the treatment of contributions is expressly addressed in the language.

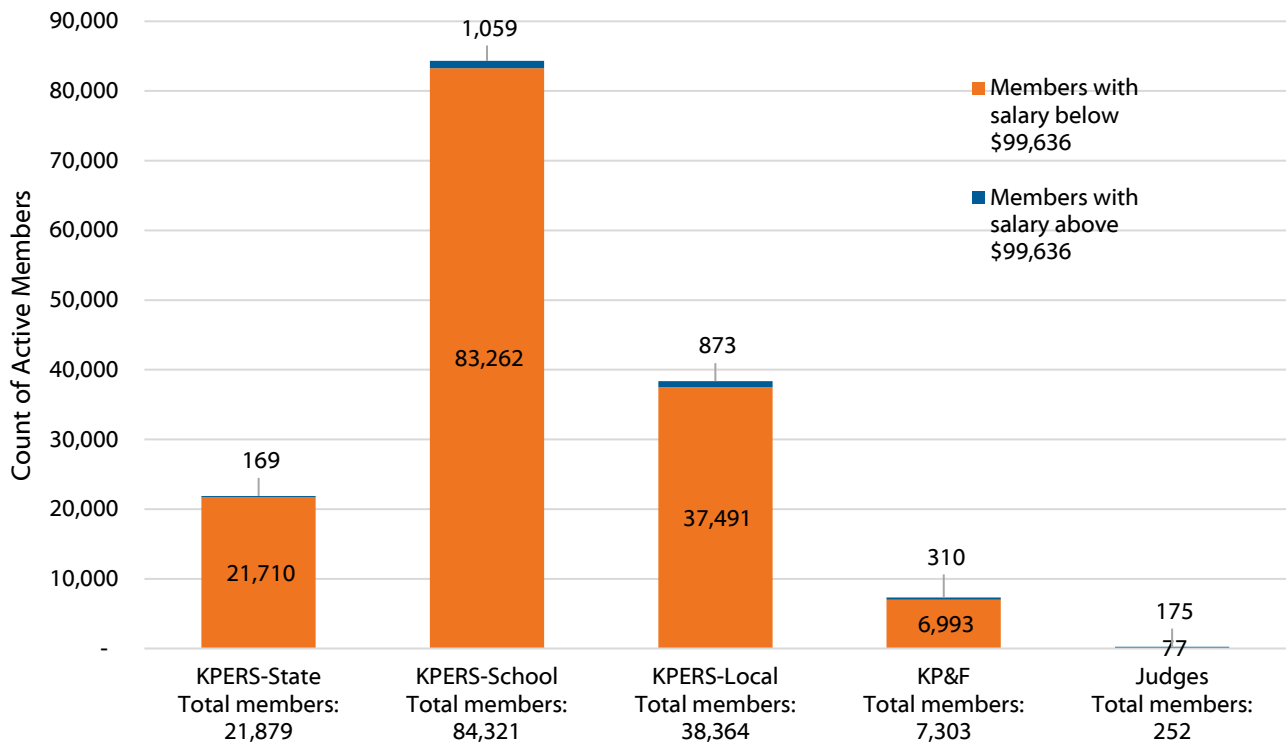
Attachment

KPERS member salaries above the Governor's statutory salary (\$99,636)

Group	Members with salary above \$99,636	Total Active Members	Percent of Total Members	Average salary of members above \$99,636
KPERS-State	169	21,879	0.8%	\$ 126,392
KPERS-School	1,059	84,321	1.3%	\$ 118,422
KPERS-Local	873	38,364	2.3%	\$ 138,504
KP&F	310	7,303	4.2%	\$ 112,139
Judges ¹	175	252	69.4%	\$ 121,679
Total	2,586	152,119	1.7%	

¹Judges salaries are set by statute (see K.S.A. 75-3101 et. seq.).

KPERS member salaries above the Governor's statutory salary (\$99,636)



Data as of 12/31/2016

