



# The LATEST WORD

Summer 2006

FOR IPERS EMPLOYERS

## Governor signs bill authorizing contribution rate increase

*Vilsack says action secures good futures for Iowa's public servants*

Governor Tom Vilsack signed House File (HF) 729, authorizing a contribution rate increase that is an important first step in securing IPERS' long-term financial health.

The two percentage point increase in contributions to IPERS is phased in over four years beginning July 1, 2007. Employers will pay 60 percent and employees 40 percent of the increase.

"Although IPERS' current finances are healthy and sound, this forward-thinking measure will address rising retirement costs and the future health of the fund," said Vilsack. "This law will secure good futures for the people who work day in and day out to protect our communities, care

**IPERS Contribution Rate (Regular IPERS Members)**

	Current	7/1/07	7/1/08	7/1/09	7/1/10
<b>Employee Rate</b>	3.70%	3.90%	4.10%	4.30%	4.50%
<b>Employer Rate</b>	5.75%	6.05%	6.35%	6.65%	6.95%
<b>Combined Rate</b>	9.45%	9.95%	10.45%	10.95%	11.45%

for our loved ones, and educate our children."

Although less than requested, IPERS CEO Donna M. Mueller stated that phasing in an increase now is a smart move. "Chipping away at debt and addressing rising costs sooner rather than later saves money in the long run," stated Mueller.

Mueller noted that retirement costs are rising because people are living longer. The number of retirees is also

projected to rise sharply as baby boomers reach retirement age.

The contribution rate increase is the first one since 1979. The rate applies to all IPERS members except for sheriffs, deputy sheriffs, police, firefighters, correctional officers, and those in other protection occupations, who contribute at rates determined annually by IPERS' actuary.

More details on HF 729 are in the legislative wrap-up on page 2.

## Current Special Services contribution rates similar to 1996 rates

*Annual adjustments keep benefits fully funded*

Although the contribution rates for IPERS Special Service members are about what they were ten years ago, the rates have been sufficient to keep benefits fully funded—even with benefit increases. This is possible because each year IPERS adjusted contributions to respond to changing needs. Only the legislature can change the contribution rate for IPERS' regular members, who comprise about 96 percent of IPERS' total membership.



Every year IPERS' actuary completes an annual valuation that looks at the characteristics of people

joining and leaving IPERS, benefit changes, and the economic outlook. Contribution rates are adjusted based on the valuation. The small, constant rate changes allow IPERS to respond quickly to rebalance the long-term funding equation.

IPERS needed an influx of contri-

butions for all members not in the Special Service class because it cannot adjust rates as characteristics of IPERS regular members, the benefits, or the stock market change. The rate for regular IPERS members has not changed in more than 25 years.

**Special Service Contribution Rates\***

	FY1996	Through June 30, 2006	July 1, 2006–June 30, 2007
 <b>Protection Occupations</b>	15.03%	15.39%	<b>15.20%</b> 6.08% employee 9.12% employer
 <b>Sheriffs and Deputies</b>	17.12%	16.40%	<b>16.74%</b> 8.37% employee 8.37% employer

\*The rates reflect that benefits for Special Service members differ from those for regular members.



## IPERS Legislative Wrap-Up

### House File (HF) 729

(HF 729 also makes changes to the Judicial Retirement System.)

**1** Increases the contribution rate by one-half percentage point a year for four years, beginning July 1, 2007.

Read about this change on page 1.

**2** Limits how much people can inflate their wages to get a higher pension.

IPERS uses the average of the highest three years of wages to figure the amount of a member's pension. The higher the average wage, the higher the pension. However, people do not pay their fair share for their higher pensions when there are huge wage increases in the highest three years compared with the rest of their employment history.

Beginning July 1, 2007, IPERS will use a spiking control that limits how much of a wage increase applies when calculating pensions. IPERS will compare the average of the highest three years, or the final average salary, to the fourth highest year's salary.

If the final average salary is more than 121 percent of the fourth highest wage, the final average wage is adjusted. This approach allows for a wage

increase of approximately 10 percent in each of the highest three years.

**3** Restricts retirees who return to work for an IPERS-covered employer while drawing an IPERS pension from diverting wages to noncovered types of compensation in order to avoid the cap on earnings.

Employer contributions to deferred compensation retirement plans, currently not considered wages by IPERS, will count as earnings starting July 1, 2007, although IPERS will not collect contributions on them. IPERS reduces pensions when retirees earn more than the limit.

**4** Cancels a future change in how the final average salary used in the benefit formula is figured.

On July 1, 2008, IPERS was scheduled to start using the average of the highest twelve consecutive quarters of wages in the benefit formula, rather than the highest three years. IPERS originally requested the change because of its potential to control intentional wage spiking that inflates pensions.

IPERS twice has asked for an extension of the deadline. IPERS still does not have the technology necessary to move to the highest twelve consecutive quarters. IPERS also determined the change was not an effective way to control wage spiking.

*Example: Joe, age 65, retires in 2009 after working 30 years in an IPERS-covered position.*

**Step 1. Figure the final average salary.**

Joe's highest three years of salary are:

2007 — \$50,000

2008 — \$55,000

2009 — \$75,000 (year of retirement)

$$\$180,000 / 3 = \$60,000$$

Joe's final average salary is \$60,000.

**Step 2. Figure the spiking control by multiplying the highest annual salary outside the highest three years by 121%.**

Joe's next highest annual salary was \$46,000 in 2006.

$$\$46,000 \times 121\% = \$55,660, \text{ the spiking control}$$

**Step 3. Compare the final average salary from Step 1 and the spiking control in Step 2.**

Joe's final average salary = \$60,000

Spiking control = \$55,660

Since \$55,660 < \$60,000, \$55,660 is used as the final average salary in the formula to figure Joe's benefits.

IPERS Benefit Formula				
Formula	Final Avg. Salary	X	Multiplier	= Annual Benefit
	Avg. highest 3 yrs. salary		2%/year for 30 yrs; 1%/year next 5 yrs	
Current Law	\$60,000	X	60%	= \$36,000 (\$3,000/month)
Law Change 7/1/07	\$55,660	X	60%	= \$33,396 (\$2,783/month)

**The spiking control will not affect the benefits of most IPERS members.**

An employee can receive an increase in salary averaging about 10 percent a year before the spiking control applies. The spiking control affects Joe's benefits because of his atypical wage increases during the three years in which he earned his highest salaries (more than a 36 percent increase in the last two years).

**5 Restricts IPERS from transferring money into the Favorable Experience Dividend (FED) Reserve Account based on favorable actuarial experience, unless IPERS is fully funded. The transfer also must not bring IPERS below fully funded status.**

The Legislature created the thirteenth, or FED, check for retirees, recognizing that pensions lose their buying power over time. IPERS does not have a traditional cost-of-living adjustment. The Legislature established a reserve account with money transferred from the general IPERS Fund to pay the checks. The Legislature allowed for additional transfers to replenish the reserve account when IPERS has favorable actuarial experience. Favorable actuarial experience occurs when long-term assets and liabilities are better than predicted.

Under HF 729, IPERS can transfer additional money from the general IPERS Fund to the reserve account only when assets fully fund all pension liabilities. However, IPERS continues to credit investment earnings to the reserve account.

**6 Restricts IPERS from transferring money from the general IPERS Trust Fund into supplemental accounts of active members (SAAM).**

This technical change is necessary because of the limit on transfers into the FED Reserve Account. IPERS has never used the SAAM provision because of funding.

**7 Allows future benefit increases only when IPERS is fully funded or the Legislature passes a contribution rate increase to pay for the benefit.**

Current law contains only the second restriction. IPERS must also

stay fully funded immediately after implementing the benefit increase.

**8 Requires the Public Retirement Systems Committee to report to the Legislature by October 1, 2007, on alternatives to the current IPERS plan.**

The committee will review pension flexibility, including defined contribution, supplemental, and hybrid retirement plans, and cost-of-living adjustments.

## HF 2245, IPERS' Technical Changes

*(The bill also contains changes for the Municipal Fire and Police Retirement System. All changes take effect July 1, 2006, unless otherwise noted.)*

**1 Couples requirements for closing inactive IPERS accounts with the Internal Revenue Code (IRC).**

Currently state law says IPERS must cash out accounts that have been inactive for five or more years if the account balance is less than \$3,000. IPERS already changed its practice to comply with the current \$1,000 IRC limit. This change is retroactive to January 1, 2006.

**2 Makes reporting deadlines consistent.**

IPERS currently must submit its comprehensive annual financial report to the Governor by December 15. This deadline is different from the end-of-December reporting deadline for sending the report to the Government Finance Officers Association, which sets standards for financial reporting.

**3 Keeps the current method used to determine a person's final average salary.**

HF 2245 included this provision in

case HF 729 did not pass. Because HF 729 did pass, a third bill removes the duplication.

**4 Amends the definition of "eligible service" that counts in qualifying for retirement benefits for sheriffs and deputy sheriffs.**

Currently service in some, but not all, of the other protection occupations is counted. For example, currently if an airport firefighter or local county conservation officer becomes a county sheriff or deputy sheriff, the time that person worked as an airport firefighter or conservation officer does not count toward the retirement benefits for sheriffs and deputies. However, other firefighters in IPERS' Special Service group who would later become sheriffs or deputy sheriffs could count their firefighting service as "eligible service."

Although IPERS has two categories of Special Service members (sheriffs/deputy sheriffs and other protection occupations) with slightly different retirement benefits, all the members are in a public safety position. All pay an actuarially determined contribution rate that is higher than that paid by regular IPERS members.

**5 Allows licensed health care professionals in some public hospitals a one-month bona fide retirement period until June 30, 2010.**

A report to the Legislature on whether the shortened bona fide retirement period should be continued is due October 1, 2009.



## IPERS Performance Report

### Private equity investments: #1

IPERS was the best of all public retirement systems in the United States in selecting private equity investments, according to Private Equity Intelligence (PEI), a London-based company. One report on the PEI study results called IPERS a "savvy private equity investor." (*Institutional Investor: Hedge Fund Daily*, April 12, 2006.)

IPERS' private equity investments returned 19.8 percent for fiscal year 2005, which ended June 30. Second best was the Oregon State Treasury. The California State Teachers' Retirement System came in third.

Overall, IPERS' investments returned 11.25 percent in fiscal year 2005. The Trust Universe Comparison Service (TUCS), a respected investment benchmarking company, reported that IPERS' returns ranked in the top quartile in three of the TUCS institutional investor peer universes: TUCS Public Pension Funds with Assets Greater than \$1 billion, TUCS All Master Trusts Universe, and TUCS Public Funds Universe.

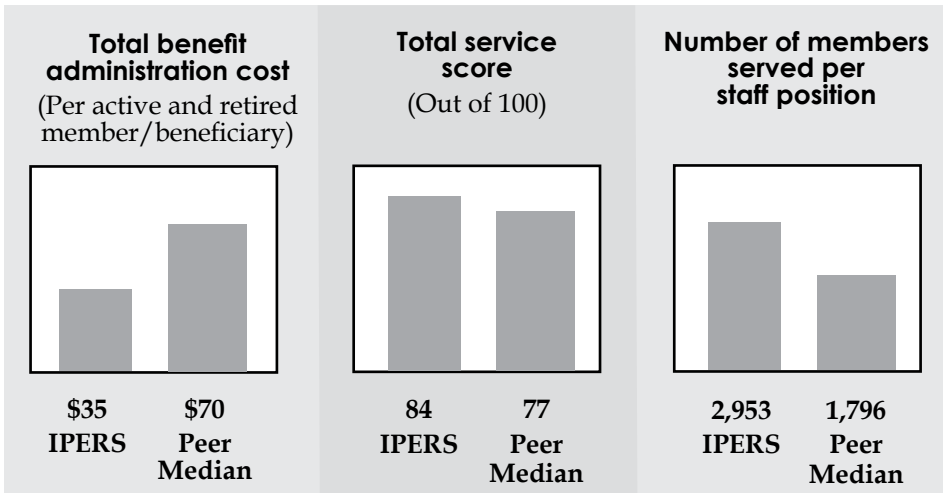
IPERS benefits are guaranteed regardless of IPERS' investment performance, but performance is critical because investments provide the largest percentage of income from

which benefits are paid. Net investment portfolio assets were \$18.745 billion on June 30, 2005. Assets have since topped \$20 billion.

### IPERS benefit administration costs lower by half

An independent company that reviews costs and performance of public retirement systems found IPERS' fiscal year 2005 benefit administration costs were lower than those of nearly all other public retirement agencies of a similar size in a recent study.

CEM Benchmarking Inc. rated IPERS' services high and concluded IPERS' administration costs were half the median of the costs of the comparison group. CEM reviewed 54 pension organizations and compared IPERS to 16 from that group that are similar in size and membership, including several systems in the Midwest. CEM, a private company based in Canada, reviews performance and costs of public pension systems in the United States and abroad.



You can read the entire 2005 CEM Benchmarking report at [www.ipers.org/publications.htm](http://www.ipers.org/publications.htm).

## IPERS to issue membership cards

*Change to protect social security numbers will not affect employer reporting*

Employees who are covered by IPERS will receive a membership card reflecting a newly assigned IPERS number, potentially as early as this fall. Assigned member identification numbers will replace social security numbers for accessing a member's

account information. IPERS is removing social security numbers from forms and correspondence.

"As identity theft becomes more and more common, we want to help our 300,000 members protect their personal information," stated Donna M.

Mueller, CEO of IPERS.

The change will not affect how employers report wages. The exact issue date for membership cards depends on the success of computer program testing.



IPERS CEO  
Donna M. Mueller

## Things change and so will we

The stock market drops. People live longer. Baby boomers reach retirement age.

IPERS can't control forces external to us. Therefore we need to adjust as things change.

Increased contributions are necessary because of past changes in benefits, life expectancy, and the stock market. IPERS' actuary will begin accounting for increased contributions authorized by the Legislature, but a retirement system's finances are so long-term that the increase will not bring down IPERS' unfunded liability for some time.

In the next few years as we assess how well the contribution increase is shoring up IPERS' long-term finances, we know that other things will change. Yet IPERS has no timely way to adjust, even minutely, the rate at which public employees and their employers pay into IPERS.

Not being able to adjust rates is costly. We estimated we lost over \$170

million in contributions and investment income by delaying the first 0.5 percentage point increase from July 2004, when IPERS first asked for an increase, to July 2007.

IPERS can adjust the contribution rates annually – up or down – for sheriffs, deputies, police, firefighters, correctional officers, and a host of others in jobs that protect the public's safety. As reported on page 1, those small, constant changes result in rate stability over time. We were able to keep the retirement benefits for IPERS' public safety groups funded at or near 100 percent with little variation in rates, even with benefit improvements, because we could adjust rates each year.

To be in a better position to manage change effectively and keep costs down, I will recommend that Iowa's Legislature establish a board of trustees with the authority to adjust rates within a set range each year for all members. We already have learned how costly delays can be.

I also will join employer representatives on the IPERS Benefits Advisory Committee in trying to answer many important questions as we search for

how best to change:

- *How do we stay flexible without trying to be all things to all people?*
- *How do we keep rising retirement costs from overwhelming employers and employees?*
- *How will retirement change as baby boomers seek second careers, work part-time, or reject retirement totally?*
- *What changes to employee benefits, including retirement benefits, are needed to address projected shortages in the work force?*

Maybe we can't predict the future, but we can prepare for it.

### IPERS Benefits Advisory Committee Employer Representation

**Iowa Association of Community College Trustees**

*Dr. Gene Gardner*

**Iowa Association of Counties**

*Jim Maloney, Polk County Assessor*

**Iowa Association of School Boards**

*Len Cockman*

**Iowa League of Cities**

*Alan Kemp*

**State of Iowa**

*Mollie Anderson,*

*Department of Administrative Services*

## Goos wants you to ace your next compliance review



Wayne Goos, an IPERS employer relations representative, knows how hard it is to keep complex policies straight. As a former private sector manager, he has had

to comply with his share of rules.

That did not stop Goos (pronounced Güz) from seeking a job at IPERS that

includes conducting employer compliance reviews to make sure employers are following IPERS' rules.

"I didn't want to be tied to a desk," explained Goos. "The parts about retail I enjoyed most were getting out and meeting people."

Goos explained that his current job allows him to travel to visit with employers. He sees his role in compliance as an opportunity to train and help employers.

"Sometimes people are nervous when I come for a compliance review," stated Goos. "When I leave, they usually tell me it wasn't as bad as they thought it would be."

Goos is an Iowa native. He grew up in southwest Iowa and graduated from Iowa State University. He recently returned to Iowa from Nebraska.



# IPERS

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Please share with your employees

## Benefit Education & Retirement Planning

### Group presentations

- IPERS overview and answers to general questions.
- Recommended for new to mid-career IPERS members.

### Individual counseling

- Projection of benefits and discussion of options.
- Recommended for everyone retiring in three to five years, and open to anyone.
- Evening appointments fill up fast; call soon.
- Appointment confirmation letter mailed to you. (Please call if you can't keep your appointment so we can schedule someone else.)

### Telephone counseling

- For those unable to meet with an IPERS representative in your area or at the IPERS office in Des Moines.
- Call 1-800-622-3849 weekdays, 7:30 a.m.-5 p.m.
- Benefit projections sent to you by mail.

## Iowa State Fair—IPERS Booth

August 10–20, 2006

Talk to a representative or pick up information explaining your IPERS retirement, death, and disability benefits. Look for our booth in the Varied Industries Building.



[www.ipers.org](http://www.ipers.org) Check the IPERS Web site often for counseling updates and other news.

	Group Presentation (No registration needed)	Individual Counseling (Call 1-800-622-3849 to schedule)
<b>Cherokee</b> , Cherokee Community School District, 600 West Bluff St.	July 24, 2006, 6:30 p.m.	July 24–25, 2006
<b>Storm Lake</b> , Buena Vista Regional Medical Center Education Center Sections A & B, 1525 West Fifth Street		July 26–27, 2006
<b>Sioux City</b> , Western Iowa Tech Community College, 4647 Stone Avenue, Robert H. Kiser Building, Room D103 (Park in Lot 4. Use Entrance 14.) AmericInn, 4230 Lewis Boulevard, Rooms 202 & 204	July 31, 2006, 7 p.m.	August 1–4, 2006
<b>Cedar Falls</b> , Hawkeye Community College, 5330 Nordic Drive AmericInn, 5818 Nordic Drive	Aug. 21, 2006, 6:30 p.m.	August 21–24, 2006
<b>Washington</b> , Washington County Hospital, 400 East Polk Street		August 29, 2006
<b>Mount Pleasant</b> , Henry County Health Center, 407 South White St.		August 30, 2006
<b>Iowa City</b> , AmericInn, 2597 Holiday Road		September 5–7, 2006
<b>Calmar</b> , Northeast Iowa Community College, 1625 Highway 150, Wilder Hall		September 11–14, 2006
<b>Davenport</b> , Country Inn & Suites, 140 East 55th Street		September 18–21, 2006
<b>Fort Dodge</b> , AEA 8—Prairie Lakes, 1235 Fifth Avenue South		September 25–27, 2006
<b>Jefferson</b> , Greene County Medical Center, 1000 West Lincolnway		September 28–29, 2006
<b>Dubuque</b> , MainStay Suites, 1275 Associates Drive		October 3–5, 2006
<b>West Burlington</b> , AmericInn, 628 South Gear Avenue		October 9–12, 2006
<b>Iowa Falls</b> , Ellsworth Municipal Hospital, 110 Rocksylvania Ave.		October 18, 2006
<b>Webster City</b> , Hamilton Hospital, 800 Ohio Street		October 19, 2006
<b>Council Bluffs</b> , Council Bluffs Public Library, 400 Willow Avenue Country Inn & Suites, 17 Arena Way, Rooms 239 & 240	Oct. 23, 2006, 6:30 p.m.	October 24–26, 2006

## QA Independent Contractors and IPERS

### Q: Why does IPERS look at how an employer classifies employees and independent contractors?

**A:** Although an employer decides when it is better to hire an employee and when it makes more sense to use an independent contractor, IPERS has a responsibility to make sure employers correctly classify their workforce. By law, IPERS covers most public employees. IPERS does not cover independent contractors. Independent contractors have no rights to IPERS benefits, and neither the contractor nor the employer contributes to IPERS.

An employee wrongly classified as an independent contractor could lose benefits the person has a legal right to receive. When discovered and corrected, both the employer and employee must make up the IPERS contributions they should have paid.

### Q: How does IPERS determine if someone is an employee or an independent contractor?

**A:** IPERS reviews information submitted by the parties involved on a *Determination of Employee/Independent Contractor Status* form, available on IPERS' Web site. Although IPERS and the IRS use different forms, both forms collect similar facts that determine whether someone is an employee or an independent contractor.

IPERS also checks supporting documentation such as a job description, contract, and tax forms. IPERS may conduct an on-site review.

In each case it is essential to consider all the facts—generally no single fact provides the answer.

### Q: How often does IPERS check independent contractor relationships?

**A:** IPERS checks independent contractor relationships during routine compliance reviews. IPERS also performs reviews when requested by an employer or individual, and whenever IPERS becomes aware of a situation that appears questionable.

### Q: Can an independent contractor fill any position?

**A:** Several years ago, IPERS determined a school district could not comply with Iowa law if the district hired an independent contractor as a teacher or superintendent. An informal opinion by the Iowa attorney general's office supported this decision.

### Q: Why can't teachers and superintendents be independent contractors?

**A:** Iowa law specifies what must be included in a school district's contract with a teacher or school administrator. The contract requirements create a degree of control by school districts that makes teachers and superintendents common-law employees, regardless of any independent contractor label.

Under common law, a person is an employee if the employer has the right to control the details of how services are performed, regardless of whether the employer exercises that control or allows freedom of action. It also does not matter whether the person works part-time or full-time. What matters is the relationship between the person and the employer.

In addition, Iowa law strictly limits delegating essential governmental functions like those fulfilled by teachers and school superintendents.

### Q: If an employer files an IRS Form 1099 rather than a W-2 form, does this make the person an independent contractor?

**A:** No, filing a 1099 does not alone

make the person an independent contractor. There are three main categories of facts that determine whether an individual qualifies as an independent contractor. *Behavioral control* factors address who has the right to direct or control how the worker does the work. *Financial control* factors indicate control over the financial, business part of the work. *Relationship of the parties* factors show the type of relationship between the person and the agency.

### Q: Can an employee work for an IPERS-covered employer as an independent contractor after the employee retires?

**A:** Retirees can be independent contractors if they and the employers meet all requirements. IPERS has found some IPERS retirees have created bogus independent contractor relationships with employers to avoid IPERS' bona fide retirement period, or to avoid having their retirement benefits reduced when they exceed the limit on earnings. In such cases, the retiree must pay back any retirement benefits received in error.

*The Latest Word* is published quarterly by the Iowa Public Employees' Retirement System for participating employers and others interested in IPERS policy and funding.

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# what's inside.

**p1 Governor signs bill authorizing contribution rate increase**

Get more details on the increase in contributions needed to maintain IPERS' long-term financial health. The increase begins in 2007.

**p1 Current Special Services contribution rates similar to 1996 rates**

The fiscal year 2007 Special Service rates change July 1, 2006. Find out why annual rate adjustments are helpful.

**p2 Legislative wrap-up**

The Iowa Legislature made several changes to the IPERS Plan during the 2006 legislative session. One getting lots of attention is the spiking control that can be applied to benefit calculations. This and other changes

are explained in an item-by-item summary.

**p4 IPERS performance report**

Iowa's retirement system rates #1 in private equity investments, is providing quality service, and has low administration costs. Join IPERS in celebrating the good news.

**p5 From the CEO**

CEO Donna M. Mueller explains why keeping the IPERS contribution rate steady since 1979 has been costly. Learn why IPERS needs the ability to make timely, small rate changes.

**p6 Employers' help desk**

Access resources and get answers to frequently asked questions.

## Thanks for your help.

Many of you took part in two recent surveys—one on redesigning the IPERS Web site and another on making electronic payments of contributions. We will include the results in the next newsletter and let you know how we are using the results to take action.