TO THE GOVERNOR AND GENERAL ASSEMBLY:

A REPORT REGARDING, AND RECOMMENDATONS FOR,

PLAN DESIGN,

MULTI-YEAR BENEFIT ENHANCEMENTS

AND CONTRIBUTION RATES FOR

THE IOWA PUBLIC EMPLOYEES' RETIREMENT SYSTEM

November 1999

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Iowa Public Employees' Retirement System

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PART SEVEN: RECOMMENDATIONS FOR CONSIDERATION FOR FUTURE PLAN DESIGN

Acknowledgements

While this report is *written* by one person[1], it is truly the product of dozens of people who have worked together intensely over the past several months. It also builds upon the previous efforts of the Legislature, IPERS' staff,[2] and IPERS' Constituent Group[3] to study ways in which our System's benefits and plan design needed to be improved.

I gratefully acknowledge their many contributions to the development of the ideas in this report. The ongoing consultative assistance offered by IPERS' actuary, Patrice Beckham of the Omaha offices of Milliman and Robertson, has also been invaluable. In addition, the valuable perspectives gained from an ongoing dialogue with national experts who have become my professional colleagues over the years are also gratefully acknowledged.[4]

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[1] After several drafts and numerous suggestions for revisions by all the members of the Constituent Group and IPERS' management team.

[2] Principally, Mollie Anderson, Director of the Department of Personnel; Kathy Comito, Chief Investments Officer; Jennifer Dixon, General Counsel; Leon Schwartz, Operations Manager; David Martin, Retirement Benefits Staff Coordinator; Karl Koch, Assistant Chief Investment Officer; Kelly Lovell, Associate Counsel; and Curt Sorteberg, a Retirement Benefits' executive officer.

[3] Please see the Appendices for a listing of the members of the Constituent Group and a discussion of how we have worked with them in recent years.

[4] Including ongoing discussions of policy trends and plan design issues with Dr. Joseph Metz of the New York office of Buck Consultants, Cynthia Moore of the Washington, D. C. office National Council on Teacher Retirements, and Nancy Williams of the Denver office of William Mercer, Inc. Dr. Metz is the author of several key reports for IPERS during the middle 1990s. Ms. Williams is the consultant employed by IPERS, the Peace Officer Retirement System, and the Municipal Fire and Police Retirement System in 1998 in the completion of the legislatively mandated study on benefits *parity* between and among the public safety employees covered by these three public retirement systems. Ms. Moore frequently represents a broad coalition of public employee retirement systems in working with, and testifying before, the United States Congress.

Executive Summary

Financial Health of Trust Fund – Status as of June 30, 1999

Our actuary, Pat Beckham of Milliman and Robertson, reports that the Trust Fund's financial status at the conclusion of FY 99, before adjustments for the two factors addressed below are factored in, is **excellent**: a substantial positive margin (of almost $500 million) and a zero years to amortize any unfunded liability (as there is none). In addition, Pat reports that the System once again had a favorable over-all investment return above 10% with the market value of our assets topping $15 billion.[5]

Impact of Adjusting Certain Basic Actuarial Assumptions and Transferring Monies to FED Reserve Fund

However, there are two mitigating factors with which we must also contend this year and, which together substantially impact our Fund's ability to absorb further benefit enhancement costs in calendar year 2000:

1) A recently completed actuarial *experience study*.
2) The required transfer of a portion of our *favorable experience* to the *Favorable Experience Dividend* Reserve Fund.

The experience study

One of the services Ms. Beckham performs for IPERS every several years is an *experience study,* wherein she examines actual System behavior (including factors such as mortality, utilization of the *Rule of 88,* and salary increases) in recent years and compares them to the assumptions she had previously made about that behavior. Where the facts require, she recommends that we adopt appropriate adjustments to the assumptions. She then uses these revised assumptions to project our current and anticipated liabilities.

Ms. Beckham recently completed such a study and reported its draft results to IPERS in October 1999. From an objective standpoint, her report contains much good news. As an example, members are living longer in retirement than had been expected. The downside for the System, in this example, is that our projected liabilities have to be increased to reflect members' longer draw-down of retirement benefits.

[5] However, because we use a cost method which spreads market experience out over several years – thus avoiding sharp swings in valuation which using full annual market value might well cause – the figure our actuary used as IPERS' asset basis at the conclusion of the fiscal year is just over $12 billion.

The net effect of all of her recommended adjustments to System assumptions is a significant *increase* in total liability and the creation, once again, of an unfunded liability. This also makes the period to fully amortize (pay off) the unfunded portion of that liability 6.3 years.

There are some aspects of the study which, when combined with very recent observations about member behavior, make it possible that a future experience study might revise a portion of future liabilities *downwards*, but it will be a few years before we will know for sure.[6] If warranted by near future experience, the actuary will recommend similar adjustments to incorporate them.

The required transfer of a portion of last fiscal year's favorable experience into the Favorable Experience Dividend reserve fund

Under current law, a portion of each year's *favorable experience* must be transferred to the Favorable Experience Dividend reserve fund. Although we are recommending that this reserve fund be capped at 10 years' reserve capacity (see our recommendation # 3 below), we had no choice for Fiscal Year 1999 but to comply with the law as it currently stands.[7] The effect of this transfer substantially enlarges our unfunded liability and dramatically extends our years to amortize this unfunded liability from 6.3 to 19.2 years!

The following table illustrates the above discussion:

Status of Fund as of 6-30-99:	**+$400 million positive balance** **No unfunded liability ("over" funded)** **0 Years to amortize**
Impact of Experience Study:	**-$200 million negative balance** **1% unfunded liability (99% funded)** **6+ years to amortize**
Impact of Transfer to FED Reserve Fund	**-$400 million negative balance** **3% unfunded liability (97% funded)** **19+ years to amortize**

[6] For example, fewer people than initially assumed are taking advantage of early retirement (the *Rule of 90* then the *Rule of 88*) when they first become eligible. Also, effective July 1, 1999 terminating members wishing a refund can now receive a portion of the employer contributions, too. Many longer term persons, for whom such a choice may not be in their financial best interest (as they have accumulated a sizable benefit upon retirement), are choosing to take a refund. If these two trends are borne out over several years they would *reduce* estimated liabilities.

[7] When we proposed the legislation creating the *Favorable Experience Dividend*, and the reserve fund from which to pay it, we suggested a five-year reserve be created before the first payout be made. This was to ensure that the FED would be able to be distributed even in years when the Fund had not experienced any *favorable experience*. The General Assembly accepted this recommendation, including the five-year reserve fund, and the first ever FED was paid in January 1999. Although we believed that this same five-year reserve would also be its *maximum* size, we have discovered that a strict reading of the law sets no such maximum. Therefore, we are required to continue transferring portions of *favorable experience* to this reserve no matter how large it might become. This is why we are urging that it be capped at 10 years during the coming legislative session.

Affordability of Benefits' Enhancements

As this is very close to the **20 years to amortize** standard we set in our *funding policy*[8] as the point beyond which we state that we cannot afford further benefit enhancements, the ***implementation*** of any benefit enhancements with significant costs (not otherwise offset by increased contribution rates) will have to be delayed beyond this current fiscal year.

Therefore, while we are asking that **all** of our recommendations be enacted by the General Assembly in the 2000 legislative session, we distinguish between:

- The vast majority of enhancements[9] which we are asking be *enacted* in the 2000 legislative session **and also** *implemented* in either January or July 2000; and,

- Those which we request be *enacted* in the 2000 legislative session **but** *implemented* within the next couple of years as IPERS, in conjunction with our actuary, determines this can be done in accord with our Funding Policy.

This concept of a period of *implementation phase-in* is the same tack the 1990 General Assembly took when it directed us to increase the formula multiplier over time from the then 1.67% per year of service (equaling a maximum 50% payout) to 2.0% per year of service (a 60% payout) for a 30 year employee).[10] The General Assembly gave IPERS the enhancement goal(s) while allowing IPERS the discretion to implement those steps within its fiscal limits. That process worked very well then (the goal of a 60% maximum multiplier was achieved in 1994 and the covered wage ceiling was ultimately eliminated in 1996), and we believe it can work equally well now.

Barring a severe and prolonged market crash (which, while not inevitable, is no more "certain" for planning purposes than a continuation of annual 20%-30% market returns), there is every likelihood that additional enhancements will be affordable as soon as calendar year 2001.

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[8] Please see the appendix for the full text of this policy.

[9] Either because they are *no* or *minimal* cost items, or because their cost will be offset by higher contribution rates.

[10] Both the 50% and 60% figures are for an employee with 30 years of service. That same 1990 law – House File 2543 – also told IPERS to increase the then existing covered wage ceiling by up to $3,000 per year, within the same limitation of adhering to existing contribution rates. The exact wording is found in Section 28 (b), second unnumbered paragraph of H. F. 2543 as passed by the 1990 General Assembly:

> *Commencing July 1, 1991, the department shall increase the percentage multiplier of the three-year average covered wage by an additional two percent each July 1 until reaching sixty percent of the three-year average covered wage if the annual actuarial valuation of the retirement system indicates for that year that the cost of this increase in the percentage of the three-year average covered wage used in computing retirement benefits can be absorbed within the employer and employer contribution rates [currently] in effect....*

Recommendations for Benefit Enhancements

Therefore, IPERS joins its Constituent Group members in recommending for consideration by the 2000 session of the General Assembly the following enhancements for IPERS' plan. These are listed by priority ranking. Also, please note that, unlike previous years, most of this year's recommendations are not cost items which will dramatically alter the fiscal standing of the Fund.[11]

1. **Giving IPERS' special public safety occupations the same kind of disability benefits enjoyed by those public employees covered by the Municipal Fire and Police Retirement System of Iowa and the Peace Officers Retirement System;**

   Cost: Significant, but covered by increased contribution rates for these members and their employers.[12]

   Recommended Enactment & Implementation Date: July 2000

2. **Increasing the Cost of Living Adjustment (COLA) for members who retired prior to July 1990 from 80% of the Consumer Price Index (CPI) to 100%, while retaining the existing ceiling on annual distributions at a maximum of 3% above the preceding year[13];**

   Cost: None[14]. In order to cover our maximum possible liabilities, our actuary already projects future payouts to retirees at the maximum of 3% per year.

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[11] IPERS expresses the impact of a benefit enhancement in two ways: 1) any increase in the System's *unfunded liabilities*, expressed as **percentage of fully funded**; and 2) any increase **in years to fully amortize the unfunded liability** of the System.

[12] As a consequence, this would not impact the time to amortize the System's unfunded liabilities.

[13] The impact of this on the *Favorable Experience Dividend (FED)* is expected to be similar. However, please recall that the FED is not by law linked by law to the dividend paid to the pre July 1990 retirees. The language governing the computation of the FED is not as specific as that for the COLA for the pre July 1990 retirees. IPERS' staff, in making the first FED distribution in January 1999, intentionally *targeted* the dividend paid to the pre July 1990 retirees as the rate they intend the *FED* to be. However, the law allows the actual *FED* to be determined by IPERS staff, following a report on the financial health of the Fund by the System's actuary. The actual language governing the determination of the *FED* is as follows, and is taken from Iowa Code section 97B.49F (2) (d):

> *The favorable experience dividend is calculated by multiplying the total of the monthly benefit payments of the retiree, beneficiary, or contingent annuitant for the previous calendar year, by the number of complete years the member has been retired or would have been retired if living as of the date the dividend is payable, and by the applicable percentage. For purposes of this paragraph, the applicable percentage is the percentage, not to exceed three percent, that the department determines shall be applied in calculating the favorable experience dividend if the department determines that the reserve account is sufficiently funded to make a distribution. In making its determination, the department shall consider, but not be limited to, the amounts credited to the reserve account, the distributions from the reserve account made in previous years, the likelihood of future credits to and distributions from the reserve account, and the distributions paid under subsection 1.*

This language may be contrasted with that governing the COLA paid to pre July 1990 retirees which is found in 97B.49F (1).

[14] With reference to the general "cost" footnote, increasing the COLA to 100% does not impact the System's funded status, or the time to amortize its unfunded liabilities, because the actuary already projects future liabilities *as if*

Recommended Enactment & Implementation Date: July 2000

3. **Placing a cap on the FED Reserve Fund equivalent to 10 years of maximum payouts;**

   Cost: None. It will actually allow monies which otherwise would be deposited in a larger than needed FED Reserve Fund to be used for: other benefits, and/or paying down any unfunded liability, and/or paying a Supplemental Account for Active Members (SAAM) distribution.

   Recommended Enactment & Implementation Date: July 2000

4. **Moving from the Current *Rule of 88* to the *Rule of 85*;**

   Cost: Significant.[15]

   Recommended Enactment Date: July 2000

   Implementation Date: In Increments of One Year, and in Those Calendar Years when IPERS Determines Its Costs Can be Absorbed within Existing Contribution Rates and in Accord with its Funding Policy

5. **Improving the death benefit for the beneficiaries of those members who die before initiating retirement;**

   Cost: Modest.[16]

   Recommended Enactment Date: July 2000

   Implementation Date: When IPERS Determines Its Costs Can be Absorbed within Existing Contribution Rates and in Accord with its Funding Policy

6. **For our public safety employees, establishing a fixed rate structure sufficient to both fund the costs of the existing benefit program plus disability and to provide a potential margin for the purchase of additional enhancements for the special groups in the future:**

   ✓ Equalize Number of Years Required to Establish 60% Formula at 22

   ✓ Provide Credit for a Maximum of Eight Years of Service beyond 22 Years

   ✓ Provide Same Credit per Year of Service

   Cost: Significant. To be paid within the higher, fixed rates recommended here.[17]

   Recommended Enactment Date: July 2000

   Implementation Date: For Fixed Rates: July 2000; for Other Benefit Enhancements towards Parity when IPERS Determines Its Costs Can be

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IPERS will be paying the maximum 3%. This is, of course, a *conservative* measure as it ensures we factor in the highest possible future liability represented by COLA increases. Obviously, too, however, the *actual cash payouts* resulting from using 100% of the CPI will be higher than they would have been under the present 80% of the CPI.

[15] "Significant" in this context means that the effect of enacting this enhancement, because the cost would be shared by the **entire** System, would likely lengthen the *time to fully amortize* the unfunded liabilities of the System by two or more years.

[16] "Modest" in this context means that the effect of enacting this enhancement, because the cost would be shared by the **entire** System, would likely lengthen the *time to fully amortize* the unfunded liabilities of the System by one or two years.

[17] As a consequence, these would not impact the time to amortize the System's unfunded liabilities.

Absorbed within the Fixed Rates Established in 2000 and in Accord with IPERS' Funding Policy

7. **For *adjunct instructors* who work for the community colleges, the right to elective coverage be extended only to those who already have an IPERS' account;**

   Cost: Nonexistent (for the Fund, but are a definite factor for the community colleges).

   Recommended Enactment & Implementation Date: July 2000

8. **Replacing our existing "calendar year" for the computation of retirement benefits to "12 contiguous quarters";**

   Cost: None, except for some administrative costs within IPERS.

   Recommended Enactment: July 2000

   Implementation Date: July 2001[18]

9. **Allowing elected officials other than legislators to terminate their full-time IPERS' covered positions and retire without having to resign from their elected positions;**

   Cost: None.

   Recommended Enactment & Implementation Date: July 2000

10. **Adjustments to the retirement formula for the higher paid, including increasing the "default" standard by $10,000 per year beginning January 2000 and freezing the multi wage year averaging at the current six, and to return to the average of the highest three salary years effective January 2002;**

    Cost: Insignificant. The cost of paying for the benefits of the higher paid has never been a major cost issue for IPERS.

    Recommended Enactment & Implementation Date: January 2000

11. **Creating a "pop-up" option for retirement Option 4 to Option 2 upon a contingent annuitant's death (occurring before the member's death), to be paid for actuarially by members choosing it; and**

    Cost: None.

    Recommended Enactment Date: July 2000

    Recommended Implementation Date: July 2001[19]

12. **Raising the ceiling on re-employment wages for the 2% of IPERS' retirees who have returned to covered employment from $12,000 to $25,000.**

    Cost: Insignificant.

    Recommended Enactment & Implementation Date: July 2000

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[18] We are asking for a delay in *implementation* as it will take us time to reprogram our computers and notify members.

[19] The delay in implementation is to allow us to build this change into our current re-engineering project.

IPERS' Recommendations for Benefit Enhancements Sorted According to "Cost" to Trust Fund

[Please Note: The following are ranked according to "cost". In this context, "cost" means having the effect of *increasing* the System's liabilities. Numerical ranking of the enhancements represents their priority in the recommendations arrived at by IPERS in conjunction with its employer and employee Constituent Group.]

NO COST

Priority Ranking: # 2

Increasing the Cost of Living Adjustment (COLA) for members who retired prior to July 1990 from 80% of the Consumer Price Index (CPI) to 100%, while retaining the existing ceiling on annual distributions at a maximum of 3% above the preceding year. This would also favorably impact the *Favorable Experience Dividend* paid to post June 1990 retirees, too. *(In order to cover our maximum possible liabilities, our actuary already projects future payouts to retirees at the maximum of 3% per year.)*

Recommended Enactment & Implementation Date: July 2000

Priority Ranking: # 3

Placing a cap on the FED Reserve Fund equivalent to 10 years of maximum payouts. *(It will actually allow monies which otherwise would be deposited in a larger than needed FED Reserve Fund to be used for: other benefits, and/or paying down any unfunded liability, and/or paying a Supplemental Account for Active Members (SAAM) distribution.)*

Recommended Enactment & Implementation Date: July 2000

Priority Ranking: # 7

For *adjunct instructors* who work for the community colleges, the right to elective coverage be extended only to those who already have an IPERS' account. *(Cost is nonexistent for the Fund but are a definite factor for the community colleges.)*

Recommended Enactment & Implementation Date: July 2000

Priority Ranking: # 8

Changing the law to replace our existing "calendar year" in the computation of retirement benefits with "12 contiguous quarters".

Recommended Enactment & Implementation Date: July 2000

Priority Ranking: # 9

Allowing elected officials other than legislators to terminate their full-time IPERS' covered positions and retire without having to resign from their elected positions.

Recommended Enactment & Implementation Date: July 2000

Priority Ranking: # 10

Adjustments to the retirement formula for the higher paid, including increasing the "default" standard by $10,000 per year beginning January 2000 and freezing the multi wage year averaging at the current six, and to return to the average of the highest three salary years effective January 2002. *(The cost is insignificant.)*

Recommended Enactment & Implementation Date: 2000

Priority Ranking: # 11

Creating a "pop-up" option for retirement Option 4 to Option 2 upon a contingent annuitant's death, to be paid for actuarially by members choosing it. *(Delay in implementation made necessary by IPERS' current reengineering project.)*

Recommended Enactment Date: July 2000, with Implementation Date: July 2001

Priority Ranking: # 12

Raising the ceiling on re-employment wages for the 2% of IPERS' retirees who have returned to covered employment from $12,000 to $25,000. *(The cost is insignificant.)*

Recommended Enactment & Implementation Date: July 2000

COST TO TRUST FUND OFFSET BY HIGHER CONTRIBUTION RATES FOR SPECIAL SERVICE GROUPS

Priority Ranking: # 1

Giving IPERS' special public safety occupations the same kind of disability benefits enjoyed by those public employees covered by the Municipal Fire and Police Retirement System of Iowa and the Peace Officers Retirement System. *Cost: Significant, but covered by increased contribution rates for these members and their employers.*[20]

Recommended Enactment & Implementation Date: July 2000

Priority Ranking: # 6

For our public safety employees, establishing a fixed rate structure sufficient to both fund the costs of the existing benefit program plus disability and to provide a potential margin for the purchase of additional enhancements for the special groups in the future:

- **Equalize Number of Years Required to Establish 60% Formula at 22**
- **Provide Credit for a Maximum of Eight Years of Service beyond 22 Years**
- **Provide Same Credit per Year of Service**

(Cost: Significant. To be paid within the higher, fixed rates recommended here.)

Recommended Enactment Date: July 2000

Implementation Date: For Fixed Rates: July 2000; for Other Benefit Enhancements towards Parity when IPERS Determines Its Costs Can be Absorbed within Existing Contribution Rates

COST ITEMS

Priority Ranking: # 4

Moving from the Current *Rule of 88* to the *Rule of 85*. *(Cost: Significant)*

[20] As a consequence, this would not impact the time to amortize the System's unfunded liabilities.

Recommended Enactment Date: July 2000
Implementation Date: In Increments of One Year, and when IPERS Determines Its Costs Can be Absorbed within Existing Contribution Rates and in Accord with its Funding Policy

Priority Ranking: # 5

Improving the death benefit for the beneficiaries of those members who die before initiating retirement. *(Cost: Mildly significant.)*

Recommended Enactment Date: July 2000
Implementation Date: When IPERS Determines Its Costs Can be Absorbed within Existing Contribution Rates and in Accord with its Funding Policy

Introduction

IPERS' Purpose and Mission

The Iowa Public Employees' Retirement System (IPERS) exists to provide a sound, balanced and comprehensive retirement system[21] for most of Iowa's public employees.[22] The assets of the System are held for the "exclusive benefit" of its members and beneficiaries as is required by both federal and state law.

IPERS was created to work in tandem with federal Social Security benefits. Since 1953 we have regularly reviewed the degree to which IPERS' benefits, coupled with those provided by Social Security, would provide adequate income in retirement to our members.

Traditionally, retirement income is presumed to come from three sources: Social Security, private savings, and the pension plan provided by employers. We realize that for many (probably the majority) of our members, it is difficult to set aside much in additional private savings for retirement purposes when they are faced with other, more immediate and pressing needs of providing shelter and education for their children. In the light of this reality, the pension plans provided by employers have assumed even greater importance. Accordingly, some years ago IPERS proposed that we *target* as a benefit design goal that combined benefits from IPERS and Social Security would range from at least 70%, but not to *exceed* 100%, of a member's pre-retirement income. For career employees with 30 years of service, IPERS' payout of 60%[23] plus Social Security should provide them with a retirement income from 70% to 95% of their pre-retirement income.[24]

Because IPERS does not exist in either a vacuum, we have continued to monitor developments in the public and private employment and pension spheres in order to make sound and future-oriented proposals to the Governor and General Assembly. Towards this end, we have

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[21] The exact language from Iowa Code section 97B.2 is:

> *The purpose of this chapter is to promote economy and efficiency in the public service by providing an orderly means for employees, without hardship or prejudice, to have a retirement system which will provide for the payment of annuities, enabling the employees to care for themselves in retirement, and which will improve public employment within the state, reduce excessive personnel turnover, and offer suitable attraction to high-grade men and women to enter public service in the state.*

In addition, Iowa Code section 97B.7 (3) adds:

> *All moneys which are paid or deposited into this fund are appropriated and made available to the department to be used for the exclusive benefit of the members and their beneficiaries or contingent annuitants....*

[22] Judges, state troopers, and police officers and fire fighters in Iowa cities above 8,000 population participate in separate public retirement plans (see Chapters 97A and 411 of the Iowa Code). University and community college employees also have the right to elect alternate coverage in lieu of IPERS'.

[23] IPERS' payout for employees with 35 years of service would be 65%. Members with fewer years of service will receive less.

[24] Because of the formula used by Social Security, the total replacement ratio will be lower for the higher paid employees.

occasionally undertaken special studies (many of them at the direction of the General Assembly) and have continued to work closely with the members of our Constituent Group[25].

Review of Legislative Enhancements: 1987-1998

In the past dozen years, the changes in IPERS' plan design have been dramatic. In partnership with a receptive General Assembly, IPERS has proposed numerous changes, the enactment of which have advanced our retirement plan from a very uncompetitive position twelve years ago to the upper tier today when compared to other statewide public employee retirement systems around the country.

Throughout these efforts, we have consistently sought to:

a) Preserve the financially sound status of the IPERS' Trust Fund;

b) Maintain a stable and predictable contribution rate[26]; and

c) Achieve a defensibly competitive level of benefits compared to other statewide public systems.

The following are highlights of some of the most significant improvements over the last decade:

For Active Members

1. Providing greater flexibility for service credit portability into IPERS by allowing *buy-in* of service earned elsewhere as a public employee and *buy-back* for previously refunded IPERS' service;

2. Allowing greater flexibility for service credit portability out of IPERS by granting terminating vested members a portion of the employer contributions;

3. Establishing the Supplemental Account for Active Members (SAAM) which is designed to give active members a *dividend type* credit into a separate account which will be theirs to access either upon termination from public employment or at time of retirement.

For Members Nearing Retirement

4. Allowing credit for more years of service by granting an additional 1% of value for each year from 31 through 35[27];

[25] The members of which are listed in Appendix Two of this report.

[26] For *regular* service members it has remained at 5.75% for employers and 3.7% for members for more than 20 years. Members of IPERS' special public safety groups and their employers pay rates which are annually set by IPERS' actuary to cover the value of their benefits which exceed those available to regular service members.

5. Giving greater value for each year of service by:
   - increasing the formula multiplier in annual increments from 50% in 1990 to 60% in 1994 (which increased the value of each year of service from 1.67% to 2.0%); and,
   - lifting the covered wage ceiling in 1996[28];

6. Eliminating or reducing the *early retirement adjustment* for qualifying individuals beginning with the Rule of "92" to today's Rules of "88" and "62 and 20"';

For Members in Retirement

7. Assisting retirees maintain purchasing power by:
   - First, regularly giving *ad hoc dividends*, plus occasional *permanent* adjustments to base pensions[29], to pre July 1990 retirees;
   - Second, providing that same group with an annual Cost of Living Adjustment beginning in 1996; and,
   - Third, awarding all post-June 1990 retirees[30] with a *Favorable Experience Dividend* beginning in 1999[31].

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[27] Providing for a maximum formula multiplier of 65% for members with 35 or more years of service.
[28] Even with the elimination of the ceiling, however, current law will not allow the full value of a more highly compensated employee's wages to be used in calculating his or her retirement benefits until calendar year 2003.
[29] In both 1996 and 1998.
[30] To include all future retirees, as well.
[31] Contingent upon the solvency of the FED Reserve Fund.

Part One: IPERS in the Context of Other Statewide Public Pension Plans

The Findings of the Buck Reports of 1995 and 1997

Both in 1995 and in 1997, IPERS contracted with the New York Office of Buck Consultants in order to get a snapshot of where our plan "fits" within the universe of other statewide public employee retirement systems. Our consequent recommendations, in large measure, endorsed[32] the findings and recommendations of Buck Consultants, as authored by Dr. Joseph Metz.

Because of the substantial improvements enacted by the General Assembly over the past five years, we believe IPERS is now in the upper quartile of public pension funds in the overall benefits provided its members. However, we are **not** as competitive as we would like in every particular, which is why we are making further recommendations for enhancements in this report.

The following are excerpts from Dr. Metz's two reports:

1995

Overall, "IPERS is a dynamic and progressive retirement system….At the same time, some IPERS benefit provisions – the heart of any retirement system – are ripe for revision so the System will be even more responsive to the needs of current and future members."[33]

"We have also measured IPERS benefits against generally recognized benchmarks used in the pension industry to evaluate the adequacy of retirement benefits."[34]

Our benefit formula components of a multiplier of 2% per year of service and three year average of highest salary years were found to be "competitive" and "right in line with national practices with plans having Social Security coverage", while our vesting after only four years was "among the most progressive" in the U.S.[35]

At the same time, Dr. Metz found that our normal retirement dates and rules, our limitation on providing service credit for only 30 years, and our post retirement adjustments for retirees, to be "not favorably competitive".[36] Nor is the "level of death benefits" for active members "competitive". Most other systems provide better death benefits.[37]

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[32] Often with suggested modifications, however. See reports comparable to this one issued by IPERS in 1995 and 1997.
[33] Dr. Joseph Metz, *Report on the Benefit Enhancement Study for Iowa Public Employees' Retirement System*, 1995, p. ii.
[34] *Ibid.* p. 4.
[35] *Ibid.* pp. 7,8.
[36] *Ibid.* pp. 5-6, 8, 9-10.
[37] *Ibid.* p. 12.

And, of course, writing in 1995, he found the then-existing ceiling on wages used for contributions and benefits to a unique and restrictive feature.[38]

1997

"In addition to revisiting our own recommendations [from the 1995 report] and the [1995] recommendations made by IPERS for enhancements of the core plan, in this Report we have identified other benefits of the core plan that should be improved to make the Plan more equitable and competitive with other statewide plans."[39] The effect would be, he hoped, the creation of "a comprehensive master plan of the IPERS core benefit structure which might be used into the next century."[40]

In that light, Dr. Metz made as high priority recommendations[41]:

- The Rule of 85;
- Improving the active members' death benefit; and
- Changing our Cost of Living Adjustment (COLA) Determination from 80% of the Consumer Price Index (CPI) to 100% (retaining the annual cap at a maximum 3% increase)

The proposals for changes in plan design and benefit enhancements made to the Legislature by IPERS and the Constituent Group over the last five years have closely followed the findings and recommendations of Dr. Metz in these – and related[42] – studies.

The Findings of the Benefits Parity Report of 1998

The 1998 General Assembly, in House File 2496, directed IPERS, the Municipal Fire and Police Retirement System of Iowa (MFPRSI), and the Peace Officer Retirement System (POR) [43] to conduct a study analyzing the benefit plans, administrative and actuarial reporting requirements of the three systems. The three systems jointly, and in accordance with the law authorizing the study, employed William M. Mercer, Inc. as consultants to assist in the preparation of the report's findings. The *Report to the Iowa Legislative Committee on Public Retirement Systems: Comprehensive Examination of Benefit Programs & Related Issues Pertaining to Public Safety Classifications within IPERS, POR & MFPRSI* was delivered to the General Assembly on November 2, 1998.

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[38] *Ibid.* p. 7-8.
[39] Dr. Joseph Metz, *Report and Recommendations on Enhancements to the Core Benefit Structure and Supplemental Plans and Features of the IPERS Defined Benefit Plan*, 1997, p. 8.
[40] *Ibid*, 1997, p. 1.
[41] *Ibid*, 1997, pp. 60-62.
[42] Dr. Metz and Buck Consultants also performed studies relating to *disability* and the issue of *defined contribution vs. defined benefit core plans*.
[43] The fourth Iowa system – the Judicial Retirement System – does not cover any of the public safety membership categories for which the General Assembly authorized this special study.

Its principal findings were that IPERS' special service groups (our public safety membership) sorely lagged not only those offered to Iowa public employees covered by the POR and MFPRSI, but also the national averages. The sole area where IPERS' covered persons were better off was in Social Security coverage.

Accordingly, the report recommended the following *benefit* enhancements[44]:

- ❖ Enhanced disability benefits for IPERS' special groups;
- ❖ According 60% maximum payout for these IPERS' members who attained 22 years of service;
- ❖ Allowing these IPERS' members the right to accrue up to 8 additional years of service, with a value of 1.5% for each additional year;
- ❖ Setting a *fixed*, as opposed to the current annual *floating*, contribution rate structure for IPERS' special groups[45]; and,
- ❖ Granting a supplementary payment to members of POR and MFPRSI to compensate for their lack of Social Security coverage.

Its chief *administrative* recommendations were[46]:

- ❖ Maintain the systems as separate entities;[47] and,
- ❖ Combine IPERS' two existing public safety groups into one.

Its chief *actuarial* recommendations were[48] that:

- ❖ IPERS should "conduct and report a separate actuarial valuation of the assets and liabilities for its public safety groups";
- ❖ Each system should "conduct an actuarial valuation of their assets and liabilities utilizing [a common] method and assumptions"; and,
- ❖ Each system "continue to utilize[,] for financing of their systems, the established actuarial method and assumptions, as endorsed by their Board of Trustees or governing official."

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[44] *Report to the Iowa Legislative Committee on Public Retirement Systems: Comprehensive Examination of Benefit Programs & Related Issues Pertaining to Public Safety Classifications within IPERS, POR & MFPRSI*, p. 18.
[45] For regular IPERS' members (96.5% of all IPERS' covered employees), the contribution rate paid by employers (5.75%) and employees (3.7%) has been fixed by law for over 20 years. For the public safety groups, an annual floating rate has been in effect since 1988. The exact rate, adjusted effective each July 1, is determined by IPERS' actuary and is intended to reflect *the portion of the higher system costs due to the more favorable benefits available to public safety membership*. One of the reasons this floating rate has declined modestly in recent years is a lessening of the difference in value of benefits between regular membership and those of the special groups.
[46] *Report to the Iowa Legislative Committee on Public Retirement Systems: Comprehensive Examination of Benefit Programs & Related Issues Pertaining to Public Safety Classifications within IPERS, POR & MFPRSI*, pp.19-20.
[47] Memberships of all three systems strongly expressed their wishes on this matter, apparently believing that any attempt to combine systems would lead to loss of membership control over their respective systems and the possibility of erosion of benefits in the future.
[48] *Report to the Iowa Legislative Committee on Public Retirement Systems: Comprehensive Examination of Benefit Programs & Related Issues Pertaining to Public Safety Classifications within IPERS, POR & MFPRSI*, p. 26.

Part Two: Guiding Principles for A Balanced And Fiscally Sound System

The *design* of any pension plan inherently reflects the values of both its original creators, and those who follow working to sustain and improve it. A *defined benefit* plan such as IPERS is intended to benefit primarily career employees who eventually retire under the System. This reflects the perceived value that the public owes its career employees a higher retirement benefit than members with fewer years of service, or those who sever membership in the system through taking a refund of their contributions upon termination of public employment. Even with all of the many changes made over the several decades of its existence, this orienting purpose of the Fund remains constant. However, changes to our plan design made in the 1990s have provided greater value to all of our members, even to those who never retire under the System.

Guiding Principles from Iowa Code Chapter 97D

In 1990, the Iowa General Assembly established long-term goals by which each public retirement system in the State was to guide itself and by which proposals for benefit enhancements should be measured.

> *1. The general assembly declares that legislative proposals for changes in specific public retirement systems should be considered within the context of all public retirement systems within the state, with emphasis on equity and equality among the systems. The following list of guiding goals shall apply to the consideration of proposed changes:*
>
> > *a. Select those benefit enhancement options which most successfully deliver the greatest good to the greatest number of employees.*
> >
> > *b. Choose those options which best correct existing inequities between and among the various retirement groups in the state.*
> >
> > *c. Determine those options which most ably serve the twin objectives of attracting and retaining quality employees.*
> >
> > *d. Avoid enacting further incentives toward earlier retirement with full benefits.*
> >
> > *e. Avoid further splintering of benefits by disproportionate enhancement of benefits for one group beyond those available to another.*

Additional Guiding Principles Developed by IPERS in Past Years

In our 1995 response to the Buck Study we also added some additional guiding principles for use in assessing proposed enhancements to the Fund. That articulation reflected years of our efforts to portray the impact of benefit enhancements with respect to both the demographic segments of our membership whom they were designed to benefit, as well as their financial cost to the Fund. We believe that these additional principles, coupled with those found in Chapter 97D, are of fundamental importance in helping us attain – and sustain - a balanced and soundly funded retirement plan.

1. As stewards of a public fund[49], we must balance our obligation to provide a generous retirement system - one which is competitive with other statewide retirement plans – with the need to be sensitive to public perceptions of the cost/benefit ratio of benefits received by IPERS' members. In this context, IPERS' formula is designed so that *a member's total retirement payout from IPERS and Social Security should not exceed 100% of the member's pre-retirement income at time of retirement.* As IPERS now allows a member to retire with a maximum of 65% of the member's highest average three years of covered wages, this – together with Social Security – will bring a member with 35 years of service into the 90% plus range.[50]

2. *Insofar as is possible, those members who receive the value of benefit enhancements should pay their proportionate share.*[51]

3. *Inter-generational equity must be preserved and protected: our benefit program must be designed with all of our members in mind* - the already retired, those nearing retirement, and those many years from retirement.[52] We believe that a well-designed pension system must not only fairly credit members' accrued values based upon such factors as years of service and earned wages, but also heed the special needs which the few sometimes have of the many: the disabled, those who have taken time from the work force to raise children (truly an *accrued value* to the larger society), or retirees struggling near the poverty line. A balanced perspective founded on inter-generational equity allows us to factor in the interests of all of our members.

4. *Individual equity*, while not the sole indicator of plan design balance, *is also important.* Insofar as is possible, neither retirees nor actives should receive disproportionate value relative to the other, and an active member's account value for service time should fairly reflect accrued value of their years of service and not their age.

5. *Weigh proposed enhancements as to their value for sound plan design many years from now.* Many proposals for benefit enhancement result from the latest "great idea" enacted

[49] The employer contributions to which is derived through taxation.

[50] As the average IPERS' member still retires with between 20 and 25 years of service, however, the vast majority of our membership can expect an IPERS' return of between 40% and 50% of his/her highest three average years of covered wages.

[51] Even where members are able and willing to pick up the additional cost themselves - in conjunction, of course, with the support of their public employer - we must be sensitive to how easily improvements for *some* quickly become goals for *others*. If not carefully monitored, this quickly becomes Plan design of the worst kind by incrementally adding uncoordinated elements.

[52] As it is difficult to fix a precise standard by which inter-generational equity can be achieved, we will attempt - in assessing the various proposed recommendations we will be making in this paper - to give each an *"inter-generational equity"* ranking.

by several states or proposed by an influential constituent group. Demographic pressures which may be relatively time specific also fuel others. We must weigh benefit proposals according to not only how they would affect our total membership today, but also as to how well they will serve us tomorrow.

Part Three: External Forces

A. Baby Boomer Retirements

We are just beginning to see the wave of interest in, and activity toward achieving, retirement among the "baby boom" generation[53]. This presents us with interesting challenges (including rising demands upon IPERS' staff), among them appropriate support for those wishing to take early retirement while also positioning us to offer suitable incentives to utilize older workers[54], who will be needed in a labor market which is predicted to be much tighter than that of recent years.

B. Continuing Debate Over, and Interest In, Fundamental Plan Design Issues

The debate over whether or not to replace, or supplement, public employees' core defined benefit plans with defined contribution plans remains an on-going discussion at the national and regional level. We caution that it is not likely to go away any time soon, for a number of reasons:

1. Some individuals legitimately believe they would be better off under a *defined contribution* plan. In the context of the amazingly resilient bull market, the risk of equities has come to appear to be severely diminished. Accordingly, being able to participate in the market as directly as possible appears to many as the surest way to near-term riches. They perceive that there is no significant "down side". A *defined contribution* plan allows them to participate in the market's experience directly.

2. There is a lot of money at stake. Public employee *defined benefit* plans together are responsible for more than **one trillion dollars**. There are many in the money management field who would dearly love to compete directly for those dollars, and for the sizable administrative fees management of individual accounts represents.

3. Some political forces believe that public retirement funds should only be in defined contribution vehicles. Much of this is fueled by their knowledge that defined contribution plans transfer investment risk from the employer and the retirement fund to the individual.

4. Some politicians – and some members – want to end the traditional emphasis on rewarding longer term employees by moving to a plan vehicle which more directly benefits younger, and short term, employees.

5. The ongoing debate over the future of Social Security – the arguments supporting it as well as various solutions proffered to "fix" it – also impacts peoples' assessment of the soundness

[53] Those persons born between 1947 and 1961. They have begun to retire and will impact our System with a significant rise in annual retirements through at least 2010.
[54] Either by inducing them to stay longer before retiring, or by welcoming them back after retirement into part-time employment.

and value of their public pension plans. If nothing else, it sows doubt and uncertainty, which can be fertile fields for scare-mongering.

We will need to continue to remain vigilant in explaining, defending, and preserving our defined benefit plan even while we remain open to creative ways to spread its values more evenly throughout our work force.[55] We continue to believe that our *defined benefit* plan is the better core vehicle[56] for retirement because:

1. Risk remains with the *employer*, not the employee. The ups and downs of the market will not erode the benefit the member earns, precisely because that benefit is determined by a formula, not by an accumulated amount the value of which is determined by the market.
2. Planning is more definite. An IPERS' member can reasonably project his/her retirement benefits, using clearly understood assumptions (years of employment, salary growth, age at retirement), then use that estimated retirement value to assist in other planning efforts, including supplementary savings accounts, retirement accounts, and insurance.
3. A *defined benefit* plan recognizes that public employees are members of a community; as such, we are able to help those who need our collective assistance through modest reallocations of portions of the Fund's assets – for disabled persons, for beneficiaries of members who die, and to counter the reality of females disproportionately bearing child rearing responsibilities and costs (and thus accruing, on the average, fewer years of service credited towards retirement) by subsidizing unreduced retirement benefits for them (1998's "62 and 20" rule).

C. Increased Complexity

Modern life seems to be steadily more complex, with a greater number of "choices" facing citizens every day. The same is true with regard to saving for retirement. Even as younger workers must juggle complicated decisions for day care, housing, and saving for college education, they are now expected to play a more significant role in deciding upon their retirement planning as well. They face a host of products, each claiming to be a primary tool in providing them with "financial independence" in retirement.

IPERS' covered employees are no exception. Each must ponder the fate of Social Security, while estimating the projected value of IPERS' benefits at retirement with the decision about participating in supplemental savings products offered by their employers.[57] The confusion and concern this can engender makes IPERS' continuing need for highly skilled and well-trained

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[55] Please see Dr. Metz's 1997 report on this issue, as well as comments on the matter contained in the 1997 companion to this present report.

[56] As we also said in 1997, the "best of all possible worlds" is a core *defined benefit* plan and a supplemental *defined contribution* plan.

[57] IPERS found in a 1998 study that almost three-quarters of its members had a supplemental plan *available* to them through their employer, the most common being tax-sheltered annuities offered through schools and deferred compensation through other governmental bodies. Overall, however, *participation* rates are no better than 40%-50%.

staff of the highest priority. Staff will need strong interpersonal, information, and systems skills and will require continuing training in pension policy and technology.

It is likely that, even with improved internet and other communication vehicles, we will continue to see an increase in the number – and length – of calls and interviews from and with our members as they attempt to "sort it all out". Members continue to expect personal attention from attentive and sympathetic human beings. Improved services will be necessary to remain competitive with other statewide public retirement plans.

D. Flexibility and Portability

Neither are especially new forces, yet the desire for both will likely continue to grow as the workforce steadily becomes more diverse with great variety of pension accrual among employees. It will be even more essential that their retirement plans provide flexible provisions allowing them to accrue, retain, and transfer service value from one employment situation to another. IPERS' current purchase of service laws, coupled with our recently improved portability provision[58], make us very competitive compared to other statewide pension plans.

Lastly, even though our move to an actuarially determined cost of service purchase was the correct move for the Fund, its impact on members may be to dissuade some persons from purchasing needed services. Going forward, IPERS should consider allowing installment payments, including payroll deductions, for service purchases.

[58] Effective July 1, 1999, terminated vested members taking a refund will receive, for the first time, a portion of their employer contributions plus accrued interest.

Part Four:
Overview of Recommendations for Additional Benefit Enhancements

Summary of Recommendations

We believe that IPERS has now reached the status of a "mature pension plan," soundly funded and with a balanced and competitive plan design. Nonetheless, we believe some additional enhancements to our plan design are justified[59]. In summary, they are:

1. **Giving IPERS' special public safety occupations the same kind of disability benefits enjoyed by those public employees covered by the Municipal Fire and Police Retirement System of Iowa and the Peace Officers Retirement System;**
   Cost: Significant, but covered by increased contribution rates for these members and their employers.
   Recommended Enactment & Implementation Date: July 2000

2. **Increasing the Cost of Living Adjustment (COLA) for members who retired prior to July 1990 from 80% of the Consumer Price Index (CPI) to 100%,[60] while retaining the existing ceiling on annual distributions at a maximum of 3% above the preceding year[61];**
   Cost: None[62]. In order to cover our maximum possible liabilities, our actuary already projects future payouts to retirees at the maximum of 3% per year.
   Recommended Enactment & Implementation Date: July 2000

3. **Placing a cap on the FED Reserve Fund equivalent to 10 years of maximum payouts;**
   Cost: None. It will actually allow monies which otherwise would be deposited in a larger than needed FED Reserve Fund to be used for: other benefits, and/or paying down any unfunded liability, and/or paying a Supplemental Account for Active Members (SAAM) distribution.
   Recommended Enactment & Implementation Date: January 2000

4. **Moving from the Current *Rule of 88* to the *Rule of 85*[63];**
   Cost: Significant.[64]

[59] And are supported by the various Buck Consultant and benefit parity reports, as referenced above.
[60] This was part of our 1997 recommended package.
[61] The impact of this on the *Favorable Experience Dividend (FED)* is expected to be similar.
[62] With reference to the general "cost" footnote, increasing the COLA to 100% does not impact the System's funded status, or the time to amortize its unfunded liabilities, because the actuary already projects future liabilities *as if* IPERS will be paying the maximum 3%. This is, of course, a *conservative* measure as it ensures we factor in the highest possible future liability represented by COLA increases. Obviously, too, however, the *actual cash payouts* resulting from using 100% of the CPI will be higher than they would have been under the present 80% of the CPI.
[63] This was also part of our 1997 recommended package.

Recommended Enactment Date: July 2000
Implementation Date: In Increments of One Year, and in Those Calendar Years when IPERS Determines Its Costs Can be Absorbed within Existing Contribution Rates and in Accord with its Funding Policy.[65]

5. **Improving the death benefit for the beneficiaries of those members who die before initiating retirement[66];**
   Cost: Modest.[67]
   Recommended Enactment Date: July 2000
   Implementation Date: When IPERS Determines Its Costs Can be Absorbed within Existing Contribution Rates and in Accord with its Funding Policy.

6. **For our public safety employees, establishing a fixed rate structure sufficient to both fund the costs of the existing benefit program plus disability and to provide a margin for the purchase of additional enhancements for the special groups in the future:**
   - ✓ Equalize Number of Years Required to Establish 60% Formula at 22
   - ✓ Provide Credit for a Maximum of Eight Years of Service beyond 22 Years
   - ✓ Provide Same Credit per Year of Service

   Cost: Significant. To be paid within the higher, fixed rates recommended here.[68]
   Recommended Enactment Date: July 2000
   Implementation Date: For Fixed Rates: July 2000; for Other Benefit Enhancements towards Parity when IPERS Determines Its Costs Can be Absorbed within the Fixed Rates Established in 2000 and in Accord with its Funding Policy.

7. **For *adjunct instructors* who work for the community colleges, the right to elective coverage be extended only to those who already have an IPERS' account;**
   Cost: Nonexistent (for the Fund, but are a definite factor for the community colleges).
   Recommended Enactment & Implementation Date: July 2000

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[64] "Significant" in this context means that the effect of enacting this enhancement, because the cost would be shared by the entire System, would likely lengthen the *time to fully amortize* the unfunded liabilities of the System by three or more years.

[65] This same kind of delayed implementation date was used by the 1990 General Assembly when it directed IPERS to increase the formula multiplier over time from the then maximum of 50% to 60%. The exact wording is found in Section 28 (b), second unnumbered paragraph of House File 2543, passed by the 1990 General Assembly: **Commencing July 1, 1991, the department shall increase the percentage multiplier of the three-year average covered wage by an additional two percent each July 1 until reaching sixty percent of the three-year average covered wage if the annual actuarial valuation of the retirement system indicates for that year that the cost of this increase in the percentage of the three-year average covered wage used in computing retirement benefits can be absorbed within the employer and employer contribution rates [currently] in effect....**

[66] This was also part of our 1997 recommended package.

[67] "Modest" in this context means that the effect of enacting this enhancement, because the cost would be shared by the entire System, would likely lengthen the *time to fully amortize* the unfunded liabilities of the System by one or two years.

[68] As a consequence, these would not impact the time to amortize the System's unfunded liabilities.

8. **Replacing our existing "calendar year" for the computation of benefits to "12 contiguous quarters";**

   Cost: None, except for some administrative costs within IPERS.
   Recommended Enactment Date: July 2000
   Implementation Date: July 2001

9. **Allowing elected officials other than legislators to terminate their full-time IPERS' covered positions and retire without having to resign from their elected positions;**

   Cost: None.
   Recommended Enactment & Implementation Date: July 2000

10. **Adjustments to the retirement formula for the higher paid, including increasing the "default" standard by $10,000 per year beginning January 2000 and freezing the multi wage year averaging at the current six, and to return to the average of the highest three salary years effective January 2002;**

    Cost: Insignificant. The cost of paying for the benefits of the higher paid has never been a fiduciary issue for IPERS.
    Recommended Enactment & Implementation Date: January 2000

11. **Creating a "pop-up" option for retirement Option 4 to Option 2 upon a contingent annuitant's death (occurring before the member's death), to be paid for actuarially by members choosing it; and**

    Cost: None.
    Recommended Enactment & Implementation Date: July 2001

12. **Raising the ceiling on re-employment wages for the 2% of IPERS' retirees who have returned to covered employment from $12,000 to $25,000.**

    Cost: Insignificant.
    Recommended Enactment & Implementation Date: July 2000

Long Term Goals and Segments of Membership Served by These Recommendations

To Protect IPERS' Retirees, Current and Future

2. Increasing the COLA payable to the pre July 1990 retirees from "80%" of the Consumer Price Index to "100.

3. Placing a cap on the *Favorable Experience Dividend (FED)* reserve fund equivalent to 10 years' worth of estimated payments.

11. Create a "pop-up" option for existing *Option 4.*

12. Raise the current ceiling on wages earned in re-employment by retired members before IPERS begins reducing their IPERS' retirement benefit from the current $12,000 to $25,000.

To Allow for More Orderly Retirement

4. Minimize the "window" or "cliff" approach to retirement, in which certain classes of people receive more favorable treatment than others by enacting a *Rule of 85* (This was also part of our 1997 recommended package.)

9. Allowing elected officials other than legislators to terminate from their full-time IPERS' covered positions and retire without having to resign from their elected positions;

To Create a More Uniform Value per Year of Service for All Members

5. Increasing the value of the death benefit paid to active members by giving the member's designated beneficiary the option of receiving either a lump sum payment – or an annuity – of the present value of the member's accrued benefit at date of death, adjusted for the beneficiary's estimated lifetime. (This was also part of our 1997 recommended package.)

7. Giving *adjunct instructors* who work for the community colleges the right to elective coverage be extended if they already have an IPERS' account;

To Better Harmonize with the Educational Membership of IPERS' System and Create Better Understanding by Members of the Computation of Their Retirement Benefits

8. Amending the Iowa Code to allow for the use of "12 contiguous quarters", rather than the current "3 calendar years", for purposes of accruing service credit and computing retirement benefits.

To Advance the Achievement of Parity Of Benefits among Similar Classes of Employment in the Field of Public Safety[69]

1. Creating *ordinary* and *in-service related* disability benefits for members of IPERS' public safety groups similar to those enjoyed by members of the Peace Officer Retirement System and the Municipal Fire and Police Retirement System of Iowa;

6. Instituting a fixed contribution rate for both employers and employees of IPERS' special service groups; and within the margin allowed by this fixed contribution rate, grant the other enhancements as recommended in the 1998 parity study.[70]

To Address the Problem Facing the "Higher Paid" Portion of IPERS' Membership

10. Allowing the existing standard of $55,000, reached in January 1999, to increase annually by $10,000, beginning January 2000; and freeze the number of years used in the calculation of a member's retirement benefit at the present six rather than rising to seven, as is scheduled to happen under existing law in January 2000.

[69] All of the following were recommended in the *Benefits Parity Study* of 1998.

[70] Allowing members of IPERS' special groups to retire with a 60% formula at age 55 with 22 years of service, and giving them service credit for up to eight additional years beyond 22 years of service with an additional multiplier accrual of 1.5% for each additional year of service.

Sources of These Recommendations

In our planning efforts during the past few years, our central focus has been to identify what further *incremental* enhancements may still be needed to "flesh out" our plan design in order to achieve greater balance and equity for all of our members. The recommendations in this paper come from three primary sources:

1. Action items from our 1997 report[71] which were not passed in the 1998 Legislative session;
2. Proposals arising from legislatively mandated special studies: 1998-1999; and
3. Suggestions arising from discussions with members, legislators, staff, and the Constituent Group.

Recommendations from our 1997 Report Not Passed in the 1998 Legislative Session

Productive as it was, the 1998 session of the General Assembly did not address all of the recommendations IPERS made to it for benefit enhancements that year. Thus, some of our recommendations for the 2000 session of the Legislature are re-endorsements of them. These include:

- Increasing the Cost of Living Adjustment (COLA) for members who retired prior to July 1990 from 80% of the Consumer Price Index (CPI) to 100%, while retaining the existing ceiling on annual distributions at a maximum of 3% above the preceding year;
- Passing the "Rule of 85"[72]; and,
- Improving the death benefit for the beneficiaries of those members who die before initiating retirement.

Recommendations Arising from Legislatively Mandated Special Studies: 1998-1999

Benefits Parity Report

This was issued in the autumn of 1998 by the three retirement systems participating in the study: IPERS, the Peace Officer Retirement System (PORS), and the Municipal Fire and Police Retirement System of Iowa (MPRSI).[73] Its relevant recommendations for IPERS' special service groups (public safety employees) are:

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[71] *To the Governor and General Assembly: A Report Regarding Plan Design, Multi-Year Benefit Enhancements and Contribution Rates for the Iowa Public Employees' Retirement System*, September 1997, Greg Cusack, Chief Benefits Officer, IPERS.

[72] Our 1998 recommendation included both the Rules of "85" and "62 and 20". The Legislature passed the latter.

[73] For greater detail, please see: *Report to the Iowa Legislative Committee on Public Retirement Systems: Comprehensive Examination of Benefit Programs & Related Issues Pertaining to Public Safety Classifications within IPERS, POR & MFPRSI*, p. 18.

1. Disability coverage equivalent to that enjoyed by members of PORS and MFPRSI
2. Equalize number of years required to establish 60% formula at 22[74]
3. Provide same credit per year of service[75] for at least 30 years of service[76]
4. Provide same credit per year of service[77]
5. End fluctuating contribution rates by establishing a fixed rate structure

IPERS endorses all of these recommendations, and recommends the following priority for enactment:

1. Expanded disability for all 5,263[78] IPERS' special service members.
2. Establishing a fixed rate structure sufficient to both fund the existing benefit program as well as disability and to provide a margin for the purchase of additional enhancements for the special groups in the future.
3. Buying, over time and from any existing margin between the established and needed contribution rates, the remainder of the parity enhancements:
   - Equalize Number of Years Required to Establish 60% Formula at 22
   - Provide Credit for a Maximum of Eight Years of Service beyond 22 Years
   - Provide Same Credit per Year of Service

Adjunct Instructors Report

The Legislature asked IPERS to investigate whether or not *adjunct instructors* at the State's community colleges should be eligible for IPERS' coverage. Under current law, and as long as they continue to meet the Code[79] definition of *adjunct instructor*, they are excluded from coverage. In a collaborative effort with the community colleges, IPERS' conducted a survey of adjunct instructors and recommends[80] to the General Assembly that:

1. The right to elective coverage be extended only to those adjunct instructors who already have an IPERS' account[81]; and,

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[74] Currently, members of the PORS and MFPRSI – and sheriffs, deputy sheriffs, and airport fire fighters in IPERS (27% of IPERS' members who in public safety related positions) – earn 60% for 22 years of service, while the remaining 73% of IPERS' public safety members must work 25 years to earn 60%. The value of each year of service for those who earn 60% after 22 years is 2.727% for each year of service, while it is but 2.4% for those who accrue 60% at 25 years.

[75] Members of MFPRSI, PORS and IPERS' sheriffs, deputy sheriffs, and airport firefighters receive 1.5% credit for years of service beyond 22, while the rest of IPERS" special service members receive 1%.

[76] Members of the MFPRSI and IPERS' sheriffs, deputy sheriffs, and airport firefighters can receive credit for up to eight years of service beyond the 22 necessary to earn 60%. Members of the PORS can receive credit for up to 10 years beyond 22 years of service, while the rest of IPERS' special groups can only receive credit for a maximum of 5 years of service beyond 25.

[77] Members of MFPRSI, PORS and IPERS' sheriffs, deputy sheriffs, and airport firefighters receive 1.5% credit for years of service beyond 22, while the rest of IPERS" special service members receive 1%.

[78] As of the end of the first quarter, 1999.

[79] See Iowa Code section 97B.1A (8)(a)(3).

[80] Please see *Report to the General Assembly on Whether or Not Persons Employed by Community Colleges as Adjunct Instructors Should be Eligible for IPERS' Coverage*, Greg Cusack, Chief Benefits Officer, Iowa Public Employees' Retirement System, September 1, 1999.

[81] Including those with both an *inactive* and *active* account.

2. Consideration be given to providing additional revenue for the community colleges in order for them to cover their increased salary-related costs so that adjunct instructors do not have to see their take home salary reduced.

Recommendations Arising from Discussions with Members, Legislators, Staff, IPERS' Actuary, and our Constituent Group

Interest in the IPERS' plan remains high between legislative sessions, too, and we are constantly encountering persons who have questions about – or proposals regarding – possible future benefit enhancements. Some of these subsequently arise to the level of actual recommendations which we make to the General Assembly, others become the subject of more focused study in the months ahead, and a relative few are discarded after investigation.

Some of these which we felt merited consideration to you for the 2000 session are:

1. Allowing elected officials other than legislators to terminate from their full-time IPERS' covered positions and retire without having to resign from their elected positions (raised by IPERS, IPERS' members, the Constituent Group, legislators, and the Governor's office);
2. Options on how to address the issue of *substitute teachers* for whom the existing *bona fide retirement* provision is thought to be too restrictive (raised by legislators);
3. Options on how to make IPERS more "school year friendly" (raised by IPERS' staff, the Constituent Group, and school representatives);
4. Placing a "cap" equivalent to 10 years' maximum payouts (e.g., @ 3% annually) on the *Favorable Experience Dividend (FED)* Reserve Fund;
5. Adjustments to the retirement formula for the higher paid (raised by IPERS, IPERS' members, the Constituent Group, and legislators);
6. Adjusting the ceiling on re-employment wages for the 2% of IPERS' retirees who have returned to covered employment (raised by IPERS' staff); and;
7. Require spousal signatures for member desired changes in beneficiaries, whether the member is active or retired.

8.

Part Five:
In Depth Analyses of Major Recommendations For Additional Benefit Enhancements

Recommendation #1: For All IPERS' Public Safety Occupation Members:

That IPERS provide enhanced disability benefits similar to those offered similar public employees covered by the Peace Officer Retirement System (PORS) and the Municipal Fire and Police Retirement System (MFPRSI).

Discussion

IPERS covers a significant number[82]of public employees engaged in public safety related jobs. Of the 3.5% of IPERS' active membership who are in these *special service* categories, 2,439 work for the State: as correctional officers (2,190), Department of Transportation weight officers (113), or Department of Natural Resources conservation police officers (136).

Another 1,411 work for the counties as sheriffs and deputy sheriffs and another 1,413 work for city government in police and fire positions. IPERS also covers a total of 31 airport firefighters and airport safety officers.

Like their colleagues in the POR and MFPRSI systems, they face inherent risks by the nature of their occupations, risks they assume on behalf of the rest of us. However, unlike their colleagues covered by the other two systems, they do not have expanded disability coverage beyond what is already afforded them through IPERS.

Like all IPERS' members, should they become disabled *according to Social Security* standards, they would be able to retire without incurring any reduction in their earned benefit because of "early" retirement. Indeed, should they be younger than 55, they would still be allowed to begin IPERS' benefits.[83]

POR and MFPRSI members, while not eligible for Social Security coverage, have two different levels of disability available to them: a) if they become disabled[84] in a service related incident, they would be eligible for 60% of the average of their highest three salary years for the remainder of their disability; or b) if they became disabled in a non-service related incident, they would be eligible for 50% of the average of their highest three salary years for the remainder of their disability.

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[82] A total of 5,263 persons. These and other demographic figures appearing both in the body of this text, and in the attached demographic report, are taken from 1st quarter 1999 IPERS' data.
[83] Persons who are disabled according to Social Security are the only members who can retire prior to age 55.
[84] A determination made ultimately by their retirement system, following employer and medical board reviews.

Application of Guiding Principles[85]

Equity Scale:

1) Conforms to guidelines of 97D: Yes.

   a) *Greatest good to greatest number*: This would potentially benefit all members of these special groups.

   b) *Corrects existing inequities:* Yes. It is not equitable that this sizable segment of public safety workers should not have the same level of disability benefits available to them as to those who work for employers covered by their sister retirement systems.

   c) *Serves to attract and retain qualified employees:* We believe it would be positive for both purposes, especially for smaller towns who often lose their police officers to larger communities.

   d) *Avoids offering further incentives toward earlier retirement with full benefits:* Yes.

   e) *Avoids splintering benefits by disproportionately rewarding one group over the general membership:* It delivers equity *within* the public safety group.

2) Equity: Yes.

3) Cost: As the cost[86] is to be paid by members and their employers, there is no overall cost impact to the System.

4) Demographic group(s) affected: All public safety employees covered by IPERS.

5) Future Plan Design: Positive. As part of our recommendations for over-all parity among and between public safety employees covered by the three systems, it would make IPERS' plan design comparable to our sister Iowa systems for this segment of our membership.

Discussion of Related Special Study

In the summer and early autumn of 1998, I worked with Dennis Jacobs, Executive Director of the MFPRSI, and Carroll Bidler, Chief Financial Officer for the PORS, in studying the entire issue of benefits *parity* between and among our three systems' public safety membership. This was in response to a directive from the 1998 General Assembly.

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[85] As discussed in Part Two above.

[86] The proposed hike in contribution rates would also cover IPERS' anticipated additional administrative costs related to expanded disability coverage.

Our subsequent report[87] found many areas of *dis*parity between our three systems. In most cases, including that of disability, IPERS was the system which had to "catch up" for those members. (The exception was that we provide Social Security coverage in addition to that of our pension plan; members of the other plans are not covered by Social Security.) We remain hopeful that the General Assembly will adopt all of our recommendations for benefit parity for these members of the three systems.

[87] Please see *Report to the Iowa Legislative Committee on Public Retirement Systems: "Comprehensive Examination of Benefit Programs & Related Issues Pertaining to Public Safety Classifications within IPERS, POR, & MFPRSI"*, submitted on November 2,1998, pp. 6-18.

Recommendation # 2: For Those Retirees Currently Receiving a Cost of Living Adjustment (COLA)

That the COLA Paid to Pre-July 1990 Retirees be Increased from 80% to 100% of the Consumer Price Index, retaining the cap of a maximum of 3% annually.[88]

Discussion

In our 1995 report to the Governor and Legislature,[89] we recommended the existing 80% limitation as a method of cost control for the new COLA program.[90] In testimony before both the interim committee on public retirement plans and the standing committees of State Government, however, we also spoke of our hopes to keep the broad spectrum of our membership's retirement benefits at 80% of their original purchasing power at the time of retirement. This was to be done in two ways: first, through the implementation of the minimum benefit program which, in conjunction with dividends currently being paid to pre-July 1990 retirees, would raise most retirees to that 80% target; and, second, through the inception of the annual COLA program which would maintain that 80% target level. The Legislature adopted both recommendations.

In our 1997 report, cognizant of the fact that a growing number of our members had retired after June 1990 and therefore, were not eligible for any kind of post-retirement adjustment or supplement, we recommended the institution of the *Favorable Experience Dividend* program. The Legislature responded, and the first ever *FED* was paid in January 1999.

Although the language governing the paying of the *FED* does not require IPERS to make that dividend identical to the COLA paid to the members who retired prior to July 1990, we recognized that for a whole number of reasons it would be desirable to use the COLA dividend as the target dividend[91] for the *FED*.

By 1997, we had also come to appreciate the fact that our current 80% of the CPI formula would only ensure that our retirees lost ever more purchasing power. Thus we recommended then, and endorse again today, our proposal to change the formula to 100% of the CPI, while retaining the maximum payout of 3% above the previous year's dividend.

Application of Guiding Principles

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[88] This would also affect the target dividend level which IPERS' staff references before setting the FED.

[89] *A Report to the Governor and General Assembly Regarding Guiding Principles of, and Recommendations for Benefit Enhancements to, the Iowa Public Employees' Retirement System*, October 1995.

[90] The Legislature followed our recommendation and converted the existing ad hoc cost of living adjustment program (where members received an adjustment without any guarantee that it would be reflected in their base annual pension distribution) into a genuine COLA program whereby the recipients' total annual distribution does increase steadily over time.

[91] So that, everything else being equal, we would seek to match the annual COLA dividend with the *FED* dividend.

Equity Scale:

1) Conforms to guidelines of 97D: Yes.

   a) *Greatest good to greatest number*: This would benefit all retired members.

   b) *Corrects existing inequities:* Yes. While we have set our goal as desiring to preserve the purchasing power of retirees throughout retirement, setting the COLA as less than 100% of the impact of inflation guarantees they will fall behind.

   c) *Serves to attract and retain qualified employees:* A well functioning post-retirement supplement program is a very attractive feature of a defined benefit retirement plan.

   d) *Avoids offering further incentives toward earlier retirement with full benefits:* Yes.

   e) *Avoids splintering benefits by disproportionately rewarding one group over the general membership:* Yes. All retirees.

2) Equity: Yes.

3) Cost: No actuarial consequence as IPERS' actuary already projects these costs at the maximum of 3%.

4) Demographic group(s) affected: All retirees, existing and future.

5) Future Plan Design: Positive. We would like to preserve retirees' purchasing power.

Discussion of Related Special Study

In his 1997 Report and Recommendations on Enhancements to the Core Benefit Structure and Supplemental Plans and Features of the IPERS Defined Benefit Plan,[92] Dr. Metz notes that the original 80% of the Consumer Price Index limitation was proposed primarily for cost control reasons. He further observes that if our goal is truly to attempt to maintain those retirees' purchasing power at 80%, a policy of awarding a COLA based on 80% of the total CPI (even allowing for the maximum payment allowed of 3% per year) is certain to ensure the decline of purchasing power over time. He, therefore, recommended that we move the figure to 100% of the CPI while retaining the limitation on the maximum increase in any one-year at 3%.

[92] Pp. 39-40.

Recommendation # 4: To Assist Employees and Employers Alike Prepare for Orderly Retirement Transitions by Redefining "Normal Retirement" to Allow for Earlier Retirement

That, effective July 1, 2001, or as soon thereafter as IPERS determines in consultation with its actuary that the costs of this enhancement can be achieved without any increase in contribution rates or in violating IPERS' Funding Policy, IPERS allow members who attain the Rule of 85 (at a minimum age of 55) to retire without any otherwise applicable early retirement adjustment. If IPERS determines in conjunction with its actuary that the full Rule of 85 cannot be achieved in one step, IPERS be given the authority to implement the change from the present Rule of 88 to an eventual Rule of 85 in one year increments.

Discussion

Whether or not to eliminate the otherwise applicable age reduction factor at ever-lower combinations of age and service has been central to discussions among IPERS' staff and its constituent groups for at least a decade. Both IPERS and its constituent representative members agree that permanent eligibility criteria (such as established through the existing *Rule of 88*) are preferable to the ad hoc programs which occasionally were implemented by the state and other public employers throughout the latter half of the 1980s and the early years of the 1990s.

IPERS, while supporting the creation of the initial *Rule of 92* in 1988, was initially cautious in embracing lowering such *Rules*. Key constituent groups have consistently argued, however, that *Rules* which allowed more of IPERS' members[93] to consider retirement without suffering an early retirement reduction in their benefits would allow "burned out" members to leave employment while creating opportunities for new workers to take their place. In any case, they said, keeping positions filled by "chaining" people to their desks out of fear of reduced lifetime benefits was not a sound management policy.

Over the years, I have come to better understand that IPERS' various *Rules* have functioned less as an early retirement mechanism than as a means of *erasing otherwise applicable reductions which cause many people to delay their decision to retire*. In other words, the substantial 3% per year reduction in benefits which IPERS applies to persons who do not meet "normal"[94] retirement acts as a disincentive, *distorting* their retirement decision. Insofar as is possible, it is preferable that the retirement system be *neutral* regarding when a member leaves. Everything else being equal, members should be free to decide to leave employment based upon a number of factors, including their accrued benefits, their health (and that of their spouse), their job satisfaction, and their comfort level with retirement. The *Rule of 85* would make it possible for a larger pool of persons to decide freely when it is best for them to retire. Also, because it applies to a larger pool of people than the *Rule of 88*, it conveys the benefit of eliminating the otherwise applicable early retirement reduction to many more retiring members.

[93] Who were already eligible by age – at least 55 – to consider retirement.
[94] Currently, age 65 for all, or "62 and 20" for those who are at least 62 years of age with at least 20 years of service, or the "Rule of 88".

If some persons are concerned about making it easier (often argued, "too easy") for persons to retire, they might look to occasional *employer* behavior whereby various incentives are offered to select, narrow bands of employees to get them to elect to retire earlier than they otherwise might. *Both* incentives to retire, and incentives to stay, are best and most appropriately handled by the *employers*. The retirement system should be neutral.

Relevant Data

Almost 27,000 of IPERS' currently active members (18% of all active members) are currently eligible by age to retire; that is, they are 55 or older. Of this number, a total of 4,114 (15% of all eligible for retirement by age) meet the criteria for the *Rule of 88*.[95]

Those eligible to retire under a future *Rule of 85* number an additional 2,299 which, when added to the existing *Rule of 88* eligible pool, would make 24% of those already 55 or older eligible under the *Rule of 85*.[96] (It is important to note that historically only about 25% of those eligible for a particular *Rule* retire. For a variety of reasons, the vast majority of those eligible work beyond their earliest eligibility date. We have no reason to believe that the experience of the System under a *Rule of 85* would be any different.)

Application of Guiding Principles

Equity Scale:

1) Conforms to guidelines of 97D: Mixed. Specifically:

a) *Greatest good to greatest number*: No. While it significantly expands the number of persons otherwise eligible for retirement who could potentially take advantage of it – for persons retiring now and into the future – the cost of this program (as have the earlier *Rules of...* before it) would be borne by the entire System.

b) *Corrects existing inequities:* No. While IPERS may not be as competitive vis-a-vis other systems in this area, our existing standards for normal retirement are not inequities. However, this is an area – demonstrated in Dr. Metz's reports – where IPERS is at a competitive disadvantage vis-à-vis other statewide systems.

c) *Serves to attract and retain quality employees:* Attract, yes; retain, yes, for mid-career employees, especially.

d) *Avoids offering further incentives toward earlier retirement with full benefits:* No. Directly violates this provision.

[95] The proportion of school employees is higher by 9% (58%) than their share of all actives – 49%. The State's share is also higher than its segment of the total active population (19% compared to 16%).
[96] Of whom 61% are school employees. The state's segment, on the other hand, drops to 14% (from 19% eligible for the Rule of 88). Members potentially eligible for this rule average 28 years of service and are 59 years of age.

e) *Avoids splintering benefits by disproportionately rewarding one group over the general membership:* No, and yes. No, in that the general membership subsidizes the costs of all such *Rules of...* programs, which benefit less than a majority of our members. Yes, in that taken together, these benefit more potential retirees than any prior program. A *Rule of 85* is far more attainable by more people than the original *Rule of 92*, for instance.

2) Equity: *Inter-generational*: Mixed. *Individual*: Mixed.

3) Cost: Significant: It would increase the time to amortize our unfunded liability by two or more years.[97]

4) Demographic group(s) affected: About 25% of the current population of active members who are 55 or older.

5) Future Plan Design: Demographics suggest that this has become such a prominent issue in recent years because of the large number of baby boomers who are just beginning to enter, or ponder entering, retirement.[98]

Discussion of Related Special Study

In endorsing the strong sentiment for a *Rule of 85* from IPERS' Constituent Group members, we also acknowledge both the argument and the proposals made by Dr. Metz in his paper Report and Recommendations on Enhancements to the Core Benefit Structure and Supplemental Plans and Features of the IPERS Defined Benefit Plan[99] where he supported the *Rule of 85* and the companion measure of *"62 and 20"*. We supported both recommendations in 1997. As the General Assembly did make "62 and 20" law effective July 1, 1998, we repeat our support for the enactment of the *Rule of 85* during the 2000 General Assembly.

In addition, it is useful to cite the conclusion of an inter-agency cooperative task force on the issue of early retirement that not only was retirement policy really a component of management policy, but also that early retirement "windows" are an undesirable form by which to encourage people to consider retiring. Rather, permanent conditions by which people - employer and employee alike - can plan for retirement were strongly encouraged. The *Rule of 85* is just such a "permanent" solution for which all members, and their employers, can plan and take into account.

[97] More precise numbers will be available sometime in the November-December 1999 period.
[98] This is also supported by the recent dramatic surge in member demand performance measures which Retirement Benefits' staff tracks annually.
[99] Pp. 20-28.

Recommendation # 5: Improving the Death Benefit for Active Members

That, effective July 1, 2001, IPERS increase the value of the death benefit paid to the beneficiaries of members who die before retiring by providing their survivor(s) with the option of taking either the death benefit payable under today's law or, as an alternative, selecting a payout equivalent to the members' actuarial present value of their benefit at time of death, with the survivors choosing to receive this benefit either as a lump sum or as an annuity.

Discussion

We are aware that on a comparative basis our current death payout for beneficiaries of members who die before retirement could be more favorable. In addition, we recognize that the plight of the survivors of members who suffer such premature deaths is often significant. Our proposal would provide the beneficiaries benefits more commensurate with that of survivors of members who retire under the system.

Application of Guiding Principles to Proposal

Equity Scale:

1) Conforms to guidelines of 97D: Yes. Specifically:

a) *Greatest good to greatest number*: This enhancement would benefit all of the beneficiaries of our members who die before initiating retirement.[100] While admittedly impacting a relatively small number of persons, we recognize that death at any age can have tragic consequences for those left behind. This proposal would provide spouses, children, or other beneficiaries left to cope when members die in the prime of life with a much-improved benefit.[101] While IPERS provides reasonable death benefit options for those members who attain retirement, its payout for longer served members who die before reaching retirement needs to be improved.

b) *Corrects existing inequities:* Yes. We do not currently annuitize any payments to survivors of members who die before retirement, nor is the value received by survivors of longer-termed members related to the value of the member's accrued benefit at the time of death.

c) *Serves to attract and retain quality employees:* A mild plus factor.

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[100] Approximately 453 persons (.3% of our non-retired members) die each year.

[101] The disparity between the death benefit available to beneficiaries of *retired* members versus *active* members is greatest as the member nears retirement. For much younger people, the existing death benefit *may* still be superior. This is why we are recommending that the beneficiary have a choice between today's death benefit and the enhancement proposed here.

d) *Avoids offering further incentives toward earlier retirement with full benefits:* Does not apply.

e) *Avoids splintering benefits by disproportionately rewarding one group over the general membership:* Yes. This would be a proportionate award of accrued benefits.

2) Equity: *Inter-generational*: Yes (retired members already have available to them a much better, actuarially determined death benefit selection). *Individual*: Yes.

3) Cost: Modest.

4) Demographic group(s) affected: A very small number of our 151,000 active members – under 400 persons annually.

5) Future Plan Design: We believe this proposal has a favorable over-all impact on plan design.

Discussion of Related Special Study

In his 1997 study, *Report and Recommendations on Enhancements to the Core Benefit Structure and Supplemental Plans and Features of the IPERS Defined Benefit Plan*, Dr. Metz recommends "that the survivor benefit be increased to provide greater protection for the younger, shorter-service employee.... For longer service members, the members' accrued normal retirement benefit would be payable as a 100% joint-and-survivor annuity, if greater." He also proposes that, where "a death is the result of an accident incurred in the performance of duty," an alternative to the regular death benefit would be "a survivor pension equal to 50% of final average salary payable to a surviving spouse, dependent children, or dependent parents" and subject to a COLA.[102]

IPERS accepts his premise that our survivor benefits for members who die before retirement are not as adequate as we (and others) would like. In a variation of his proposals, we propose that our survivor benefits be enhanced by providing either a lump sum benefit, or an annuitized payout of the actuarial present value of the accrued benefit members had earned under our formula current to the time of death. We also believe that this enhanced survivor benefit ought not be limited to family members (as the designation of the beneficiary is the member's right). Our proposal enhances the payout without exceeding the amount actually earned by members at the time of their deaths.

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[102] *Report and Recommendations on Enhancements to the Core Benefit Structure and Supplemental Plans and Features of the IPERS Defined Benefit Plan*, 1997 Report, p. 36.

Part Six:
Briefer Analyses of Other Recommendations For Additional Benefit Enhancements

Recommendation # 3: For All Members of the System

That, effective January 1, 2000, a cap equivalent to 10 years anticipated payout of maximum dividends be placed upon the separate reserve from which the Favorable Experience Dividend is paid.

Discussion

When the 1998 General Assembly approved our recommendation for the creation of a *Favorable Experience Dividend (FED)*, it also required us to establish a separate reserve fund (within the IPERS' Trust Fund) **and** to allocate funds there sufficient to pay *five years' worth* of maximum (3%) dividends. IPERS complied and, after establishing this separate reserve with the stipulated amount, paid the first ever FED in January 1999.

In the months since, as we have prepared for future years' accumulations to, and distributions from, this fund, we have discovered that without any limitation on the maximum size of this fund it will devour the lion's share of all *favorable experience* and continue to grow in size.

Our concerns about this are twofold:

1. *The fund only has to be of a certain size to ensure that distributions will very likely be made every year.*
   Both our actuary, Pat Beckham of Milliman and Robertson, and IPERS' Chief Investment Officer, Kathy Comito, believe a fund equivalent to 10 years worth of maximum distributions *should* be quite adequate.[103]

2. *Without such a cap, the existing law directs IPERS to funnel much of any year's favorable experience into this separate reserve[104], when some of this amount could*

[103] IPERS' Chief Investment Officer Kathy Comito says that 10 years is greater than two "typical public market cycles" and, therefore, should be sufficient to weather occasional market downturns or corrections, even if sustained for many months.

[104] IPERS has attempted to creatively allocate the percentage of the favorable experience available for the reserve in the following manner. Taken from the Iowa Administrative Code 581--21.30(97B) Favorable experience dividend under Iowa Code section 97B.49F(2).

21.30(1) Allocation of favorable experience. The department shall annually allocate the system's favorable actuarial experience, if any, between the reserve account created under Iowa Code section 97B.49F(2) and the remainder of the retirement fund according to the following schedule.

also be used to: pay for additional benefits as directed by the Legislature, or pay down any existing unfunded liabilities of the Fund, or assist in IPERS making SAAM[105] *payments.*

Without a cap, the FED fund's continual expansion might truly have unintentional consequences, including making it more difficult to rapidly pay down any unfunded liabilities and, therefore, delaying any or further payments of a SAAM.[106]

Years to Amortize Unfunded Liability	Percentage to FED Reserve	Years to Amortize Unfunded Liability	Percentage to FED Reserve
20	0	9	27
19	5	8	31
18	6	7	36
17	7	6	42
16	8	5	49
15	9	4	57
14	11	3	66
13	14	2	77
12	17	1	90
11	20	0	100
10	23		

The portion of the favorable actuarial experience, if any, that is not initially credited to the reserve account using the foregoing table, but which, if applied to the retirement fund, would result in the actuarial valuation of assets exceeding the actuarial accrued liability of the system based on the most recent annual actuarial valuation of the system, shall be credited to the reserve account.

21.30(2) Determination of applicable percentage. The department shall have sole discretion to determine the applicable percentages that will be used in calculating favorable experience dividends payable under this rule, if any, subject to the actuary's certification that the resulting favorable experience dividends meet the requirements of Iowa Code section 97B.49F(2) and this rule.

a. The department's annual applicable percentage target for calculating dividends under Iowa Code section 97B.49F(2) shall be equal to the applicable percentage used in calculating dividends payable to retirees under Iowa Code section 97B.49F(1). Notwithstanding the foregoing, the department may set a greater or lesser applicable percentage for calculating dividends under this rule depending on the funding adequacy of the reserve account. In no event shall the applicable percentage exceed 3 percent.

b. In determining the annual applicable percentage, the department shall consider, but not be limited to, the value of the reserve account, distributions made from the reserve account in previous years, and the likelihood of future credits to and distributions from the reserve account. The department shall make its annual applicable percentage decisions using at least a rolling five-year period.

c. If for any year the department cannot afford an applicable percentage equal to that payable to retirees under Iowa Code section 97B.49F(1), the department may use application percentages in succeeding years that are higher than those used in calculating dividends for retirees under Iowa Code section 97B.49F(1) (but not in excess of 3 percent).

d. An applicable percentage in excess of the applicable percentage declared under Iowa Code section 97B.49F(1) made for catch-up purposes shall not reduce the funding of the reserve account below the amount the system's actuary determines is necessary to pay the maximum favorable experience dividend for each of the next five years, based on reasonable actuarial assumptions.

[105] Supplemental Account for Active Members.

[106] Just as occurred this year, as IPERS learned in October 1999.

Recommendation # 6) Establishing Fixed Contribution Rates for Public Safety Members by Which Future Benefit Enhancements Would Be Paid

That, effective July 1, 2000, fixed contribution rates, sufficient to fund existing benefits and expanded disability, be established for public safety member and their employers[107]; and that the other recommendations of the benefit parity study for IPERS' memberships be purchased over time from within the margin created by these fixed rates.

Discussion

One of the recommendations of the benefit *parity* study performed in 1998 was that IPERS establish a fixed contribution rate for its special group membership.[108] The current floating rate structure was devised in 1988 as part of the agreement whereby IPERS' special groups received a more favorable retirement formula (same payout but with fewer service years required). The floating rate above the 9.45% which paid for the core level of benefits enjoyed by all IPERS' members was to be annually determined by IPERS' actuary and was to reflect the cost of the *additional* benefits enjoyed by the public safety membership.

While this has worked well in the years since, the very fact that it is precisely determined by IPERS' actuary every year means that no "margin" accumulates wherein surpluses develop that could be used to purchase additional benefits. For example, had the rates assessed the special groups five years ago been retained, they would have paid for most, if not all, of the additional costs of the expanded disability program we are recommending as our number one priority.

Further, fixed rates bring predictability to budget planning, not only for members, but for their employers.

Lastly, the fixed rates would also allow special groups' members to enjoy a Supplemental Account for Active Member (SAAM) distribution when one becomes payable in the future.[109] Floating rates, precisely because they are exactly what the System needs to cover its liabilities for that portion of the membership, will never allow a SAAM distribution.

We recommend that the Legislature adopt the additional benefit enhancements for IPERS' special groups, and that IPERS be instructed to implement them as sufficient margin

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[107] Our actuary recommends two fixed rates until such time as we have achieved true parity between and among IPERS' special service groups: one for the sheriffs, deputy sheriffs, and airport firefighters, and the other for the protection occupation groups.

[108] Please see *Report to the Iowa Legislative Committee on Public Retirement Systems: "Comprehensive Examination of Benefit Programs & Related Issues Pertaining to Public Safety Classifications within IPERS, POR, & MFPRSI"*, submitted on November 2,1998, p.18.

[109] A SAAM would not be allowable until all unfunded liabilities represented by parity enhancements had, in fact, been fully paid for.

becomes available within the new fixed contribution rates for these groups.[110] These additional benefit enhancements from the 1998 benefits *parity* report, are:

1. Equalize number of years required to establish 60% formula at 22[111]
2. Provide same credit per year of service[112] for at least 30 years of service[113]
3. Provide same credit per year of service[114]

Also, consistent with the *parity* report, the above additional enhancements assume that the existing **two** special groups, which currently have their own benefit disparities *between* them, would be combined into one.[115]

[110] It is very likely that this would mean the full implementation of these various enhancements would take several years. Our suggested method is very similar to the approach taken by the 1990 General Assembly when it directed us to increase the formula multiplier from 50% to 60%, as well as to annually increase the ceiling in the then covered wage ceiling. IPERS was directed to attain these goals, and the pace was determined by our keeping within the existing contribution rates.

[111] Currently, members of the PORS and MFPRSI – and sheriffs, deputy sheriffs, and airport fire fighters in IPERS (27% of IPERS' members who in public safety related positions) – earn 60% for 22 years of service, while the remaining 73% of IPERS' public safety members must work 25 years to earn 60%. The value of each year of service for those who earn 60% after 22 years is 2.727% for each year of service, while it is but 2.4% for those who accrue 60% at 25 years.

[112] Members of MFPRSI, PORS and IPERS' sheriffs, deputy sheriffs, and airport firefighters receive 1.5% credit for years of service beyond 22, while the rest of IPERS" special service members receive 1%.

[113] Members of the MFPRSI and IPERS' sheriffs, deputy sheriffs, and airport firefighters can receive credit for up to eight years of service beyond the 22 necessary to earn 60%. Members of the POR can receive credit for up to 10 years beyond 22 years of service, while the rest of IPERS' special groups can only receive credit for a maximum of 5 years of service beyond 22.

[114] Members of MFPRSI, PORS and IPERS' sheriffs, deputy sheriffs, and airport firefighters receive 1.5% credit for years of service beyond 22, while the rest of IPERS" special service members receive 1%.

[115] *Report to the Iowa Legislative Committee on Public Retirement Systems: "Comprehensive Examination of Benefit Programs & Related Issues Pertaining to Public Safety Classifications within IPERS, POR, & MFPRSI"*, p.20.

<u>Recommendation # 7) For *Adjunct Instructors* Who Work for the Community Colleges, the Right to Elect IPERS' Coverage</u>

That, effective July 1, 2000, adjunct instructors with existing accounts with IPERS be allowed to elect IPERS' coverage for their service as adjunct instructors.

Discussion[116]

For the overwhelming majority of IPERS' eligible employees, participation is <u>mandatory</u> and begins with the employee's first day of employment. For a minority, coverage rights are <u>elective</u>. Even these individuals begin their employment covered by IPERS, but have 60 days within which they may elect *out* of IPERS.[117] These elections are one-time events and are irrevocable.

<u>Special Class of Non-Covered Public Employees: *Temporary Employees*</u>

The Legislature has long recognized, however, that some persons come into public employment for relatively short periods of time. These are designated *temporary employees* in Iowa Code Chapter 97B. As <u>non-permanent</u> employees, their need for and, indeed, *right* to pension coverage is of a significantly different order than that of permanent employees. As a consequence, it has been a long-time feature of IPERS' law that persons with *less than six months of employment with a public employer* are <u>not</u> eligible for IPERS' coverage.

There are occasions when persons are legitimately hired by an employer as a "temporary" employee, but who either end up working longer than was initially intended or, alternatively, succeed in being promoted into a permanent position. There have been some instances as well when we have discovered persons who have clearly been with an employer for some time on an on-going basis but are still classified as temporary. On such occasions, we have required the employer to file the appropriate wage related documents necessary to give that person requisite service credits.

For these reasons, and to protect persons whose employment transitioned from "temporary" to "permanent", IPERS has further defined the nature of "temporary employee" in its administrative rules. The relevant portion of Iowa Administrative Code 581 - 21.5 (1) (a) reads:

> (13) Persons hired for temporary employment are excluded from IPERS' coverage providing that they have not established an ongoing relationship with an IPERS-covered employer. Effective January 1, 1993, an ongoing relationship with an IPERS-covered employer is established when the employee is paid covered wages of $300 or more per quarter in two consecutive quarters, or if the employee is employed by a covered employer for 1,040 or more hours in a calendar year. Coverage will begin when the permanency of the

[116] The discussion and recommendation which follow are from our *Report to the General Assembly on Whether or not Persons Employed by Community Colleges as Adjunct Instructors Should be Eligible for IPERS' Coverage*, filed September 1, 1999.

[117] Most of these persons are either *elected officials*, including legislators, or *employees of the community colleges or state universities*. The latter may specifically elect into another retirement system, which is usually TIAA-CREF.

relationship is established, and shall continue until the employee's relationship with the covered employer is severed. If there is no formal severance, coverage for a person hired for temporary employment who has established an ongoing relationship with a covered employer will continue until that person completes four consecutive calendar quarters in which no services are performed for that employer after the last covered calendar quarter. Notwithstanding the foregoing sentence, no service credit will be granted to a temporary employee who has become a covered employee under this rule for any calendar quarter in which no covered wages are reported unless the employee is on an approved leave of absence. Contributions shall be paid, and service credit accrued, when wages are paid in the quarter after the ongoing relationship has been established.

The status of temporary employees is not *position-specific*, except in the case of **adjunct instructors.**

The 1998 General Assembly asked IPERS to investigate whether or not adjunct instructors should be covered employees of IPERS. IPERS was to solicit input from employees and employers alike on this issue.[118]

We asked Dr. Gene Gardner, the representative of the Iowa Association of Community College Trustees, and also Vice Chair of the IPERS' Constituent Group, to work closely with us in this study in order to ensure that the interests and concerns of the community colleges were addressed. To assess the sentiment of the *adjunct instructors* themselves, we asked Ann Selzer, of Selzer & Company, Inc., to assist us in surveying adjunct instructors employed by the community colleges.[119] Selzer & Company contacted "an accurate cross section"[120] of adjunct instructors via a telephone survey in the week of July 7, 1999.

Because IPERS has consistently favored *inclusion* over *exclusion*, the best option from our perspective is allowing each eligible[121] adjunct instructor to be covered from the first day of eligibility unless he or she elected out of coverage.[122]

On the other hand, as this would be the most expensive option, and because we recognize that IPERS' coverage for persons without a current IPERS' account has comparatively little value,

Our recommendations are:

1. Extend elective coverage only to those adjunct instructors who already have an IPERS' account[123]; and,

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[118] House File 2496, Section 85, 1998 Acts of the General Assembly.

[119] We have utilized Ms. Selzer's firm twice within the past year. Last winter she surveyed our members preparatory to our completing the legislatively mandated study on the desirability of IPERS offering a statewide supplemental deferred compensation plan. In May of 1999 she surveyed our membership to both measure their assessment of many of the services we offer and to learn their wishes with respect to the location of a future IPERS' headquarters building.

[120] Adjunct Instructor Survey, Selzer & Company, Inc., p. 1.

[121] Eligible according to the same temporary and permanent employment rules as apply to all other IPERS' members.

[122] The data from the Selzer survey which indicate interest in IPERS' coverage across the board among adjuncts, even among those who have no current account with IPERS, supports this more inclusive approach.

2. Consider additional revenue for the community colleges in order for them to cover their increased salary-related costs so that adjunct instructors do not have to see their take home salary reduced.

[123] Including those with both an *inactive* and *active* account. Note that under current law, it would appear that such adjuncts – extended the right to elect IPERS' coverage – could thereby also gain the right to choose an alternative plan.

<u>Recommendation # 8) For All Employees, Changing the Method IPERS' Uses to Track Service Credit – and the Computation of Retirement Benefits – from the *Calendar Year* to *Rolling Twelve Quarters.*</u>

That, effective July 1, 2001,[124] IPERS begin to use a "rolling twelve quarters" in lieu of our existing "calendar year" as the basis for computing retirement benefits.

Discussion

IPERS has used *calendar years* consisting of *four quarters* for over thirty years as the basis for both tracking service credit and computing the retirement benefits to which members are eligible. In addition, IPERS has used a *computed year* to "fill in" the portion of the final calendar year in which the member did not actually have employment.

In recent years, it has become increasingly obvious that this method is <u>not</u> *school friendly*, nor is the *computed year* a particularly easy concept to explain. Unlike IPERS' other covered employers, schools utilize a "contract year" which typically begins in the late summer (August) or autumn (September) and runs either through the following spring (usually June) or early summer (July).

The problems that result from the IPERS' *calendar year* and the schools' *contract year* do not usually become apparent or burdensome until a member teacher's final year when it can make a world of difference whether or not that teacher receives his or her pay:

- Over a 12 month period;
- Over a 9 month period; or
- Gets the final pay that he or she otherwise would have received during the summer "paid off" in June.

How this is done can dramatically impact both the amount of retirement benefits the member receives <u>and</u> how soon the member can begin drawing benefits.

Frankly, we not only have seen repeated disparities created between members of various school districts because of district policy on these matters, but we also have encountered members *within the same district* who have either received unequal treatment or, more likely, advice of uneven quality. The net result is increasingly one of perceived, and actual, *inequity*:

a) frustrated IPERS' staff, who attempt to administer the existing law as uniformly as possible;
b) frustrated retirees, many of whom feel they receive less benefits than they deserve[125]; and,

[124] We are asking for a delay in *implementation* as it will take us time to reprogram our computers and notify members.

c) the payment of retirement benefits which frankly often exceed what other public employees, with the same service credits and same wages but who work for a non-school employer, can receive.

During this past year we have worked with our educational representatives on the Constituent Group to come up with both a *short term* and a *long term* solution that will bring much greater equity for school and non-school employees alike. Our proposed solution, happily, is *not* school employee specific; rather it will bring a greater degree of simplicity and equity to all retiring members.

Long Term (proposed effective date July 1, 2001)

With legislative support (and the requisite law change), effective July 1, 2001, IPERS would begin tracking wage reporting, and the computation of benefits, for *all* employees on a "rolling twelve quarters" basis. In effect, this would mean that when a member applied for retirement benefits, our normal course would be to take the actual wages paid over the highest twelve contiguous quarters[126] and use them as the basis for computing retirement benefits.[127] In addition, we believe we will also need *two* anti-spiking provisions: one to guard against significant increases in pay within a year or two of retirement, the other to eliminate any temptation to "load up" the final quarter of employment by rolling into that quarter wages which otherwise would have been paid in later months, for example. We believe these changes will keep the basic structure of our formula very similar to what it is today, while making the administration of the law easier for both school districts and IPERS.[128]

Short Term (until July 1, 2001)

We would use the interval to not only reprogram our computer to allow for this change, but also to educate our members and covered employers about the reasons, method, and effect of this change. IPERS will need to continue to monitor existing retirements to ensure that various forms of wage spiking do not occur beyond the parameters currently in the law.

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[125] Although the reality is that the present law usually works to the teachers' advantage as they have options to elect when they are paid in their final year in a manner that other public employees do not.

[126] This preserves our current formula's use of the *average of the highest three years* as the basis for the computation of the member's retirement benefits.

[127] We would also need an exception provision for those rare persons for whom their highest wages did not appear in the twelve quarters immediately preceding termination and retirement.

[128] Thus, the existing problem of whether to receive pay over a 9 or 12 month basis would disappear. So would the much disliked "computed year". The "computed year" is a device IPERS has long used which is *required* by the use of the "calendar year if we are to attempt to capture a retiring member's most inflation-rich salary. As most people do not terminate and retire exactly at the end of a calendar year, the "computed year" allows us to "fill in" the remainder of a person's last calendar year of employment with needed quarters taken from the average value of quarters in their highest calendar year not used in calculating their average highest three calendar years of wages. Ingenious as it is as an attempt to assist members, it is fraught with difficulties and is open to manipulation through collusion of employees and employers.

<u>Recommendation # 9) For All Elected Officials, Allowing them to Retire under IPERS without Having to Resign their Elected Positions.</u>

That, effective January 1, 2000, elected officials be extended the same right as legislators currently have to terminate their non-elected service, cease coverage for their elected service and retire without having to resign their elected position.

Discussion

IPERS has supported this change in past years and again requests it for the 2000 legislative session.

When the law was changed in recent years giving legislators this privilege, many believe the divorcement between legislators and other elected officials of the right to retire from non-elective covered positions without resignation from elective positions was unintentional. In current law, the two groupings of elected officials are treated in separate sections. The change drafted for one was not, unfortunately, applied to the other.

Here is the language which IPERS most recently[129] recommended to the Governor and General Assembly for consideration to resolve this problem:

A. Amend section 97B.42 by adding a new unnumbered paragraph (probably in next to last position).

> Notwithstanding any other provision of this section, effective {insert date}, an elective official, as defined in section 97B.1A(8)"a"(1), who is contributing to the system with respect to employment as an elective official and who is also in other covered employment, shall be excluded from coverage with respect to the employment as an elective official if the elective official:
>
> 1. Has a bona fide severance of employment from all covered employment other than the employment as an elective official; and
> 2. Applies to begin receiving a retirement allowance.
>
> An elective official excluded under this section shall be excluded from coverage as of the last day of the month preceding the member' first month of entitlement.

B. Also amend section 97B.52A by adding the following as paragraph 4.

> A person: 1) in employment for which IPERS coverage is optional and who is not covered in that employment; or 2) in employment, other than employment in a position described in Iowa Code section 97B.1A(8)(b)(3), for which coverage is unavailable, may

[129] In communications of August 1999.

continue to be employed in such a position during and after the person's four-month bona fide retirement qualification period.

Recommendation # 10) For the "Higher Paid" among IPERS' Membership, to Make Appropriate Adjustments to the "Leveling of Benefits" Provisions Originally Enacted in 1996

That, effective January 1, 2000, the "default" figure which triggers the use of a average wage year formula greater than three years be increased from the present $55,000 to $65,000 (and by $10,000 annually each year thereafter until the restoration of the average of the highest three years for everyone), and that the number of years used in the multi-year average remain at six until the restoration of the high three on January 1, 2002.

Discussion

When the Legislature agreed to remove the *covered wage ceiling* effective January 1997, one of the essential elements making this possible was the creation of a device to "smooth out" the impact of this removal on IPERS' members making salaries substantially above the last covered wage of $44,000. This device, cumbersome and inelegant as it has appeared to some, was the utilization of years in excess of three in the computation of one's wages to be used in estimating retirement benefits. In essence, this additional formula said, "If a person's actual highest-3 years' average salary exceeds $55,000 (1999's reference level), then this person's final average salary will be the greater of the average of the person's highest 6 (or 7 in 2000) years[130] or $55,000."

The *reason* behind the creation of this device was less concern over the financial health of the Trust Fund[131] than they were concern for equity between and among members. That is, if higher paid persons were allowed to retire immediately after 1996 with their benefits figured upon their actual wages, the resulting lifetime benefit stream would represent a tremendous one year spike compared to the year before. In addition, there was concern that the "average" (i.e., non-high paid member) might experience substantial resentment toward those so favored. The resultant law was designed to "smooth out" any such "spiking" and has, in fact, so far served that purpose.

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[130] The number of years of covered wages to be used in the smoothing formula started at four. The number of covered wage years to be averaged rises by one each year until it reaches a maximum of seven in the year 2000.
For covered wage years ending prior to 1997, each year was limited by relatively low covered wage ceilings (e.g., $44,000 in 1996). In 1997, the covered wage ceiling was raised to the maximum permitted by federal law ($150,000 at that time).
The smoothing formula and low pre-1997 covered wage ceilings allowed potential retirement benefits to increase each year, but constrained increases by requiring the inclusion of low covered wage ceiling years in the smoothing formula. For example, an affected individual who retired in 1999 (under the six-year formula) would be required to include the 1994, 1995, and 1996 maximums ($38,000, $41,000 and $44,000) when figuring their six-year average salary, even if their actual wages in those years were much higher. Once the seven-year maximum was attained in year2000it would stay in place two more years. The adverse affect of the smoothing formula is lessened, but not entirely removed, by the replacement over time of the low covered wage ceiling years with covered wage years subject to the much higher post-1996 covered wage ceiling.

[131] The numbers of folks involved – and their demographic spread throughout our membership – was too small to be significant in impacting the Trust Fund one way or another.

The remaining number of persons making above $55,000 (the "old maximum ceiling" fixed by former law at which the covered wage ceiling was to stop progressing upwards) is 4,497[132], of whom only 1,290 are of retirement age.[133] Frankly, the administration of this provision of the law is quite time-consuming for IPERS' benefits and data processing staff, is very difficult to explain to members, and causes the higher paid portion of our membership great frustration.

Accordingly, we are recommending a couple of steps which should bring some relief to those affected, while retaining the original smoothing out goals of the 1996 legislation:

1. Allow the "default" figure, currently at $55,000, to increase by $10,000 annually each January 1 – beginning with January 2000 – until the return to the use of the "average of the highest three years" formula for everyone; and,
2. Freeze the required number of years in the alternative formula at "six" rather than allowing it to rise to "seven" in January 2000 as currently is required by law.

Because the number of people still affected by the current law is but 3% of all active members – and only 29% of this tiny number is of retirement age – it would also be a defensible resolution to abolish this provision of the law before 2003. The judgment about *whether* to do so is really a policy and political call, not primarily one of retirement benefits' plan design.

[132] As reported to Senators Sheldon Rittmer and Jack Kibbie in correspondence dated July 21, 1999.
[133] Only 275 of those eligible to retire make $75,000 or above.

Recommendation # 11) For Future Retirees, Create a "Pop-up" Feature as an Alternative Option for those Selecting *Option 4* at Retirement

That, effective July 1, 2002[134], the existing Option 4 retirement alternative have added to it the additional optional feature whereby a member could choose a "pop-up" feature which would restore his or her benefit to the Option 2 level should the member's designated contingent annuitant predecease the member.

Discussion

At retirement, IPERS offers its members a number of options regarding whether or not they wish to leave to another person or persons a "death benefit" to follow their own death. (*Option Three*, for example, has no death benefit.)

One of the most attractive to our members has long been *Option 4* which allows members to select a *contingent annuitant* who, upon the member's death, can receive for the duration of their life (again, at the member's designation at retirement) 25%, 50%, 75%, or 100% of the member's monthly benefit. To keep this cost neutral for the system, and to preserve equity between members, the member's benefit is reduced according to both the magnitude of the percentage he or she designates and the birth date of the *contingent annuitant*.

The problem is that all too often the person named *contingent annuitant* dies before the member. Under current law, the member cannot either designate another person nor have his benefit adjusted for the fact that there is no longer a *contingent annuitant* payable. This means the member lives with a permanently lower adjusted benefit for the rest of the member's life.

Understandably, this is not a popular outcome.

This proposal would give the member the *optional choice* of selecting an *Option 4* payout together with the direction that, should the *contingent annuitant* predecease the member, the member's monthly benefit would "pop-up" to the *Option 2* (higher) level. Further, we propose that any actuarial cost to the System for providing this option be absorbed by the members selecting it.

We believe this will encourage many more members to choose what is basically a wonderful death benefit option (and one which provides the greatest level of security and dependability for surviving spouses or family members).

[134] This time-frame is required because this new option will need to be programmed into our computer system which is currently undergoing substantial re-engineering.

Recommendation # 12) For the Small Percentage of IPERS' Retirees who Return to Covered Employment following a Bona Fide Retirement, Raising the Current Ceiling on Reemployment Wages from $12,000 to $25,000

That, effective January 1, 2001, the level at which members must have their IPERS' retirement benefit reduced by $.50 for each $1.00 earned be raised from the current $12,000 to $25,000.

Discussion

Only 4,985[135] of IPERS' retirees have returned to covered employment following a *bona fide retirement.*[136] This percentage of our membership has remained fairly constant in recent years.

Under current law, such re-employed persons are allowed to earn re-employment wages and collect their IPERS' pension until such time as re-employment wages exceed $12,000 in any calendar year. After that point, retirees' IPERS' pension is reduced $.50 for each $1.00 that re-employment wages exceed $12,000. As there is a "lag" in the reporting of wages (inevitable in a system that tracks contributions by a *quarter of year service* basis rather than daily or monthly), we frequently end up "billing" members for the amount of overpayment after the fact.

Administering this provision consumes a lot of IPERS' time, relative to the small population involved. So far this calendar year, for instance, only 32 persons out of the 4,985 have exceeded $12,000 (one-half of one percent of all retired re-employed members).

Because we think having the option to re-employ skilled former employees is likely to be an increasingly attractive option for IPERS' covered employers in the near future, we would like to see re-employment be made as attractive an option as possible.

Accordingly, we propose that the Legislature raise the ceiling above which IPERS must begin reducing benefits of the re-employed retirees from the current $12,000 to $25,000. Of those currently above the ceiling (at $12,000), this would leave only 9 persons who would still be subject to benefit reduction.

Another option would be to eliminate the ceiling altogether. IPERS did propose that a few years back. However, then – as perhaps now – reasonable persons could raise the concern about that isolated re-employed member who might be receiving a handsome IPERS' pension and also secure a re-employment position with very high wages. The resulting publicity could call into question an otherwise very sound policy, and is the reason we hesitate to make this our first priority with regard to this issue.

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[135] Less than 2% of all members, and only 8% of all retirees.

[136] There are probably others of our retired membership who have gone back to work, but for non-IPERS' covered employers. We have no way of knowing how many as their post-retirement wages for such employers are not reported to us.

In general, we would prefer to not make policy decisions because of the *exception*. Accordingly, it would also be legitimate for the General Assembly <u>to abolish the re-employment ceiling on earnings entirely.</u>

Part Seven: Recommendations for Consideration for Future Plan Design

Because the Governor has indicated his intent to call for a study of IPERS' structure and governance, there is a possibility that I will be in a different position with respect to benefits' policy and plan design issues during the next "IPERS' year" in the General Assembly in 2002. I believe that it is incumbent upon me, therefore, to give you the best recommendations I can for possible future enhancements.

The following proposals, therefore, do not necessarily enjoy the same degree of support as do the other recommendations to you in this report, either among other IPERS' managers or from the Constituent Group. Nonetheless, because of the importance I believe they might have in helping IPERS attain an even more competitive and balanced plan design, I wish to draw them to your attention for possible future consideration.

A. **Reducing the number of years to attain a payout of 60% for regular membership from 30 to 25.** I believe this merits study for two primary reasons:

   1. The average years of service for an IPERS' retiree remains approximately 21[137] years, not the 30 required to receive 60% of one's average highest three years of covered salary. This means the average benefit is closer to 42% (21 x 2%) than 60% or 65%.

   2. About 58% of our current active membership is female. Women historically retire with fewer years of service then men[138].

   If the ratio of females to males in our system is either static or increasing, our plan design would be more friendly to women (and, indeed, to all with fewer years of service than the maximum) if the payout of 60% were fixed to 25 years of service rather than 30.

B. **Creating an incentive for vested, terminating members to keep their money in IPERS until retirement by indexing the value of their accrued benefit at termination by up to 3% per year until they retire.**

   This idea, which has been around for a few years, gained new urgency with the additional payout value granted to terminating vested members in 1998, and which took effect July 1, 1999. Now vested members who terminate and request a refund can receive a portion of the employer's contributions in addition to all of their own contributions and accrued interest.

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[137] For all of our retirees, including those members retired longest, the average is 20.62 years. For those who have retired since June 1990 – the FED-eligible group – that number rises slightly to 21.5 years of service.

[138] Women are 66% of those retirees who left with fewer than 19 years of service, and 67% of those who left with less than 30 years of service, while they drop to only 47% of those who retired with more than 30 years of service.

IPERS, however, is a retirement system; I believe we should offer these same people an attractive incentive to keep their money in the Trust Fund.

Approximately 6,000 public employees terminate public service and request a refund from IPERS each year. Upon taking a refund, the member loses membership status and forfeits all rights to any future payment from IPERS. Alternatively, the member does have the right to leave his or her money in IPERS until reaching retirement age at which time the member will receive the same benefit (in constant dollars) that he or she had accrued at the time of termination. Currently, over 33,800 vested, inactive members have left their money in IPERS.

Many point to this as a form of inequitable payout (as compared to the subsidized retirement benefits received by members who retire under IPERS). When contrasted to the compensation features of a *defined contribution* type plan, this is the single most noticeable area in which our plan falls short. Further, there is rising demand for more *portable* pension benefits.[139]

IPERS first advanced the proposal to index the accrued value of a terminating member's benefit to the Legislature several years ago. In doing so, we recommended that our primary focus on the career employee be broadened to include those employees whose termination from public employment does not coincide with their retirement. This position is consistent with existing efforts to provide a sound retirement for all employees, and can serve both to keep more money in the System and allow IPERS to provide an equitable portion of what could be an eventual sound retirement for the thousands of vested, but terminated, employees.

C. **Substituting a side by side *defined contribution* plan, funded by a 1% distribution from employee contribution, for the current SAAM[140] provision in the law.**

This proposal will require at least as much study as the other two. Although I have come to this conclusion somewhat reluctantly (as the SAAM was partly my idea), I believe it does merit your attention. Here, in brief, are my reasons:

1) The original reason *behind* the *SAAM* proposal was two-fold: to give active employees, too, a "piece of the surplus pie" akin to what we wished to give all retirees (as evidenced in our expanded *FED*); and, to blunt the criticism of some who contended that most of our benefits under our *defined benefit* plan were directed

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[139] See, for example, the discussion in Pension Portability for State and Local Government, written by Gary I. Gates, and published by the Milbank Memorial Fund; 615 Madison Avenue, 15th Floor; New York, NY 10022. Our proposal is not nearly as aggressive as many discussed in the Milbank report, as IPERS has retained our traditional emphasis on members who retire under IPERS and on members who keep their money in IPERS as having a greater demand on us for retention of full value of accrued benefits than those who terminate public service and pull their money out of the Fund.

[140] *Supplemental Account for Active Members.*

primarily to retirees. If we were going to retain the loyalty and support of coming younger generations we had to design a more flexible vehicle.

2) The *SAAM* was a step in the right direction. But, from the beginning, it had a questionable – if not fundamentally flawed – feature: it would be paid only under a combination of circumstances including:

   - IPERS cannot even consider making a SAAM distribution to a separate account *unless the Fund's unfunded liability is zero or "less"*.[141] Two years ago, for example, when we proposed this concept, IPERS was at 95% funding, short of this target. Today, we are at 97%.
   - There must be a margin between the statutory contribution rate of 9.45% and the normal cost rate determined by the actuary.
   - There is no separate reserve by which to "shelter" monies for future SAAM payments. By law and design, any SAAM ever allocated will be funded from *current* year's status. The payment stream, especially when compared to the FED, will therefore be both more unpredictable and variable.

   Only when these conditions are met would a *SAAM* be paid. At best, *SAAM* payments would be irregular and perhaps miniscule (both are hard to "prove", but this year the difference between statutory and normal cost shrunk considerably).

3) If we are going to go to the trouble of offering such a feature, it might as well have actual value, especially as perceived by active members. What features are needed for "perceived value"? Perhaps:

   - Regular accrual
   - Predictable
   - Explainable
   - Accessible

4) Of these, the proposed *SAAM* had only "accessible" going for it.

Proposal: Consider instituting a side by side defined contribution plan <u>in addition to</u> the core IPERS' defined benefit plan. It would belong totally to the members and could be accessed by them either at time of termination and refund of accumulated service credits or upon retirement. It could be funded in a variety of ways, for example by: 1) diverting 1% from the current employee contribution of 3.7% *at such future time when the System is 100% funded*; or 2) increasing the amount of employee contributions by 1%; or 3) a combination of the two, ½ of 1% of existing employee contributions and a hike of ½ of 1% in the level of employee contributions.

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[141] "Less than zero would represent a "surplus" funding level.

Conclusion

Each of the above is more expensive than any of the proposed enhancements we have brought to you in the package adopted by IPERS and the Constituent Groups. However, each of this is also, in my opinion, worth investigating for possible future action.

I propose that, if you are interested, each be investigated through a combination of: surveys and meetings with members, hearings by the General Assembly, and comparisons with plan design features in the public and private arena.

APPENDICES TO THE REPORT

Appendix One: IPERS' Funding Policy and the Trust Fund

All of our recommendations are predicated on IPERS adhering to the *funding policy* that was developed by the Investment staff of IPERS in collaboration with our System actuary.[142] This *funding policy* governs the pace of achieving the benefit enhancements proposed in this paper. Obviously, IPERS does not propose to add any benefit enhancements in a year when the actuary declares that further enhancements are not possible without exceeding the parameters of the *funding policy.*

Introduction[143]

In 1996 the Iowa Public Employees' Retirement System (IPERS) experienced some of the most significant changes to its benefit structure and actuarial methods in many years. The impetus for these changes was the desire to more closely align IPERS with other major U.S. public pension systems. More importantly, those changes enabled IPERS, for the first time, to more accurately and realistically value both its assets and liabilities. On the heel of these changes, the Iowa Legislature directed IPERS to develop "objective actuarial standards" and "safeguards" that will ensure that the Fund remains financially sound in the future. Toward that end, IPERS' staff has worked with the System's actuary, Milliman and Robertson (M&R), to develop a "funding policy" which will ensure that the System continues to be soundly funded on an actuarial basis going forward. Furthermore it will provide an objective means of determining when, and to what extent, the Legislature might wish to implement further benefit enhancements.

Background

Iowa Code Chapter 97B.61 states that "The Department shall cause an actuarial valuation to be made of the assets and liabilities of the retirement system and shall prepare an annual statement of the amounts to be contributed...under this chapter...." The product of this actuarial valuation is the determination of the actuarially required contribution rate that the Department must certify to the governor as the rate necessary and sufficient to fund the retirement benefits being credited to our members. The **actuarial contribution rate** represents the rate necessary to both fund the normal cost rate and to pay off the unfunded actuarial liability. The **normal cost rate** represents the level percentage of salary required to pay the cost of retirement benefits that are allocated to the current year of service. The **unfunded actuarial liability** represents the difference between

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[142] The 1996 General Assembly, in House File 2245, not only passed numerous enhancements to IPERS' benefits program, but also directed that several special studies be performed. One of these directed IPERS to propose how we would ensure, through our identifying "objective actuarial standards" by which we will monitor the Trust Fund's financial health, that the Fund continues to remain soundly funded.

[143] The text which follows is from *IPERS Funding Policy*, a paper developed in 1997 by IPERS' Investment staff in conjunction with the System's actuary, Patrice Beckham of Milliman & Robertson.

the actuarial value of the benefits allocated for service to date and the actuarial value of the assets accumulated to pay for those benefits.

It is noteworthy that the issue of an unfunded actuarial liability is new to IPERS, and one with which many may not be familiar. In 1996, IPERS adopted **entry age normal** as its actuarial costs method. Previously, IPERS had valued its liabilities using the aggregate cost method which does not separately identify an unfunded actuarial liability. The aggregate cost method instead develops a single contribution rate which accumulates sufficient assets to pay the normal cost rate and the unfunded liability. It must be stressed that the existence of an unfunded actuarial liability is not necessarily an indication of poor funding. Unfunded actuarial liabilities occur when actual plan experience deviates from the actuarial assumptions used to perform the annual valuations. Because assumptions cannot predict the future with absolute certainty, particularly in any given year, unfunded actuarial liabilities will occur. Unfunded actuarial liabilities will also result from the granting of benefit enhancements retroactively for members' prior years of service.

The measure of whether a pension fund is adequately funded is ultimately determined by its ability to pay the benefits it has promised. Given that this is a promise that will take decades to fulfill, it is appropriate to develop and use a measurement standard that also focuses on along term perspective. In designing the Funding Policy that follows this page, IPERS' staff and M&R were guided by the Legislature's mandate that the funding policy be objective, actuarially-based, and that it incorporates sufficient safeguards to ensure that it adequately protects the soundness of the pension fund. IPERS was also cognizant that such a policy needs to be rigid enough to provide a meaningful measure, yet flexible enough to work in an environment that is constantly evolving.

As one step in the development of the Funding Policy, the IPERS staff conducted a survey of public pension funds and their funding status. A copy of these survey results, first released in 1998, is available for review by request.

NOTE:
One common measure for evaluating funded status is the **funded ratio**, which is the ratio of the actuarial value of assets to the actuarial accrued liability. The appeal of this measure is its simplicity. It yields a ratio which is easily understood and makes possible some comparison to other systems or a target-funding ratio. The problem with using this as a measure of funding adequacy is its short-term focus. It measures the sufficiency of assets accumulated to date but fails to evaluate whether a system will be accumulating adequate assets in the future to pay for the benefits promised to current members.

In past years, pension funds commonly used the funded ratio to make comparisons with other systems. New accounting standards have rendered the Pension Benefit Obligation, a measure of the actuarial accrued liability, obsolete. Differences in actuarial cost methods, actuarial assumptions and asset valuation methods make comparability with other systems extremely limited.

IPERS FUNDING POLICY

Purpose

This funding policy is intended to provide a measure of the funded status of the Iowa Public Employees' Retirement System (System) on a long term basis and to provide a set of safeguards as guidelines to help ensure the financial solvency of the System.

Recognizing that the System and its environment are not static, periodic review of this policy shall be conducted to ensure its continuing validity.

Primary Goal

The primary funding goal of the System is to be funded on an actuarially sound basis over the long term by maintaining actuarial contribution rates, given the maximum amortization period, which are equal to or less than the statutory contribution rates.

Definition of "Fully Funded"

The term "fully funded" is used to describe the situation in which the assets are equal to or greater than the liabilities. The focus of IPERS is to define assets and liabilities on a long term basis; therefore, the IPERS funding policy defines the term "fully funded," as well as the terms "actuarially sound" and "financial solvency," to mean that the current actuarial value of assets along with the future expected contributions will be sufficient to provide the benefits promised to members for both accrued and expected future service (as set forth in Iowa code Chapter 97B) within the parameters established in this funding policy. The minimum standards for the System to be considered fully funded is that the normal cost rate plus the amortization payment on the unfunded actuarial liability may not exceed the statutory combined contribution rate. In determining the amortization payment, the amortization period shall never exceed 30 years.

Safeguards for System to Remain Fully Funded

The following safeguards are established to ensure that IPERS continues to be funded on an actuarially sound basis over the long term, so that adequate funds will accumulate to provide all benefits promised to members.

(1) The **normal cost rate** (the level percentage of salary required to pay the cost of retirement benefits that are allocated to the current year of service), based on the actuarial cost method used to determine the annual funding requirements for the System, shall not exceed the statutory combined employee/employer contribution rate minus 0.5%.

(2) Given the statutory combined employer/employee contribution rate, the amortization period for the unfunded liability as reported in the annual valuation shall not exceed 24 years.

(3) Any change in the benefit structure of IPERS that results in an increase in the normal cost rate and/or the unfunded actuarial liability, and/or any distribution to eligible members, should not be considered unless (a) the amortization period reported in the last actuarial valuation report is 20 years or less, and either (b) the amortization period has been less than the maximum (24 years) for at least three consecutive years or (c) the amortization period has been less than ten years for at least two consecutive years, subject to the additional constraint that any distribution does not prevent the amortization period of the prior period from declining.

(4) Consideration should be given to increasing the statutory contribution rate if either of the following occur at least three years in any five consecutive year period:
- The normal cost rate exceeds the standard set in item (1) above
- The amortization period exceeds the standard set in item (2) above by more than 5 years.

Appendix Two: IPERS' Constituent Group and the Process Used to Develop the Enhancement Package

Part One: Membership of the Constituent Group

[A = Actives; R = Retired; ST = State; S = Schools; MEE = Multiple Employees; ER = Employers; MER = Multiple Employers; C = City; CO = County; P = Policy Maker/Advisor]

[Alternate representatives are designated by italics]

Chairman: Lowell Dauenbaugh **Vice-Chairman: Gene Gardner**

Schools

Iowa State Education Association - A, R, S	Lowell Dauenbaugh (*Brad Hudson*)
Iowa Association of Community College Trustees - A, ER, S, P	Gene Gardner
School Administrators of Iowa - A, S	Gaylord Tryon
Iowa Association of School Boards – ER, S	Jenifer Owenson
Retired School Personnel Association – R, S	Walt Galvin

State

Conservation Officers – A, ST	Diane Reid
Director, Department of Personnel - ER, ST, P	Mollie Anderson

Multi-Level

IPERS' Improvement Association – A, R, MEE	Janie Garr (*Harold Zarr*)
American Federation of State, County, and Municipal Employees (AFSCME) – A, R, MEE	Mike Campbell (*Marsha Nichols*)

County

Sheriffs and Deputy Sheriffs' Association – A, CO	Bill Hutchins (*Bill Sage, et.al.*)
Association of Counties – A, MER, CO, P	Jim Maloney

City

Association of Police – A, C	Terry Dehmlow (*Mike Rolow*)
League of Iowa Cities – A, MER, C, P	Andi Stewart (*Curt Svalstad*)

Policy/ Advisory

Benefits Expert – Policy Advisor	Larry Zimpleman (Principal Financial Group)
Legislative Staff Person (Appointed by Chapter 97D Retirement Committee) – P	*Vacant*
Representative from Department of Management – P	Steve Timmons

Part Two: Process Used in Identifying and Prioritizing Recommended Enhancements

From a communication to the Constituent Group of Tuesday, June 09, 1999

A few words on this subject might be in order as we have a number of new members "around the table" since we last worked on plan design and benefits enhancements issues.

Personal Philosophy

I believe that we all have a right to be "at the table".[144] I do not pretend that we have equal statutory responsibility for the Plan, or for attesting to the current status of its benefit program or recommendations for needed enhancements. But I do believe we have equal interest in attaining – and preserving – a sound and financially sound retirement system. We have different roles to play. I see them as mutually complementing one another, not by their nature conflicting.

Consensus Decision-Making

In our deliberations together since the formation of this group, we have pursued a *consensus* mode in arriving at our eventual recommendations.[145] Some of the essential ingredients of arriving at consensus with this large a group are:

1. Inasmuch as is possible, we deal with each other without titles or any other form of "status" designations.

2. Everyone has a right to put an issue or proposal "on the table".

3. Everyone has a right to expect that his/her proposal or position on an issue will be treated respectfully.

4. No one person has the right to take an issue "off the table", or "dismiss" a proposal or a point of view.

5. All are expected to be open and honest, to place their proposals, their reasoning, and concerns "on the table".[146]

6. In a group this large, it is nearly impossible to achieve a package which, in its totality, will please everyone. Recognizing this, we ask that each person indicate as necessary when she or he is "taking their oar out of the water". Such a statement can mean many

[144] There may well be others who should be here, too. I am confident we will continue to be sensitive to the need to add new members as appropriate, even as we have repeatedly enlarged this group over time.

[145] I am sure many of you recall that before the Constituent Group was created it was common for IPERS and one or more of the individual associations to be at odds over what elements of plan design or benefits enhancements should be enacted.

[146] I have learned the hard way that consensus is very difficult, if not impossible, to achieve if there are issues "under the table" which are not being dealt with openly.

things. Some examples: "you are not taking me (or my position) seriously"; or, "this issue is an absolute 'must' for my organization"; or even "I believe the course you are pursuing on this point is fundamentally flawed". Whatever its exact meaning, it is a sign that we all have a problem and must focus on dealing with this issue.[147]

7. As we proceed, we will do our "darnedest" to see that each person's hot or must do issue is: a) achieved, if at all possible; or b) at the least, dealt with sufficiently so that the reason(s) why it cannot be achieved are clear and understand and that the person pressing the issue is sufficiently persuaded to keep her or his "oar in the water".

8. While it will be my principal responsibility to facilitate this process and help us arrive at consensus positions, it is all of our responsibility to pull together so that this can happen.

I personally believe that if it would ever come to a standoff between *some* of "us" and *others* of "us", we all lose. This is true whether it be a stark contrast between representatives of member and employee associations and IPERS, or whether it is a more complex scenario where some of IPERS' staff stand with association members and some association members stand with other IPERS' staff. If we can just continue to focus on the fact that we all have a sincere interest in serving our members, providing them with a sound and balanced retirement plan, while ensuring that it remains financially sound, I believe we can avoid any thorny issues that lie beneath the surface. We also have the encouraging history of the past several years of working together to demonstrate that we do place the interests of our members above all else.

SUGGESTED TIME-LINES

June 2 Constituent Group Meeting

- Review of suggested process and time-lines
- Review of issues: Do we have them all? Do we concur as to their nature, wording, and intent?
- Initial discussion on prioritization of issues

Steps between meetings

1. Members will submit their individual priority and intensity rankings to Greg by June 15.
2. Greg will collate them and affix them on the priority/intensity matrix.
3. Greg will distribute them by mail in advance of July meeting.
4. Greg will also distribute a *draft* copy of his report which will have the context, guiding principles, trends, and policy targets fleshed out for review.

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[147] I recognize that this *seems* to give a person inclined to be difficult a means by which he or she could "tie up" the group. In practice, however, I have observed that most people: a) try to be reasonable; b) (in a consensus environment, especially) truly want the group to succeed, too; and c) rarely use this tactic precisely because it is a "card" which, if played often, loses its value and that person is dismissed by the group as a "non-team player".

July 7 Constituent Group Meeting

- Group will review and discuss the priority/intensity matrix results.
- Group will discuss in detail areas of disagreement or mixed agreement for possible resolution (including identifying whatever data is needed to assist in resolving issues).
- Group will provide feedback to Greg's initial draft report.

Steps between meetings

1. Greg will "reiterate" both the matrix and draft report for review.
2. Group (including appropriate subgroups) will perform whatever data collection/analysis is required regarding outstanding issues.
3. Group will give Greg written suggestions for improving his draft report.

August 4 Constituent Group Meeting

- Group will review reiterated matrix and draft report.
- Group will identify any remaining issues of disagreement or discord.
- Group will agree on process to resolve these.

Steps between meetings

1. Greg will incorporate and distribute changes to both the matrix and draft report for review.
2. Group (including appropriate subgroups) will perform whatever data collection/analysis is required regarding remaining outstanding issues.
3. Group will give Greg written suggestions for further improving his draft report.
4. Greg will issue second draft of report for review.
5. Greg and Mollie will seek a courtesy briefing for the Governor on likely principal issues.

September 1 Constituent Group Meeting

- Group will review priority list and revised draft report.
- Group will identify any remaining issues of disagreement or discord, including those issue(s) to be "put aside" requiring further study or continued discussion.
- Group will review "concepts" or drafts of other significant law changes being sought by IPERS (including "fine tuning" of existing statutes).
- Initial report of subgroup working on an *academic employment year*.

Steps between meetings

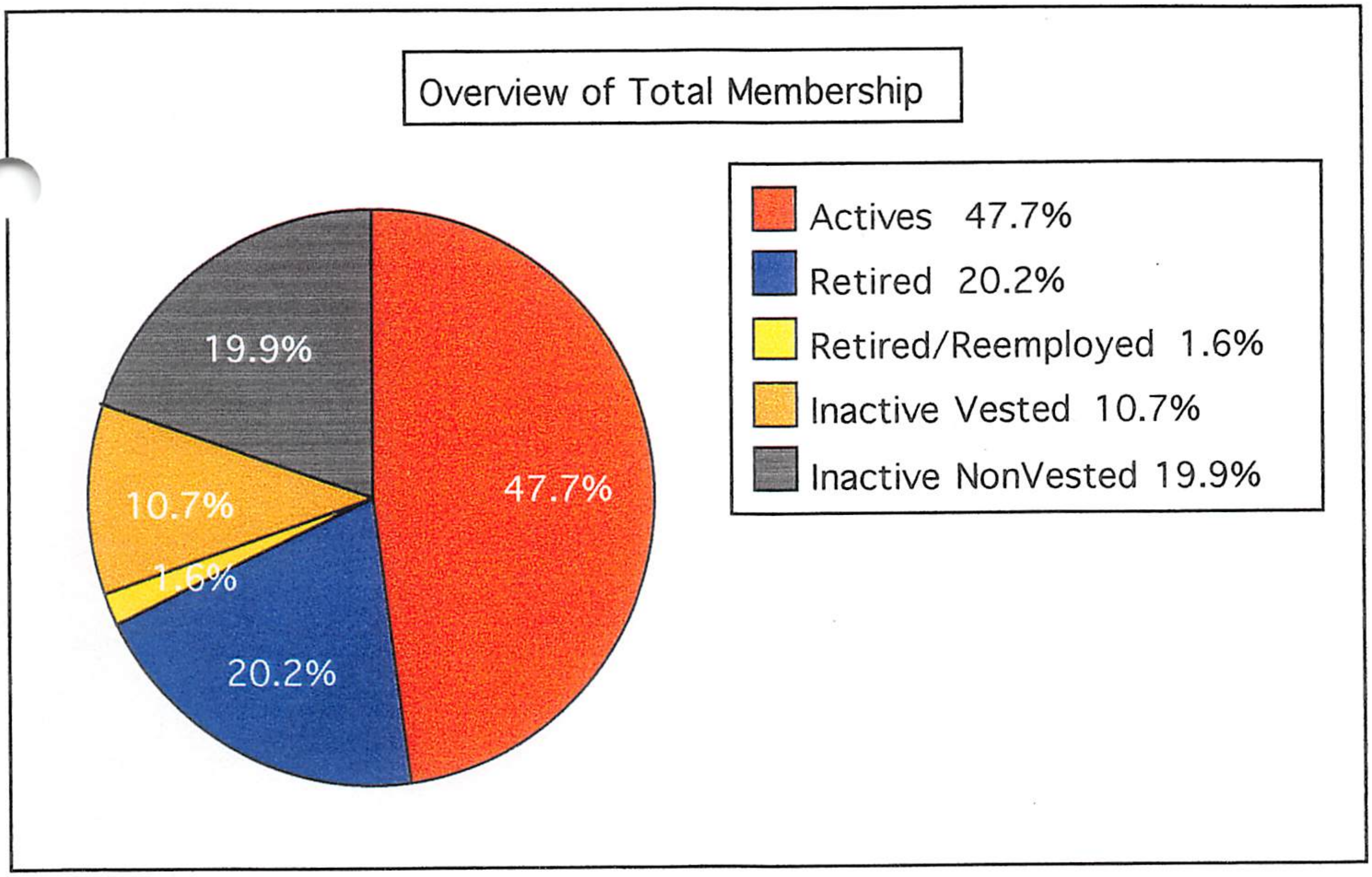
1. Greg will incorporate and distribute changes to the draft report by September 10 for review.
2. Group will provide feedback on remaining desired changes by September 20.
3. Greg will issue third draft of report for review by September 25.

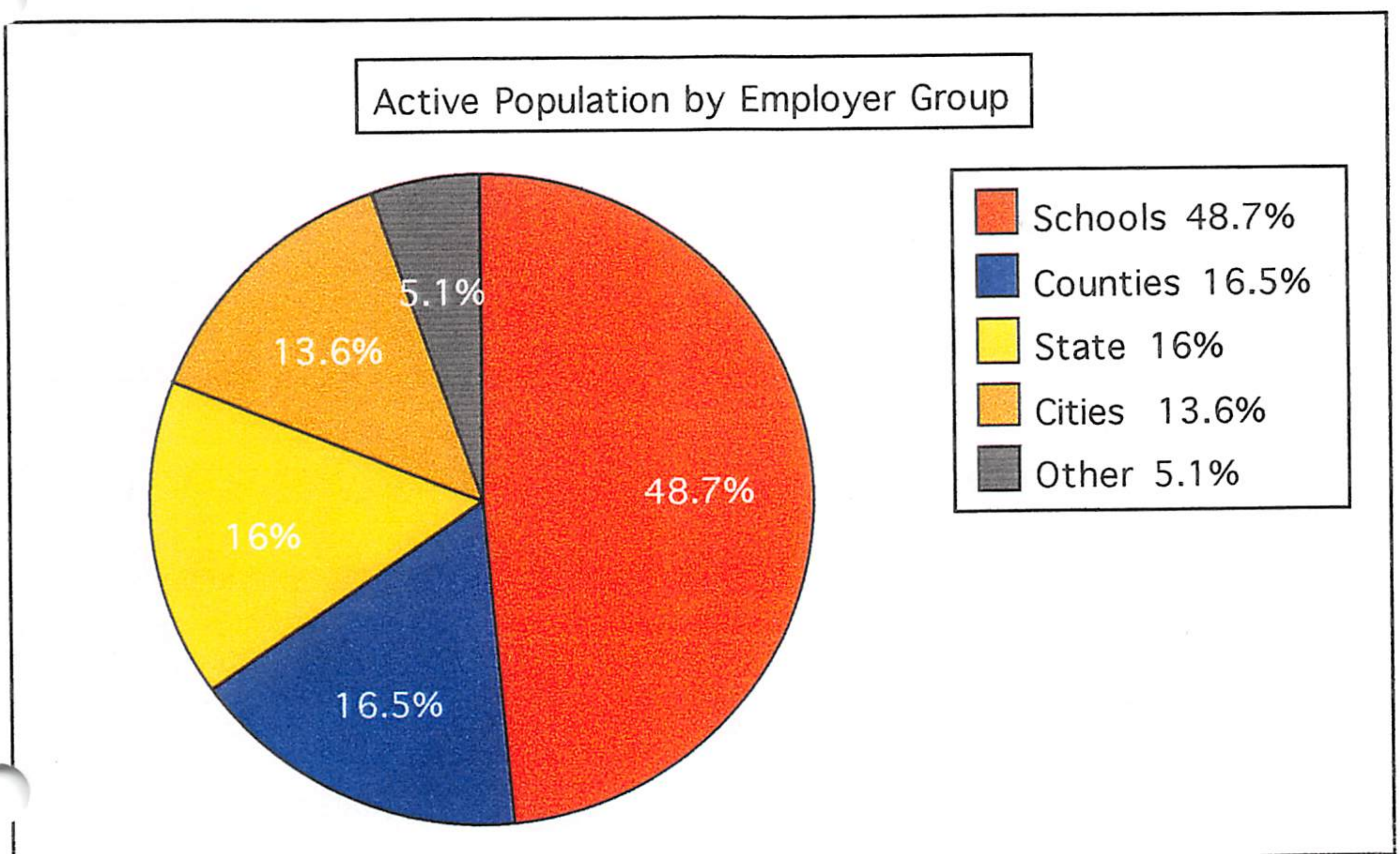
October 6 Constituent Group Meeting

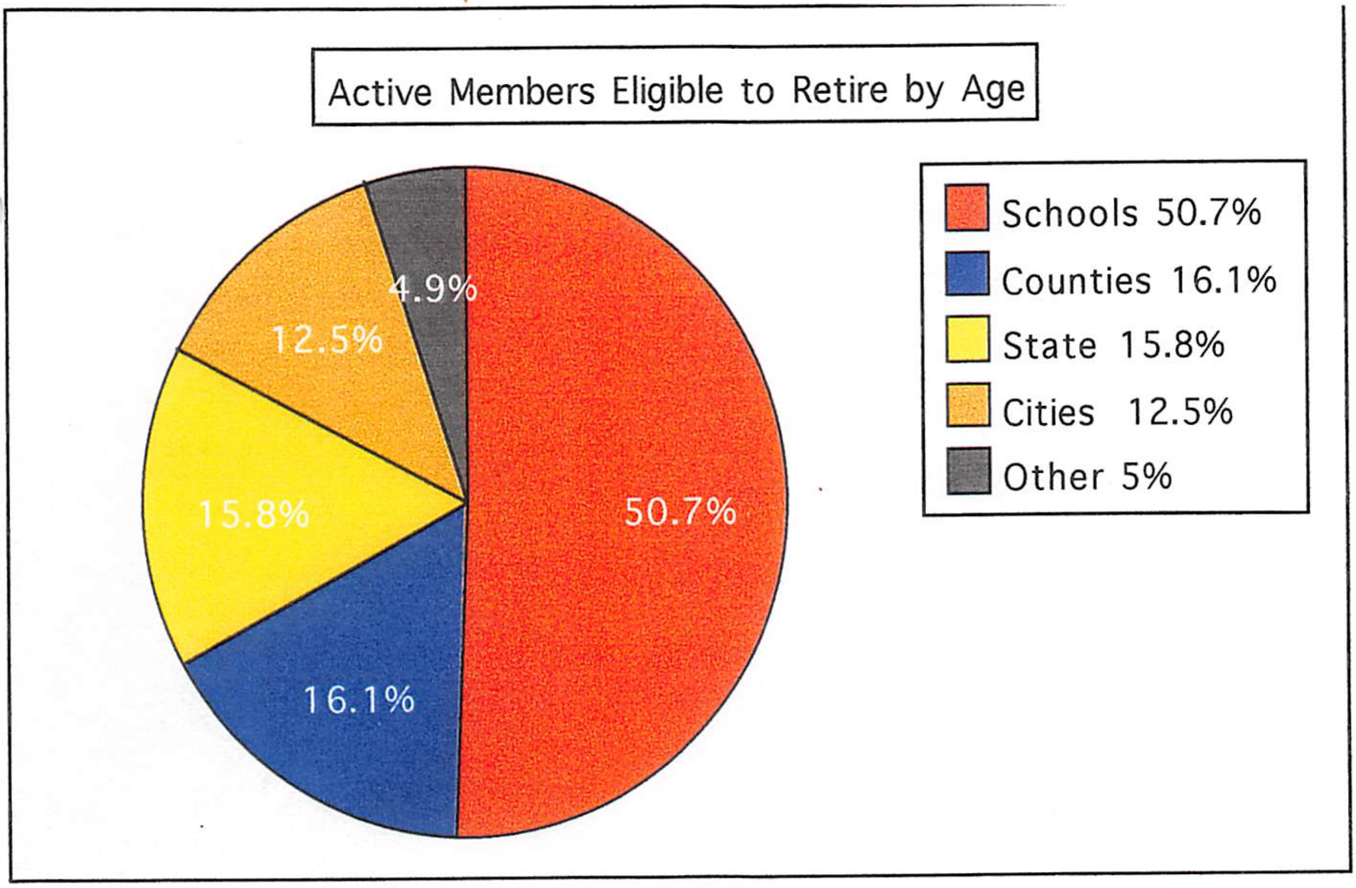
- Group will provide “final” comments/suggestions on third draft of report.
- Group will discuss presentation/negotiation strategies for Legislature

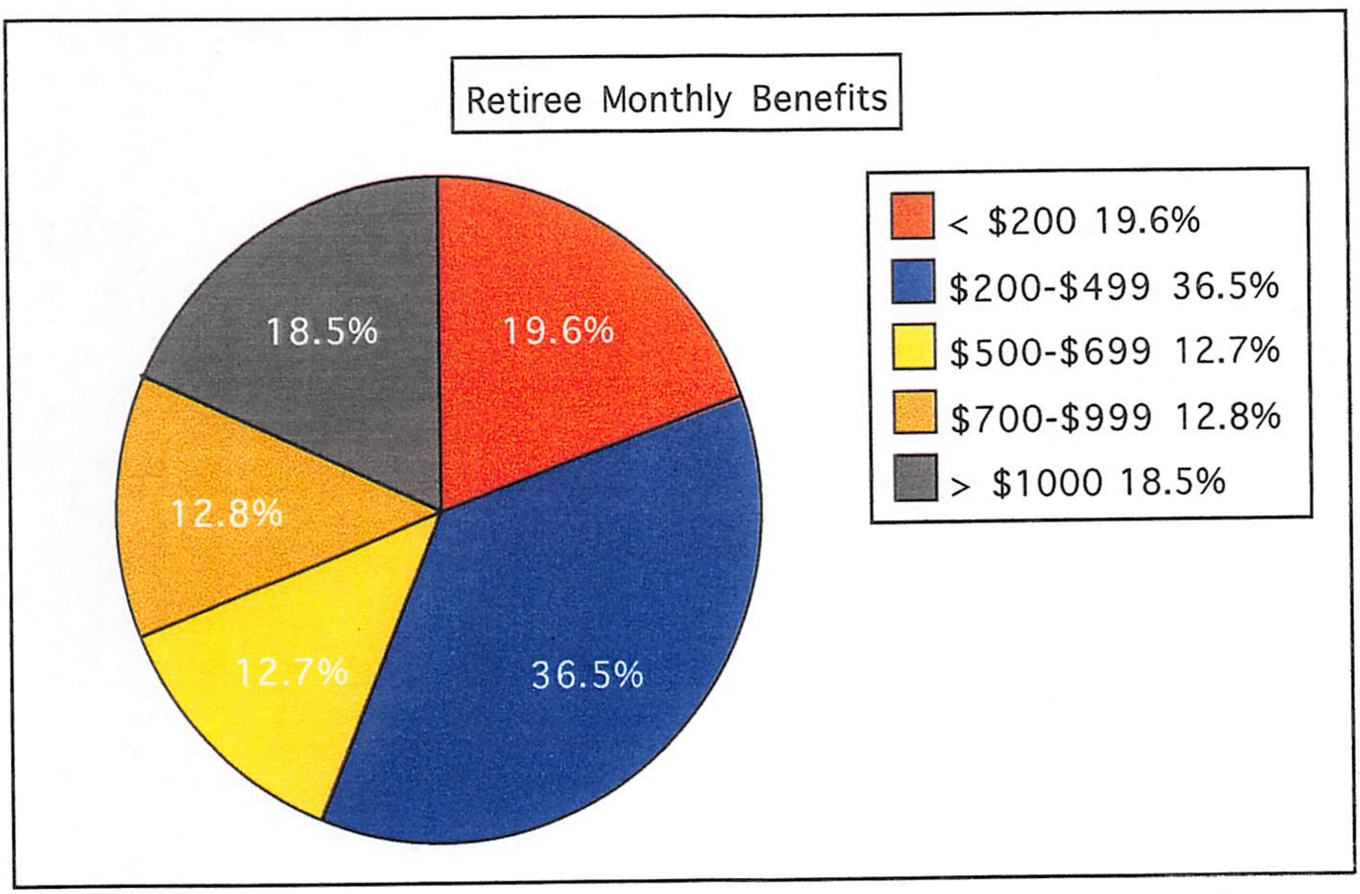
Appendix Three: Salient Demographics

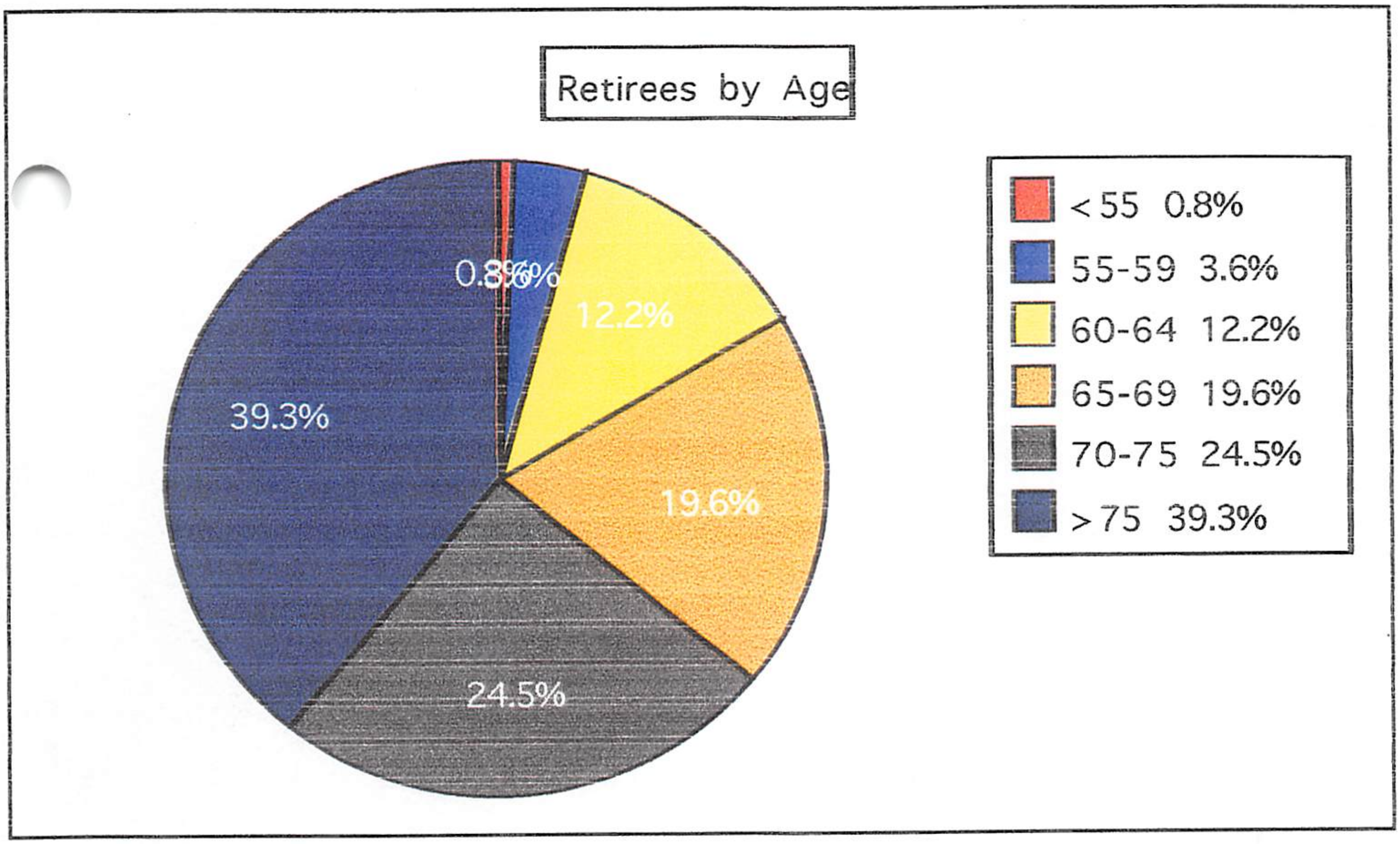
Charts and Tables
Illustrating Important Aspects of IPERS' Demographics
Follow This Page

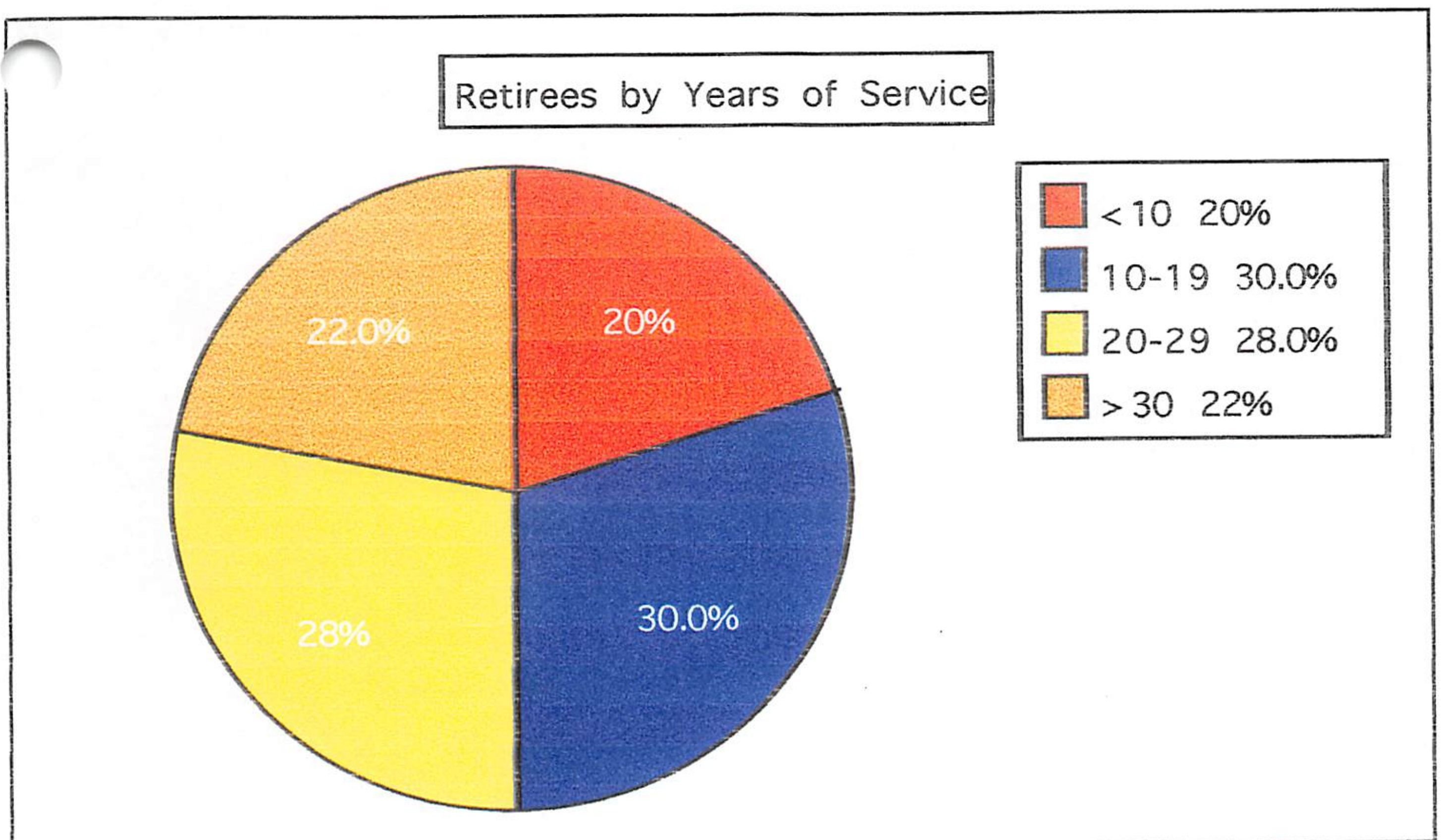

Overview of Total Membership
Actives 47.7%
Retired 20.2%
Retired/Reemployed 1.6%
Inactive Vested 10.7%
Inactive NonVested 19.9%
19.9%
47.7%
10.7%
1.6%
20.2%

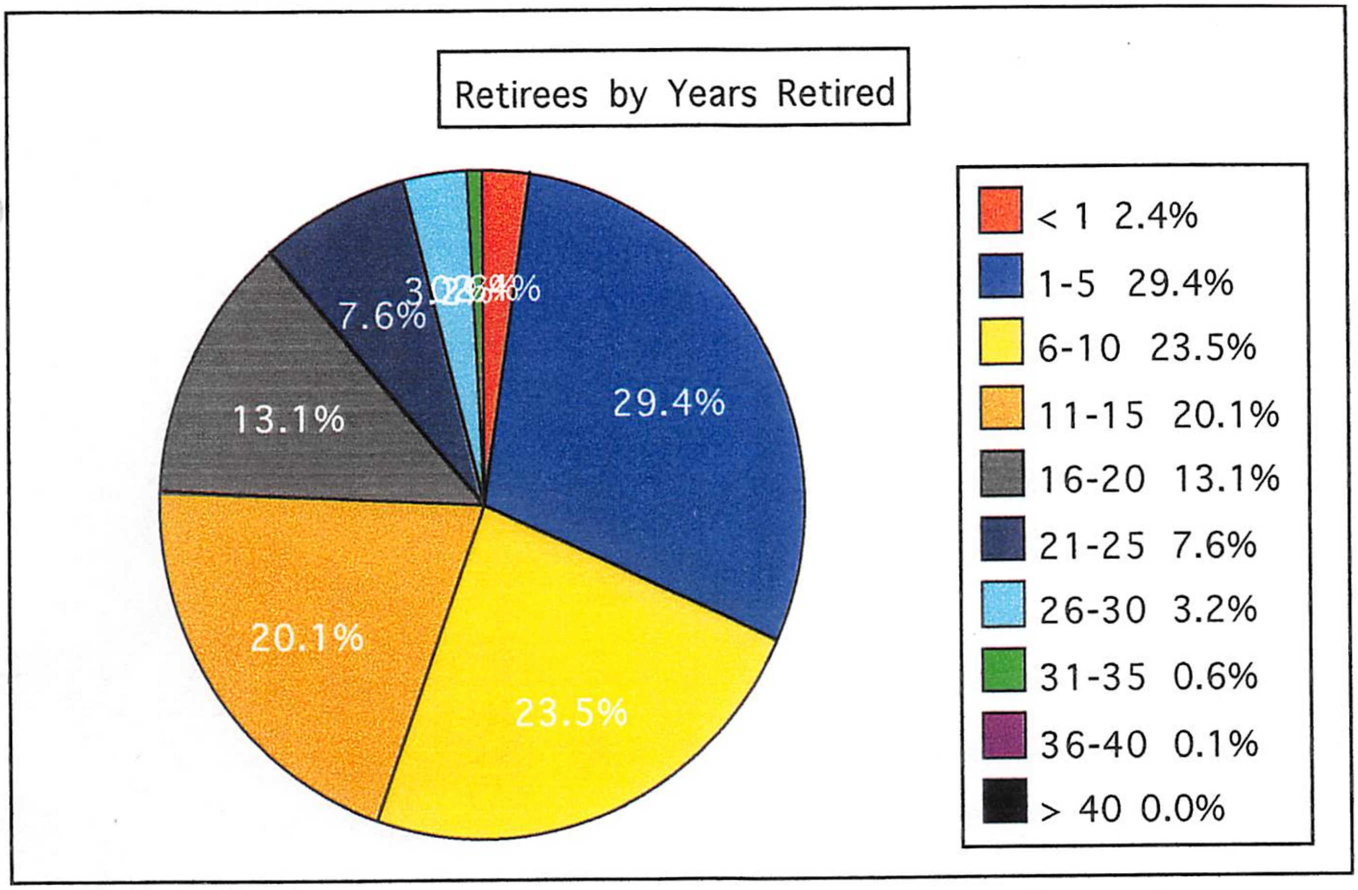

Active Population by Employer Group
Schools 48.7%
Counties 16.5%
State 16%
Cities 13.6%
Other 5.1%
5.1%
13.6%
48.7%
16%
16.5%

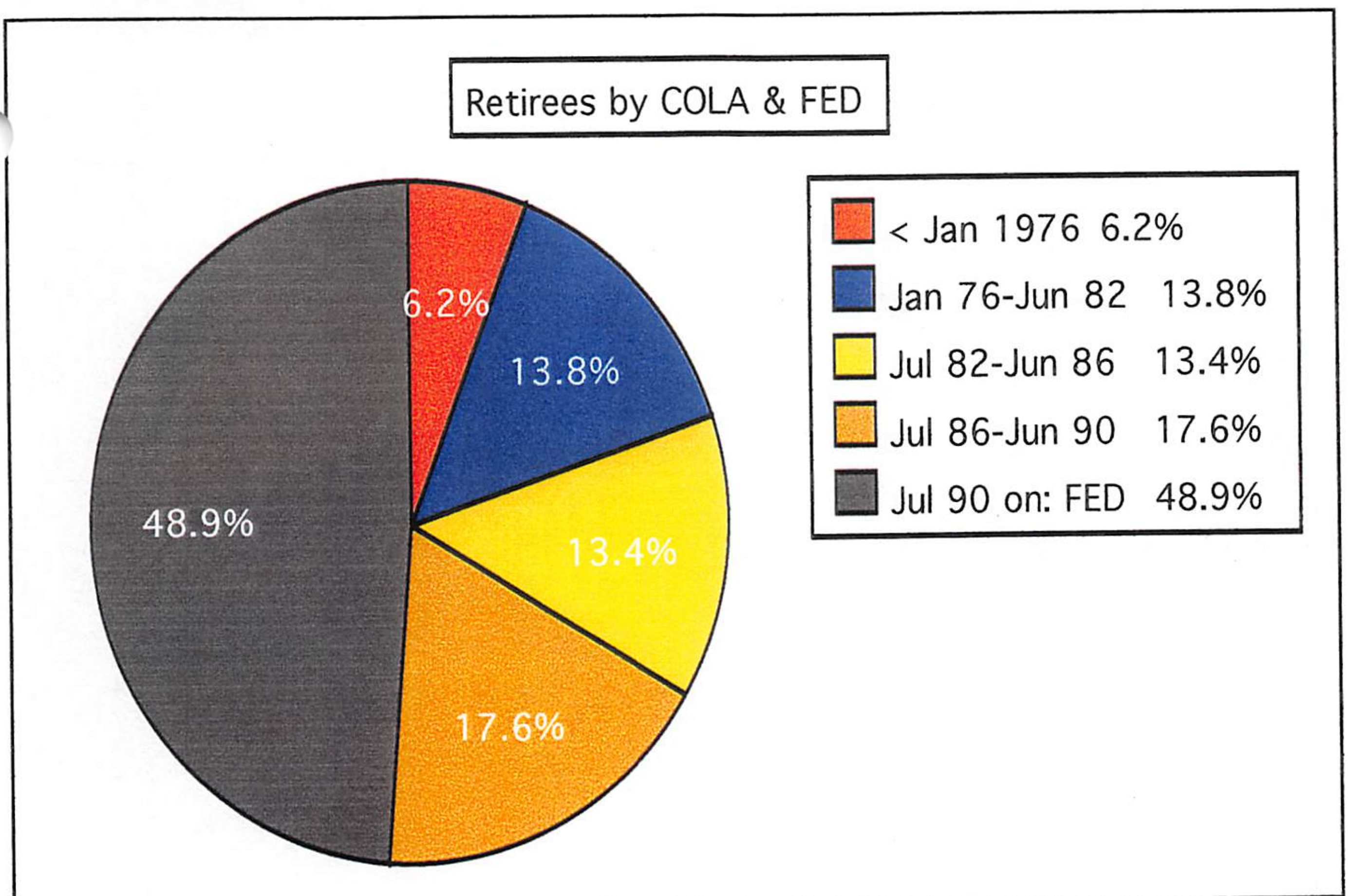

Active Members Eligible to Retire by Age
Schools 50.7%
Counties 16.1%
State 15.8%
Cities 12.5%
Other 5%
50.7%
16.1%
15.8%
12.5%
4.9%

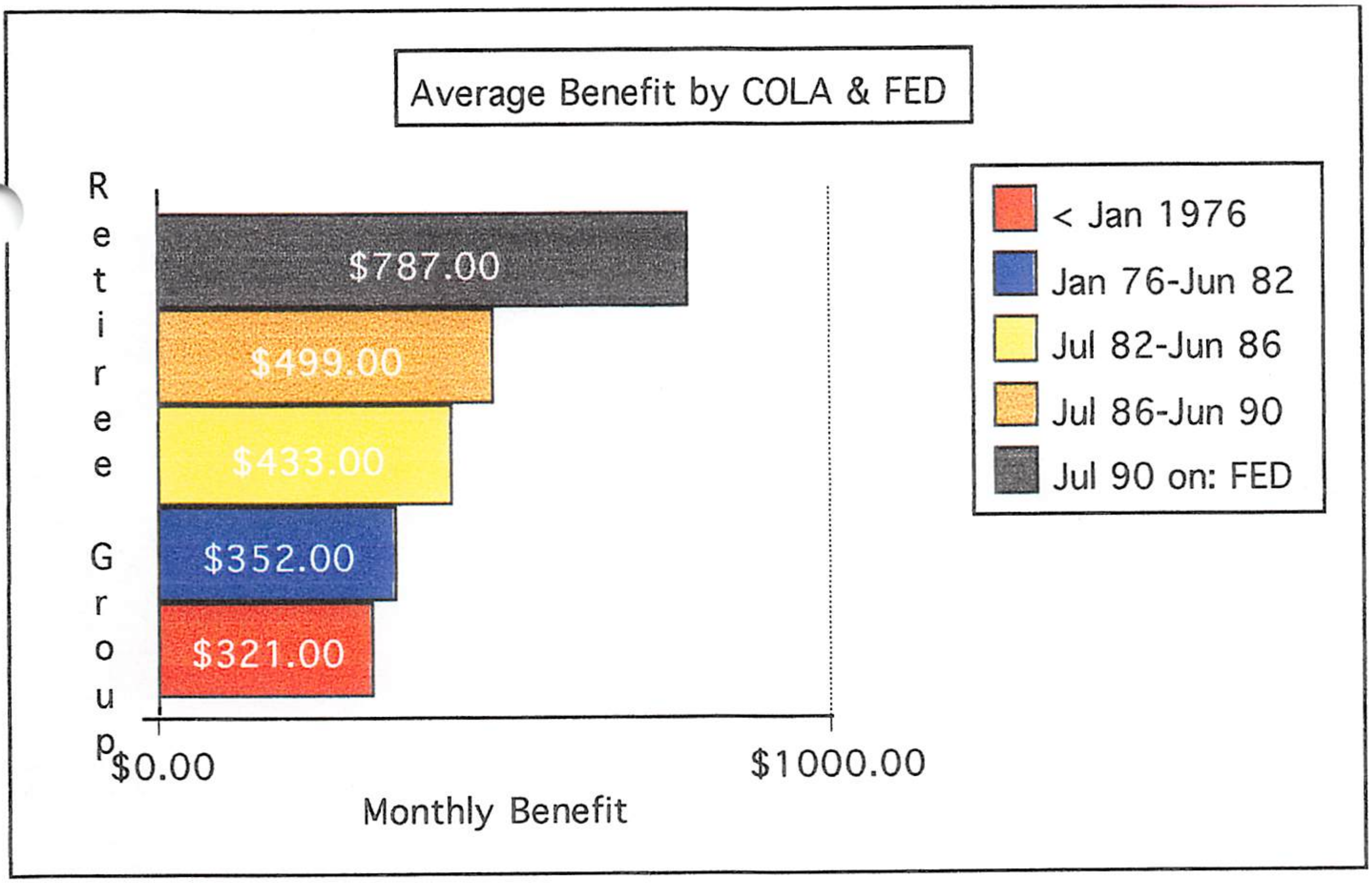

Retiree Monthly Benefits
< $200 19.6%
$200-$499 36.5%
$500-$699 12.7%
$700-$999 12.8%
> $1000 18.5%
19.6%
36.5%
12.7%
12.8%
18.5%


Retirees by Age
12.2%
39.3%
19.6%
24.5%
< 55 0.8%
55-59 3.6%
60-64 12.2%
65-69 19.6%
70-75 24.5%
> 75 39.3%


Retirees by Years of Service
22.0%
20%
28%
30.0%
< 10 20%
10-19 30.0%
20-29 28.0%
> 30 22%


Retirees by Years Retired
7.6%
29.4%
13.1%
20.1%
23.5%
< 1 2.4%
1-5 29.4%
6-10 23.5%
11-15 20.1%
16-20 13.1%
21-25 7.6%
26-30 3.2%
31-35 0.6%
36-40 0.1%
> 40 0.0%


Retirees by COLA & FED
6.2%
13.8%
13.4%
17.6%
48.9%
< Jan 1976 6.2%
Jan 76-Jun 82 13.8%
Jul 82-Jun 86 13.4%
Jul 86-Jun 90 17.6%
Jul 90 on: FED 48.9%


Average Benefit by COLA & FED
Retiree Group
$787.00
$499.00
$433.00
$352.00
$321.00
$0.00
$1000.00
Monthly Benefit
< Jan 1976
Jan 76-Jun 82
Jul 82-Jun 86
Jul 86-Jun 90
Jul 90 on: FED

Part One: Current System Profile

Overview of Total Membership

Total Membership: 316,798

Actives:	151,108 (48%)
Retired:	63,997 (20%)
Retired/Re-employed:	4,985 (2%)
Inactive Vested:	33,821 (11%)
Inactive, Nonvested:	62,886 (19%)

Discussion

There has been a slight growth in the *active* population in recent years, from approximately 144,000 five years ago to the present 151,000. Barring extraordinary events, we expect the number of actives to continue relatively constant. Over ninety-six per cent (96.5%) of our members are in "regular" service, while but 3.5% are in "special class" service (public safety positions).

The number of *retirees*, however, continues to show a steady increase of between 2,000 and 2,500 annually, as it has for the past dozen years. However, as the post World War II "baby boom" generation enters retirement we anticipate this rate to significantly pick up through at least 2012.

The number of *retired, reemployed* persons[148]remains about the same: only 2% of all of our members.

The number of *inactive vested* members[149] continues to be significant. It is logical that former public employees who have attained a significant number of quarters <u>and</u> are nearing retirement age would choose to keep their money in IPERS in order to be eligible for a retirement benefit.

We also continue to carry accounts for a very large number of *inactive non-vested* members[150]. We believe that most of these worked for a public employer for only a brief period and have since probably forgotten that they earned any retirement credits with IPERS. As we did not begin to store members' home addresses on our computer until 1992, once such persons left

[148] These are members who legally entered into a *bona fide retirement* and then, sometime following the requisite number of months, returned to covered employment. Under current law, such a person may earn up to $12,000 annually in reemployment wages before his or her IPERS' benefit is reduced ($.50 for every $1.00 earned above $12,000).

[149] These are members who, while not currently working for a covered public employer, have attained through previous service sufficient quarters of service to be *vested* and, thus, eligible for a retirement pension from us. Please note that, as members can also attain vesting by reaching age 55 or above, some of these 33,000 may have fewer than four years of service but nonetheless be vested.

[150] They are not eligible for retirement benefits because they did not attain *vesting* status before terminating public employment. *Once they reach age 55, however, they become automatically vested and eligible for retirement benefits.*

covered employment we lost our ability to contact them.[151] During the past year, we began a very concentrated effort to capture the addresses of these people so that we could notify them of their accounts and of the options open to them. We think it likely that a considerable number of them will consequently choose to take a refund of their relatively modest account values. We expect, therefore, that this group of our membership will be notably smaller in future years.

The proportion of *female to male* public employees appears to be static, with our over-all active population in a roughly 58%-42% female-male ratio.[152] If anything, there *may* be a slight increase in the percentage of women workers.[153] This bears watching, as it has implications for our plan design. Women historically have borne the greater burden of child rearing, including taking time off from their careers. This is shown as, overall, women have fewer years of service at the time of retirement than men.[154] As a means of partially adjusting our benefit structure for the majority of our members, IPERS two years ago recommended – and the General Assembly and Governor endorsed – creating a new "normal" retirement criterion of "62 and 20". That is, anyone 62 years of age (or older) with at least 20 years of service would not take an early retirement deduction in their benefit. This was because most persons, including the overwhelming number of women, retire with closer to 20 years of service than the plan maximum of 35. Further changes in plan design – beyond the "Rule of 85"[155] – may be required to better serve this majority of our membership.[156]

Overview of Active Members

By Age

Eighty per cent (80%) of all active members are below the earliest possible retirement age of 55. Only thirty percent (30%) are under age 40, however. Thirty-four percent (34%) are between the ages of 40 and 49, and sixteen percent (16%) are in the crucial pre-retirement years of 50-55.

Twenty percent (20%) are eligible for retirement because of their age[157], but are still working. Eleven percent (11%) are between 55 and 59 years of age, another six percent (6%) between 60 and 65, and only two percent (2%) older than 65. These numbers reflect the reality of the baby boomer generation nearing retirement age, as well as the smaller demographic group which immediately follows them. These numbers represent challenges for both *retirement* and *workforce* planning.

[151] Until 1994, the only way we could contact active members was through their employer.
[152] This is a *projection* and is based upon the ratio of females to males during the first 15 years of retirement.
[153] Source: Conversation with Lowell Dauenbaugh of the Iowa State Education Association, July 1999.
[154] See the figures for the retired population under *by years of service* analysis below.
[155] The *Rule of 85* would help at least as many women as men. As the figure representing the combined total of age and years of service becomes less (from the original *Rule of 92* to the present *88*, for example) a greater number of people become eligible for it.
[156] One proposal which may have merit is having our basic maximum formula of 60% - currently awarded when a person attains 30 years of service – be credited at 25 years of service instead. This would change the service year multiplier factor from the current 2% per year to 2.4%. Twenty-five years is much closer to when the average member actually retires than is our current thirty years.
[157] Being at least 55 years of age.

By Employer Group

Little has changed in recent years in the proportion of employees who work for our major employer groupings. Half of our entire system consists of school employees, while counties have overtaken (albeit by a very small number) the state as the second largest type of employer. State government remains the *largest single* employer. Interesting, state and school employees "look" most alike in their key demographics of average salary and average years of service.[158]

Schools:	70,342	(49%)
Counties:	23,870	(16%)
State:	23,056	(16%)
Cities:	19,662	(14%)
Other[159]:	7,427	(5%)

Those Eligible to Retire (ages 55 and up) by Employer Group

Of this active population, 26,886 (20%) are already eligible to retire by age.[160] The average state and school employee has over twelve years of service, while all other employer groups are just over ten years.

Schools:	12,236	(51%)
Counties:	3,893	(16%)
State:	3,806	(16%)
Cities:	3,010	(12%)
Other:	1,195	(5%)

Note that a larger proportion of school employees (contrasted with their over-all proportion of active members) is eligible to retire.

Those Eligible for the Rule of 88 by Employer Group

A total of 4,114 are currently eligible for the *Rule of 88*. The proportion of school employees is higher by 9% (58%) than their share of all actives – 49%. The State's share is also higher than its segment of the total active population (19% compared to 16%). Members eligible for this rule average 32.43 years of service and 60.44 years of age.

Schools:	2,380	(58%)
Counties:	455	(11%)
State:	789	(19%)

[158] See more specific discussion below in profile of newest retiree group.
[159] Such as municipal utilities, community action programs, or various programs for the elderly.
[160] When the *inactive population* is factored in, IPERS has a total of nearly 50,000 persons who are of retirement age – 55 years of age or older. Of these, over 20,000 inactive members. Also, in the crucial 50-54 years of age segment, when inactives are added there are almost 35,000 persons who will reach retirement age over the next five years.

Cities:	334	(8%)
Other:	146	(4%)

Those Eligible for the Rule of 85 by Employer Group

Those eligible to retire under a future *Rule of 85* number an additional 2,299, bringing the **total eligible** to retire without an otherwise applicable age reduction to **6,413**. Of those who would become eligible under the *Rule of 85*, 61% are school employees. The state's segment, on the other hand, drops to 14% (from 19% eligible for the Rule of 88). Members potentially eligible for this rule average 28 years of service and are 59 years of age.

Schools:	1,341	(61%)
Counties:	261	(11%)
State:	326	(14%)
Cities:	196	(9%)
Other:	125	(5%)

By Occupation Class

The overwhelming number of IPERS' active members (145,845 – 96.5%) are in *regular* service, that is, in occupations other than those of public safety. Of these, fully 75,000 are in education[161], 70,629 work for state, county, or city governments, and 116 are legislators[162]. Overall, regular members' average years of service are 11.26 and their average wage is $24,285.

Of the 3.5% who are in *special service* categories (public safety jobs), 2,439 work for the State as correctional officers (2,190), Department of Transportation weight officers (113), or Department of Natural Resources conservation police officers (136). Their average years of service is 11.42 and their average wage $32,289.

Another 1,411 work for the counties as sheriffs and deputy sheriffs, whose average years of service is 13.27 and average wage is $34,759.

Lastly, a total of 1,413 work for city government[163] in police and fire positions. IPERS also covers a total of 31 airport firefighters and airport safety officers. The average years of service of this group is 9.76 and their average salary $24,497[164].

[161] K-12, community colleges, and state universities. Persons employed by community colleges and the state universities may choose coverage by TIAA-CREF in lieu of IPERS' coverage.

[162] Although there are 150 members of the General Assembly, legislators, like other elected officials, have the right to *elect out* of IPERS' coverage if they choose.

[163] Recall that police and fire personnel of cities and towns over 8,000 belong to another retirement system by law – the Municipal Fire and Police Retirement System described in Iowa Code Chapter 411. State troopers belong to their own system, the Police Officer Retirement System described in Iowa Code Chapter 97A.

[164] This average data excludes firefighters who are frequently *volunteers* or very *part-time*. Therefore, both their average salary ($6,568) and years of service (4.57) are very low compared to the other groups.

Overview of Retired Members

Profile of Overall Retirees

At the end of FY 99, IPERS had 63,997 retirees, whose average benefit approached $600 per month ($7,200 annually), and who had 20.62 years of service at the time of retirement. Fifty percent (50%) of those retired are former school employees, while 16% worked for the state, 16% for counties, 13% for cities, and 3% for other employers. Most (75%) are relatively recent retirees, having been retired for 15 years or less. A full 39% are 75 years of age or older. The ratio of females to males is 61% to 39%[165]. The oldest retirees are overwhelmingly women, and – in general – men receive slightly higher benefits in retirement, even when allowing for differences in years of service, although for markedly shorter periods of time.

Almost 50% of our retirees are relatively recent, having retired since June of 1990. As a group, they average 21.5 years of service at the time of their retirement[166], the longest of any of our *dividend/FED* groups.[167]

Profile of Newest Retirees – Those Who Retired In FY 99

Employer	Number	%	Ave. Benefit	Annual	Ave Yrs.Serv.
Schools:	2,140	(55%)	$1,200	$14,400	24.35
State:	604	(16%)	$1,162	$13,944	22.14
Counties:	595	(15%)	$ 802	$ 9,624	19.81
Cities:	386	(10%)	$ 803	$ 9,636	19.14
Other:	155	(4%)	$1,068	$12,816	20.76

By Average Benefit

The retirees are almost evenly split – 56% to 44% – between those earning less than $500 per month in retirement from IPERS and those earning $500 or more. However, a large minority – 20% – *still*[168] receives less than $200. While not the definite answer behind the great variance among benefits received, the *years of service* a member has when beginning retirement is, nonetheless, one of the key reasons why some retirees receive so much more in retirement than

[165] If the very *oldest* are excluded, the ratio is 58%-42%. Among the oldest (75 or older), only 35% are men. Another way of viewing this same segment is by *years retired.* Of those retired more than 26 years, only 20% are men.

[166] This *may* indicate that more recent retirees are working longer before retiring. Or it may simply reflect the fact that IPERS has been in existence since the summer of 1953 and thus it is easier for more recent retirees to accumulate more years of IPERS' covered service. Or it may be a combination of the two.

[167] In the 1980s the General Assembly began distributing *dividend* payments to the oldest retirees. Over time, there came to be four distinct groups of *dividend-eligible* retirees: those who retired before 1976, those who retired between January 1976 and June 1982, those who retired between June 1982 and June 1986, and those who retired between June 1986 and June 1990. The *Favorable Experience Dividend (FED)* eligible group is all who retired (and who have yet to retire) after June 1990. These dates are not arbitrary; rather, they mark periods of significant benefit enhancements.

[168] After the two hikes in benefit levels for the longest retired in the last four years.

do others. Other important factors include *average of highest wage years used in the formula*, the *actual formula* used at retirement, and, of course, *how long ago* a person retired. There is no discounting, either, the fact that women on the average receive a lesser salary than do men. Hence their pensions will be – on the average – also lower.

Benefit Amount	Number	%	Ave. Benefit	Annual	Ave Yrs.Serv.
< $200	12,549	(20%)	$ 99	$ 1,188	8.63
$200-499	23,329	(36%)	$ 330	$ 3,960	17.15
$500-699	8,121	(13%)	$ 586	$ 7,032	24.90
$700-999	8,185	(13%)	$ 849	$10,188	28.06
>$1,000	11,813	(18%)	$1,501	$18,012	32.12

By Age Group

The ratio of females to males in retirement is relatively constant at 58% to 42%, *except* for the oldest grouping – those 75 years of age and older – where it increases to 65% to 35%. In every age group, except the last, men also have higher years of service, averaging from 2 to 5 years greater.

Age	%	Number	Female	%	Male	%
< 55	1%	526	291	55%	235	45%
55-59	4%	2,309	1,329	58%	980	42%
60-64	12%	7,783	4,485	58%	3,298	42%
65-69	20%	12,552	7,306	58%	5,295	42%
70-75	24%	15,695	9,105	58%	6,590	42%
>75	39%	25,132	16,351	65%	8,781	35%

Age	Female Average Benefit	Yrs/Service	Male Average Benefit	Yrs/Service
< 55	$545	14.33	$ 724	16.32
55-59	$720	19.30	$ 1,356	25.81
60-64	$822	21.64	$ 1,295	26.81
65-69	$662	20.57	$ 927	24.03
70-75	$484	19.51	$ 598	21.07
>75	$380	19.50	$ 404	18.63

By Years of Service

Years of Service	% of all Retirees	Female	%	Male	%
< 10	20%	7,688	60%	5,183	40%
10-19	30%	12,906	67%	6,465	33%
20-29	28%	11,681	66%	5,996	34%
>30	22%	6,592	47%	7,485	53%

Female Male

Years of Service	Average Benefit	Yrs/Service	Average Benefit	Yrs/Service
< 10	$120	7.60	$ 155	7.18
10-19	$327	15.40	$ 408	15.19
20-29	$677	24.53	$ 800	25.07
>30	$1,094	34.90	$ 1,320	34.78

By Years Retired

Years Retired	% of all Retirees	Female	%	Male	%
< 1	2%	859	56%	665	44%
1-5	29%	10,674	57%	8,154	43%
6-10	24%	8,827	59%	6,203	41%
11-15	20%	7,708	60%	5,175	40%
16-20	13%	5,343	64%	3,054	36%
21-25	8%	3,432	71%	1,418	29%
26-30	3%	1,670	80%	405	20%
31-35	1%	312	86%	49	14%
36-40	<1%	38	86%	6	14%
>40	<1%	4	100%	0	0%

	Female		Male	
Years Retired	Average Benefit	Yrs/Service	Average Benefit	Yrs/Service
< 1	$811	20.63	$ 1,140	22.45
1-5	$739	20.39	$ 1,052	23.25
6-10	$516	19.98	$ 692	22.65
11-15	$427	19.32	$ 518	20.75
16-20	$380	19.07	$ 408	18.88
21-25	$315	19.24	$ 297	18.36
26-30	$349	21.95	$ 317	21.35
31-35	$358	23.52	$ 339	23.54
36-40	$376	25.67	$ 354	28.20
>40	$516	37.18	N.A.	N.A.

By Dividend Group

	Pre January 1976	*1976-June1982*	*July1982-June1986*	*July1986-June1990*
% of all Retirees	6%	14%	13%	18%
Number of Retirees	3,958	8,849	8,597	11,293

Average Benefit	$321	$352	$433	$499
Average Yrs/Service	20.38	19.06	19.33	20.51

	Pre January 1976	*1976-June1982*	*June1982-June1986*	*June1986-June1990*
Range of Benefits Within Group				
<$500	81%	77%	65%	58%
$500-999	19%	22%	32%	33%
$1000-1499	0%	1%	3%	9%
$1500-1999	0%	0%	0%	<1%
>$2,000	0%	0%	0%	0%

The FED[169] Eligible Group

% of all Retirees	49%
Number of Retirees	31,300
Average Benefit	$787
Average Yrs/Service	21.49
Range of Benefits Within Group	
<$500	44%
$500-999	23%
$1000-1499	17%
$1500-1999	11%
>$2,000	5%

[169] Favorable Experience Dividend – for all who retired, or will retire, following June 1990.

Part Two: Key Overview of System Performance

Data

Member Demand Measures		Fiscal Year 1999		Fiscal Year 1998
Benefits Counseling:				
Number of persons receiving pre-retirement counseling in-house		4,300		3,473
Number of persons receiving pre-retirement counseling throughout State		3,535		2,837
Number of estimates prepared		66,528		46,376
Number of new retirees added to payroll		4,421		4,279
Death Benefits:				
Number of reported deaths		2,365		1,927
Number of beneficiaries paid		717		771
Amount paid in IPERS death benefits		$ 8,511,067.63		$8,660,765.80
Retirement Benefits:				
Amount paid in IPERS retirement benefits		$461,766,375.49		$398,486,449.88
Number of IPERS retirees		64,311		62,118
Average monthly benefit		$593,14		$535.51
Refunds:				
IPERS Refund Requests paid		5,632		6,099
Total Paid as Refunds (Supplementary Refunds)		$ 7,792,437.16 $ 297,290.69		$ 17,350,306.26 $321,467.71
Service Purchases (Buy-In and Buy-Backs):				
Applications for Service Purchase		4,724		2,945
Paid Service Purchases		4,532		2,269
Totals paid in Service Purchases		$19,012,074.22		$ 7,741,258.69
Miscellaneous Information:				
Phone calls logged by staff		98,187		80,166

Member Demand Measures Continued		Fiscal Year 1999	Fiscal Year 1998	
Notices Sent to Terminating Employees		7,850	8,022	
Statement of Account Requests		10,692	9,815	
Outside of Office Presentations Attendees:		111 5,381	75 1,821	
Actuarial Equivalent Claimants		968	571	
Gross Actuarial Equivalent Totals Paid:		$1,327,966.17	$978,014.84	
Beneficiary Forms & Form Changes:		29,776	N.A.	
Age 70 Notifications		2,470	N.A.	
Retirees with Adjustments		65,497	N.A.	
Number of Retired Re-Employed Refunds		123	N.A.	
Amount of Retired Re-Employed Refunds		$ 314,406.87	N.A.	
Number of Accounts Verified		22,788	N.A.	

Discussion and Projection

Number of New Retirees

Over the past twelve years, the number of new retirees annually has ranged from 3,200 to 4,500 (the latter in the earlier 1990s when the State, and other System covered employers, were downsizing). There appears to be a steady increase, which began in Fiscal Year 1999, in this base line number. We believe this reflects the demographic "bulge" of the baby boomer generation who are just entering, or nearing, retirement. *Forecast: Continuation of this increase through approximately 2010.*

Total Number of Retirees

There were approximately 47,000 retirees in 1987 vs. 64,311 at the end of Fiscal Year 1999. *Forecast: By 2010, the total retiree population will range from 92,000to 95,000. Over 32,000 of current retirees are 70 years of age or older. In keeping with national demographic trends, we expect this "older" group of retirees to keep growing in number.*

Amount Paid in Retirement Benefits

The size of increased benefit payouts is predictable, given significant benefit enhancements of the last dozen years. By way of comparison, in Fiscal Year 89 the total payout was $169,173,736. At the conclusion of Fiscal Year 1999 the total had risen to $461,766,375. *Forecast: Annual retirement payouts will be in the $900,000,000 to $1,200,000,000 range by 2010.*

Average Monthly Benefits

As of June 1999 the average benefit is $593.14, while in Fiscal Year 89 it was $296.18 per month. Members who retired prior to July 1990 receive an annual *Cost of Living Dividend Adjustment (COLDA)* as an annual lump sum payment in November. Persons retiring after June 1990 are eligible for the new *Favorable Experience Dividend (FED)* program, initiated in January 1999. Both programs are capped at a maximum 3% annual increase. *Forecast: Average benefits paid all retirees, excluding the COLDA and FED payments, will be in the range of $1,200 - $1,400 per month by 2010. The longevity of IPERS' retirees, coupled with the marked disparity in benefits received by the newer retirees contrasted to those longest retired, may well increase pressure for further "adjustments" to those longest retired.*

Employee-Employer Contributions

Except for our special service (public safety) occupations, which by current law are to fluctuate annually to reflect actual costs of the System's benefits for them, the 3.7% paid by employees and 5.75% paid by employers has remained constant for 25 years. These contributions, together with returns on our Trust Fund's investments, "fuel" the System and are the means whereby we cover our liabilities. The amount of these contributions has grown substantially from $216 million in Fiscal Year 1991 to over $348 million in Fiscal Year 1999. The increase from one fiscal year to the next is now modest, and mirrors any increase in the total covered salaries of our151,000 active members. *Forecast: The total annual contributions should be in the $700-$800 million range by 2010.*

Part Three: Summary Information Regarding Payouts to Retirees Made in Accordance with 1998 Legislation

Cost of Living Increases (Dividend)

1. Eligible: Those folks who retired *before* July 1990.
2. Method to Determine Payment Amount: The Legislature first authorized IPERS to pay an annual *dividend* distribution to the longest retired members in the early 1980s. For many years after that, the Legislature both increased the amount paid to those eligible and added new eligible groups. By the time the Legislature authorized IPERS to make annual adjustments, referencing the cost of living index for the previous year, there were four distinct eligible groups:

- Those who had retired prior to January 1, 1976;
- Those who had retired between January 1, 1976 and July 1, 1982;
- Those who had retired between July 1, 1982 and July 1, 1986; and
- Those who had retired between July 1, 1986 and July 1, 1990.

Before 1996 the Legislature periodically (usually, about every two years) authorized an increase in the *dividend* amount, with the higher percentage increase going to those longest retired. *After* 1996, IPERS was instructed to increase the *dividend* by the following method: multiply the previous year's total monthly benefit payments plus the *dividend* payable that year by a figure equivalent to 80% of the Consumer Price Index (C.P.I.) for the previous year, not to exceed 3%.

3. How Computed: 1.33% (80% of the C.P.I.) x ((monthly benefit x 12)+ previous years' dividend)
4. Total Paid: $14,087,358.65.
5. Paid to: 33,514 members:

- $2,334,281.20 to 4,233 members who retired prior to January 1, 1976
- $5,370,268.23 to 9,152 members who retired between January 1, 1976 and July 1, 1982;
- $$3,270,961.78 to 8.717 members who retired between July 1, 1982 and July 1, 1986; and
- $3.111,847.44 to 11,410 members who retired between July 1, 1986 and July 1, 1990.

Favorable Experience Dividend (FED)

1. Eligible: Those folks who retired *after* June 1990 *and who have been retired for at least one full year.*
2. Method to Determine Payment Amount: The 1998 legislation establishing the FED allowed IPERS to pay a distribution maximum of 3%, dependent upon the actuary certifying such were possible. IPERS reviewed the amount paid as a *Cost of Living Increase* to all who

retired prior to July 1990 – 1.33% [170]– and decided that it was an appropriate figure to also use in paying our first ever FED.[171]

3. How Computed: 1.33% x total of annual benefits paid x full years retired.
4. Total Paid: $12,152,683.44.
5. Paid to: 27,210 members and 629 beneficiaries of deceased members.

Permanent Increase in Monthly Benefits

1. Eligible: Persons who retired *prior* to July 1, 1990.
2. Method to Determine Payment Amount: Established by 1998 legislation.
3. How Computed: monthly benefit + 15% (or 7%) of monthly benefit.
4. Annualized Total Paid: $15,770,550
5. Paid to:

- 21,886 members who retired *before* July 1, 1986 received a 15% increase:
  - ♦ Persons who retired before January 1, 1976 saw their average benefit increase from $239.02 to $274.87;
  - ♦ Persons who retired after January 1, 1976, but before July 1, 1982, saw their average benefit rise from $262.50 to $301.88; while
  - ♦ Those who retired after July 1, 1982 but before July 1, 1986 enjoyed a benefit increase from $349.34 to $401.73.
- 11,368 members who retired *after* July 1, 1986 received a 7% increase, with their average benefit rising to $475.21 from $445.06.

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[170] The Cost of Living payable to persons who retired prior to July 1990 is to be annually determined by IPERS, conditional upon our ability to pay, by multiplying the preceding year's Consumer Price Index figure by 80%. In any case, the amount so determined is not to exceed 3%.

[171] We are sensitive to the potential difficulties we might experience should we have a disconnect between the percentage paid to pre-July 1990 retirees and those who retired after that date. Our goal, together with that of legislators, was to bridge the perceived *equity* gap between those who received some form of a cost of living adjustment and those who did not (prior to 1998, all who had retired after June 1990), not to create a new perceived disparity of treatment.

Appendix Four: Dimensions of Retirement Planning

Demographic Shifts

The "baby boomers," those born in the immediate post-World War II years, are aging. As they near retirement they are beginning to focus on what they will need to financially survive during this extended period. Their sheer numbers will place intense strain on all pension systems, public and private, for three major reasons. First, they represent such a major demographic "bulge" that they will markedly swell the numbers of those retired, from 12.6% of the population in 1990 to an estimated 16.3% in 2020.[172] Second, because people are living longer in retirement, their "draw down" of pension benefits will likely have a significant impact on retirement fund reserves and, possibly, even on the financial markets themselves.[173] Third, they are followed in the work force by significantly fewer younger workers. The result is a projected decrease in worker-to-retiree ratios from the present 2.9 persons to only 2.1 in 2020.[174] This will mean the financial "carrying power" burden of the working young for the retired elderly will increase. It is crucial that retirement systems at all levels incorporate these realities into future Plan design.

Crisis of Social Security

As is increasingly apparent, whether something will be done to Social Security as presently structured is no longer the question. Rather, it is what will be done when, and how far will those adjustments go.

Social Security's chief difficulty is that it is structured as a "pay as you go" system, and not one which uses "your investments" to pay for "your retirement."[175] Social Security, however, is an

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172 Percentages expressed are for those 65 years of age and older. Source: World Population Prospects, 1992 edition, U.N. publication. Cited in "A Global Trend: Privatization and Reform of Social Security Pension Plans," by William G. Poortvliet and Thomas P. Laine, Benefits Quarterly, Vol. 11; No. 3; 1995; p. 67.

173 The surge in dollars pouring into mutual funds in the 1990s represents, to no small degree, the baby boomers' efforts to salt away sufficient resources for their retirement. Once they attain retirement age, the dollar flow may reverse as they begin to liquidate those savings in order to maintain their purchasing power in retirement.

174 "A Global Trend...", Benefits Quarterly, op. cit., p. 69.

175 Actually, this is a feature, to a greater or lesser degree, of all defined benefit plans. A *defined benefit* plan, such as IPERS, uses a formula which is designed to reflect a combination of years of service and recent wage in order to determine monthly lifetime benefits. Its eventual payout is not intended to precisely mirror total contributions made by members and employers (plus accumulated earnings). Investment (market) risk is entirely assumed by the Plan, not the employee. A *defined contribution* plan, on the other hand, typical of the newer private plans, is truly a "what you see is what you get" plan; a person at retirement can draw down only that paid in plus accumulated earnings. Investment (market) risk is entirely assumed by the employee. Debate continues over which type plan is more favorable. In general, consensus appears to favor using a *defined benefit* plan as the core plan while providing *defined contribution* plans as supplemental offerings. In Iowa, IPERS is the core *defined benefit* plan for the bulk of our public employees, while the State's deferred compensation program and the tax-sheltered annuities offered by school districts are examples of supplementary plans and are *defined contribution* in nature.

extreme example because most of the revenue stream from today's workers is used to pay for current retirees. Once younger workers retire, it will be up to those following them to pay for their retirement. The problem, however, is that the baby boomers must be "supported" by fewer active workers. Without substantial changes, the present system will become insolvent around 2025.[176] The most likely modifications will probably entail reduced benefits and/or higher contribution rates. The conclusion is inescapable: those generations following the baby boomers will have an even more difficult time of providing for their own retirement, let alone helping to pay for the retirement of the baby boomers.[177] State pension plans must be conscious of this factor in refining their own plan designs.

Inadequate Private Savings

Funding for retirement has long been thought to involve the "three-legged stool" of Social Security, an employer-sponsored pension plan, and individual savings. Because of the growing problems involving Social Security, the role of workplace pension plans and private savings loom even larger.

If Social Security benefits are reduced to bring the system into actuarial balance, then the other two sources of retirement income - personal savings and employer-sponsored retirement plans - will have to be increased....Many experts fear that the U.S. savings rate is far too low to take on that burden, however. The U.S. national savings rate...held fairly steady at approximately 8 percent of gross domestic product (GDP) from the 1950s through the 1970s. But in the early 1980s, the national savings rate declined substantially, hitting an all-time low of less than 2 percent of GDP in the period 1990 to 1993...The level of personal savings declined from nearly 6 percent of GDP in the early 1970s to slightly more than 3 percent of GDP in the early 1990s.[178]

In 1970, the source of retirement benefit payments was 62% from Social Security, 22% from government pensions, and 16% from private pensions. By 1992, the ratio had changed to 49.9% from Social Security, 18.7% from government pensions, and 31.4% from private pensions.[179] A recent report from the Rand public policy "think tank" showed that the median retired household contributes only 10.9% in private savings to help with total post-retirement costs.[180] The median white household with members between the ages of 51 and 60 has "less than $18,000 in personal

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176 Source: Office of the Actuary, Social Security Administration. Cited in Who Will Pay for Your Retirement: The Looming Crisis, a Statement by the Research and Policy Committee of the Committee for Economic Development, New York; 1995; p. 3.

177 For "almost all individuals who currently receive [Social Security] benefits, the annuity value of their benefits exceeds their contributions paid (plus interest)....However, the return for all new retirees is falling rapidly and will become negative for higher-income individuals (particularly men) later in this decade. Single individuals retiring early in the next century face deeply negative returns." Who Will Pay..., op.cit., p. 33.

178 U.S. Retirement Policy: The Sleeping Giant Awakens, The Wyatt Company, 1994; p. 21.

179 Source: Employee Benefit Research Institute in its citation of U.S. Retirement Policy..., op.cit. p. 27.

180 Source: Rand Report on Wealth and Savings, cited in "Middle-Aged, Elderly Have Fewer Assets Than Expected," The Wall Street Journal, July 15, 1995.

wealth" excluding real estate, whereas the "typical black and Hispanic couple in the same age range has less than $500 in liquid assets."[181] Rand further notes that "wealth disparity in the United States is several times greater than differences in income and the implications should set off alarm bells for the retirement prospects of baby boomers and the generations to come after them...." The top 5 percent of white families with at least one spouse older than 70 have accumulated wealth of $655,000 - seven times the $90,000 in wealth held by median white households. The bottom 10 percent of white households has managed to accumulate less than $800.

As we look to restructure elements of IPERS' plan design, we must be aware of the disparity between the growing importance of private savings as an element of financial security in retirement and the evidence that may persons will have little in the way of private savings to devote to retirement. Furthermore, the growing wealth gap between the relatively small number of persons who have comfortable savings and the large (and apparently growing) number of persons with little private resources suggest that this must also be factored in to our plan design. In the long run, this could most be advanced through a coordinated effort to develop a national retirement policy.[182]

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[181] "Middle-Aged, Elderly...", op. cit.

[182] See "National Retirement Policy - An Awakening," by Cathie G. Eitelberg in Employee Benefits Digest, Vol. 33, No. 1; January 1996; International Foundation of Employee Benefit Plans.