

SOCIAL SECURITY AND THE TEACHER

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FOREWORD

Social Security coverage for Kentucky teachers has become a perennial question for the General Assembly, with legislation to accomplish it offered at every regular session since 1956. At the 1972 Extraordinary Session the House of Representatives adopted House Resolution No. 25, in which it directed the Legislative Research Commission to study this question and present its findings prior to the 1974 General Assembly. This report represents the fulfillment of that obligation.

The commission wishes to extend its sincere appreciation to Mr. Charles L. Bratton, Kentucky Teachers Retirement System, for his invaluable assistance in the gathering of information herein presented.

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The Capitol
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FINDINGS IN BRIEF

1. Coverage under Social Security improves the retirement benefits.
2. Coverage under Social Security improves disability and death benefits.
3. Social Security benefits are tax-free in their entirety, while KTRS benefits are excludable only to extent of members' contributions.
4. Cost-of-living increases under Social Security will help keep retirement benefits in line with the rise of inflation.
5. Teachers should be given the opportunity to vote in a referendum to choose whether or not they desire Social Security coverage.
6. The General Assembly should appropriate the necessary funds to get back on schedule for funding the prior service obligation.
7. Early retirement without reduction in benefits should not be granted unless properly funded.
8. A new method of paying the employer's share to KTRS should be developed.
9. The disparity of benefits between teachers and other state employees should be corrected.
10. A study committee should be established by the General Assembly to look into the total retirement situation for teachers and recommend alterations.

I. INTRODUCTION

Kentucky's public school teachers are the only government employees in Kentucky who, by state law, are forbidden to participate in the federal Social Security system. Instead, the teachers and the state contribute jointly, on a 50-50 basis, to the Kentucky Teachers' Retirement System.

Social Security coverage for Kentucky's public school teachers has long been a question of study and debate. The controversy dates back to 1954 when Congress passed enabling legislation that extended Social Security coverage to state and local government employees already under a retirement system. Today a surprisingly large number of public employees in state and local government are not covered under Social Security. A majority of these non-covered employees are public school teachers.

Today Social Security is an accepted part of American life. The basic design of the Social Security program is to provide coverage to the entire working population. Since 1972, amendments to the Social Security Act have raised benefits by 25.6 percent. Frequent changes by Congress make it about impossible for public employees' retirement systems to keep abreast of Social Security coverage and benefits.

As recent trends in the retirement area continue toward retirement with full benefits at relatively young ages, it is time to review the retirement situation for Kentucky's teachers. It has been a great dis-service to teachers that major reform has not been set in motion to relieve the disparity of state support to teachers' retirement as compared to other state employees. Teachers are paying more for their public retirement than other state employees and do not have the additional benefit of Social Security coverage.

Although every taxpayer financially supports the retirement of public employees, most people have a primitive understanding of the basic features of any retirement program. This study attempts to present the structure of the retirement system for teachers and the problems currently facing the Teachers' Retirement System of the State of Kentucky. The Social Security system is briefly explained, as are the retirement systems for other state employees. This report makes no specific recommendations with regard to merger of the Teachers' Retirement System with the Kentucky Employees' Retirement System, as has been suggested in past debate. However, it does recommend that teachers be given an opportunity to vote, on an individual school district basis, whether or not they desire the additional coverage available under Social Security.

The complexities of any retirement system argues for great reticence when making major changes. Before any concrete changes are made to a retirement system, the services of an actuary must be employed to insure the financial soundness of the system. Therefore, this study does not attempt to recommend solutions but endeavors to point out the inequities in retirement for teachers of the State of Kentucky.

II. KENTUCKY TEACHERS' RETIREMENT SYSTEM

The Teachers' Retirement System of Kentucky (KTRS) provides retirement benefits, death and survivor benefits, medical payments, and disability benefits to Kentucky's public school teachers. The system was established by the General Assembly in 1938¹ but no funds were appropriated until 1940.² KTRS is an independent statutory state agency which functions under the authority of KRS 161.110 - 710.

The administration of KTRS is the responsibility of a Board of Trustees that consists of the Superintendent of Public Instruction, the Attorney General, the State Treasurer, and six other trustees elected as provided for in KRS 161.260. Four of the elective trustees are members of KTRS, one is a "lay trustee" who is not involved in the teaching profession, and one is a retired teacher who is receiving benefits from KTRS.

The trustees are responsible for investing the funds of the retirement system. To carry out this function, the trustees annually appoint an investment committee of two board members and the executive secretary. The investment committee employs an experienced investment counselor to advise on investments. The investment committee reports its recommendations to the full board. All investments must have the full board's approval. Investment categories and portfolio limitations are stated in KRS 161.430.

Once every two years an actuarial valuation is made of the retirement system to insure that adequate funds will be available to meet future obligations. KTRS is an actuarial reserve, joint contributory system. Contributions are made by members of the system and the state which contributes the employer share. Members currently contribute 7 percent of gross salary which includes 1/2 of 1 percent to finance death, survivors' and medical benefits programs. Local Boards of Education deduct the contributions from the salaries of covered employees and forward it to the retirement office. The state matches the members' contributions on a biennial basis by appropriation. For 1973-74, this appropriation totals \$29,354,630.

A distinctive feature of KTRS, in contrast to the situation in many other states and one that has caused various problems, is that the entire fiscal burden of the employer's contribution is placed upon the state. In many states the local Boards of Education pay the employer's share. In Kentucky, however, local school districts are not required to contribute to the retirement system. As a result, raises are sometimes granted within the local school systems, with

little or no consideration given to their impact on KTRS. In 1966, for example, local school districts received a tax windfall and increased teacher salaries. In as much as KTRS did not anticipate this salary increase, it took three years to equalize the state's contribution.³ The employer's contribution to KTRS is a fringe benefit and needs to be considered when salaries are raised.

Membership

Membership in KTRS is comprised of full-time regular or special teachers, principals, supervisors, superintendents, assistant superintendents, librarians, attendance officers, and other full-time members of the teaching and professional staff for whom certification is required as a condition of employment. KTRS also includes the instructional and administrative staffs of Eastern Kentucky University, Western Kentucky University, Murray State University, Morehead State University, Kentucky State University, Kentucky School for the Deaf, Kentucky School for the Blind, and staff members of state and area vocational schools who are regularly employed by a board of education, board of regents, or board of trustees for a full term. In 1956, teachers in the five state universities also were brought into the federal Social Security system.

Professional members of the University of Kentucky, University of Louisville and Northern Kentucky State College belong to Teachers Insurance and Annuity Association and its companion program College Retirement Equities Fund (TIAA/CREF).

The Superintendent of Public Instruction, division heads, and other professional staff members of the State Department of Education belong to KTRS. Non-professional employees of the State Department of Education are covered by the Kentucky Employees Retirement System and also have Social Security coverage. Professional employees of the State Department of Education have had several opportunities to join the Kentucky Employees Retirement System and thereby gain Social Security coverage, but have remained with KTRS. Former members of KTRS entering employment covered by another Kentucky public retirement system may elect to remain in KTRS.

A member who withdraws from service before his benefits are vested is entitled to a refund of his accumulated contributions plus interest, currently at the rate of 3 percent. KTRS members become vested after five years of Kentucky service, although benefits are deferred until the normal retirement age of 60. Teachers who have fewer than five years' service and are absent from service for more than six years are automatically withdrawn from membership. A member who has completed five years' service may leave his deposits with the system. In 1972 there were 48,211 active members' accounts on file at KTRS.

Creditable Service

As provided by the original legislation, prior-service credit to a maximum of 30 years is provided for teaching service performed in Kentucky before July 1, 1941. Prior service benefit is determined by multiplying \$40 times each year of service before July 1, 1941. Prior service benefits are financed by special legislative appropriation more or less on a "pay-as-you-go" basis. The problems involved are discussed later in this chapter.

A member of KTRS who has served in the Armed Forces of the United States may receive service credit for up to six years upon payment by the member of his contributions plus interest. Credited military service is considered as Kentucky teaching service except for vesting or disability retirement.

Teaching in foreign dependent schools is creditable toward the member's account if the member was granted a leave of absence by his local board of education. Credit is allowed for up to three years' leave in a ten-year period and the member must pay contributions plus interest to receive credit.

If a teacher has taught under contract in a public school in another state he may purchase out-of-state service credit. The service may not be used to meet the service requirement for retirement but is considered in determining the amount of the teacher's annuity. Up to eight years' credit is allowed for out-of-state service. No out-of-state service, in which the teacher has a vested interest and will be receiving a benefit from another state retirement system, may be used for credit in KTRS.

Members may make voluntary investments of 2 percent or more of their annual salaries to the retirement system. Voluntary contributions may be made by two plans - "tax-sheltered contributions" or "after-tax contributions". These contributions are not matched by the state. The Board of Trustees annually establishes a rate of interest to be credited to these accounts. Accounts of participating members are kept separate from their regular accounts.

Retirement Options

Normal retirement is at age 60. Members may retire at an earlier age at a reduced benefit. A member must retire on the July 1 following the attainment of the age of 70, regardless of length of service.

Upon retirement, a member of KTRS must choose the one of seven plans that best serves his needs, the amount of the monthly benefit being affected by the option that he chooses. Once a member selects a retirement plan and begins

receiving benefits, the plan cannot be changed. Most teachers choose Option I - Straight Life Annuity with Refundable Balance. Before selecting any option it is advisable for the retiring teacher to have a complete medical examination. Age and physical health play an important role in selecting the proper plan.

Option I - Straight Life Annuity with Refundable Balance

This option is the basic retirement plan and provides the largest monthly benefit. The formula for figuring the Straight Life Annuity with Refundable Balance is the basic retirement formula and adjustments are made from the result to figure optional retirement plans. The following steps are the process for determining the annuity:

Step 1. Average Salary - Add the five highest years of salary and divide by five to determine the five year average salary.

Step 2. Prior Service - If there is any service that was earned prior to July 1, 1941, total it and multiply by \$40.

Step 3. Contributing Service - Total all years of service after July 1, 1941 and multiply the total by the average salary (Step 1) and then multiply times 2 percent.

Step 4. Straight Life Annuity - Total the results of Steps 2 and 3 to find the yearly Straight Life Annuity.

Step 5. Monthly Benefit - Divide the yearly annuity by 12 to find the monthly benefit.

If the teacher should die before receiving monthly benefits equal to his account, the balance is refunded to his estate. This particular option is designed for teachers who have no dependents to support after death.

Option II - Ten Years Certain and Life Thereafter

Under this option the benefit is slightly reduced to guarantee that it will be paid for ten years, whether to the teacher or a chosen beneficiary in the event of death. If the teacher survives the ten-year period he alone will continue to receive this benefit for life. This option is of particular value to retirees whose health is such that a short life expectancy is likely and who want to insure that a guaranteed amount will be paid.

Option III - Joint and Last Survivor Annuity

This option provides a guaranteed benefit for the full lives of two individuals. The actuarial calculation includes the age and sex of the individuals to formulate the benefit. The option provides a benefit as long as either individual is alive. This option is particularly valuable to retirees who have a pension that will cease at death of the recipient. There is a special "pop up" - (IIIa) option that allows the member to return to the Straight Life Annuity plan if the beneficiary should die first.

Option IV - Joint and Last Survivor Annuity, One-Half Benefit to Survivor

This option provides a reduced lifetime annuity for the teacher as long as the retiree lives and 50 percent of the annuity to a designated beneficiary. As in Option III there is a "pop-up" provision that provides an increase to the Option I level if the beneficiary should die first. This option benefits the teacher who has good life insurance coverage. It provides the teacher a guaranteed annuity for his lifetime and aids his beneficiary after his death.

Option V - Special Benefit Plans

In rare instances when none of the above options fits the particular need of the retired teacher, Option V can be designed to provide for some other form of payment of retirement benefits. All such plans must be approved by the Board of Trustees.

Survivor benefits and payments to beneficiaries under one of the option plans are not to be confused. Survivor benefits apply only to active members of the retirement system. If the retiring teacher wants to provide for a beneficiary, he must select the plan that best fits his needs.

When a teacher retires from service his annuity is guaranteed for life. Any other employment will have no effect on his annuity except positions covered by KTRS. A retired teacher may work as a substitute teacher only an equivalent of 75 days in any one school year.

A retiring teacher is entitled to receive an annual allowance totaling not less than \$60 times his total years of service. Since the retirement annuity is figured on total years of service and average high salary there is no maximum limit on the amount of the benefit.

Death Benefit

Upon the death of an active or retired member of KTRS a \$2,000 death benefit is paid to his estate. If the death of a retired teacher occurs before his account has been totally paid out and if he is under Option I - Straight Life Annuity, any portion remaining (including interest to the date of retirement) will go to his beneficiary. Active teachers are also covered by the \$2,000 death benefit, payable in addition to any other benefits.

Annual Increases

Retirement benefits increase 1 percent on July 1 of each year. The intent of this provision was to help the retired teacher offset the impact of inflation. Unfortunately inflation has been rising at a greater rate. To help remedy this situation, the 1972 General Assembly enacted cost-of-living bonus payments to retired teachers in each year of the 1972-74 biennium.⁴ These bonus payments are equal to 5 percent of the annual benefit, not to exceed \$240.

Medical Insurance Plan

Retired teachers age 60 and over and those teachers retired by reason of disability are automatically covered by a medical insurance plan. Spouses and minor children are also covered. KTRS contracts with the Aetna Life Insurance Company to provide this program. The medical insurance plan is financed by an allocation of one-fourth of one percent of the active members' salaries which are matched by the state.

The medical insurance program covers most medical expenses. Coverage is provided on an 80-20 basis. There is no deductible applying against hospital costs, but there is a \$25 per calendar year deductible for non-hospital costs. Members who are eligible for either Part A or Part B under Medicare are not covered for any cost that would be paid by these programs.

Death and Survivor Benefits

Upon the death of an active contributing member or a member retired due to disability, the deceased member's accumulated contributions are paid to the estate or beneficiary. It is also possible for the eligible survivors to receive a survivor's benefit in lieu of the accumulated contributions. One-quarter of one percent of the active member's compensation is deposited in a separate benefit fund to finance the death and survivor benefits program. This fund is matched by an equal contribution from the state.

In order for the members' beneficiaries to qualify for survivor benefits the member must have been in active, contributing service in the year preceding his death. A guaranteed annuity is then payable to the eligible beneficiaries. The annuity is the actuarial equivalent of the benefits payable to the member if he had retired on the day before his death.

Persons eligible for survivor benefits are widows, dependent widowers, minor unmarried children under 18, (age 19 if still in high school or age 23 if a full-time student in a recognized educational program beyond the high school level), handicapped adult children, incompetent or physically handicapped, dependent parents, or dependent brothers or sisters. These persons qualify in the order named and Table 1 shows the schedule of monthly survivor benefit payments.

Only four children are eligible to receive payment. Payments continue as long as there are children who are eligible. A child's benefit terminates when he marries. Remarriage by a widow or widower cancels their benefit but does not affect the children's benefit.

If a teacher dies without leaving a widow or widower, minor children, or a physically or mentally handicapped adult child, his parents, brothers and sisters may qualify for survivor benefits, if they are dependent and have been receiving one half or more of their support from the deceased teacher.

Disability Retirement

Disability retirement is available to all active teachers who have ten years of Kentucky service and have at least one year of service preceding retirement. The member must be younger than 60 and must show medical evidence that he is physically or mentally disabled, and that the condition causing the disability may reasonably be expected to continue for one year or more beyond the date of application.⁵

The disability allowance is one half of the last annual compensation. The monthly benefit is determined by dividing the annual benefit by twelve. Minimum credit is five years if the teacher has met the ten-year service requirement. Members earn one year of entitlement to disability retirement for each four years of service beyond the ten year requirement.

During the period of disability the member continues to earn credit toward his service even though he is not paying his contribution.

If a member uses up his period of entitlement and remains disabled he then will be entitled to service retirement. His benefit is recalculated and

TABLE 1
SCHEDULE OF MONTHLY SURVIVOR BENEFIT
PAYMENTS UNDER K. T. R. S.

1. Widow or Dependent Widower	\$150
2. One Child	125
3. Two Children	225
4. Three Children	275
5. Four Children	300
6. Handicapped Adult Child	150
7. One Dependent Parent	150
8. Two Dependent Parents	200
9. Dependent Brother or Sister	125

TABLE 2

SCHEDULE OF TEACHERS' RETIREMENT BENEFIT PAYMENTS

Earnings Data	Last Annual Salary - \$7,000			Last Annual Salary \$9,500		
	Average Salary (5 highest years)	20 years	30 years	Average Salary (5 highest years)	20 years	30 years
Service Credit						
Member retires at age 60 or older(1)	\$55	\$220(3)	\$330(3)	\$75	\$150(4)	\$300(4)
Member disabled under age 60	Not Eligible	292	292	Not Eligible	396	396
Surviving Widow (2)	150	150	150	150	150	150
Surviving Widow and one Minor Child(2)	275	275	275	275	275	275
Surviving Widow and two Monor Children (2)	375	375	375	375	375	375
One Surviving Child(2)	125	125	125	125	125	125

(1) Benefit amounts assume a Straight Life Annuity. Please note that other options are available.

(2) To qualify for survivor benefits, member must be disabled or classified as an active contributor at the time of death. Upon death of an active member who was otherwise eligible to retire, the spouse or legal dependent of said member, if named as beneficiary, may elect an annuity that is actuarially equivalent to the annuity that would have been paid to the member had he retired on the day preceding his death in lieu of the benefits listed above.

(3) If any service years are prior to 1941, reduce monthly benefit by \$8 for each such year.

(4) If any service years are prior to 1941, reduce monthly benefit by \$12 for each such year.

Note: In addition to the above benefits, each members designated beneficiary is entitled to a lump sum death benefit of \$2,000 at the time of the members death.

includes the service credited to him while he was receiving disability benefits. The benefit is calculated as of age 60 if the member is under that age.

KTRS members receiving disability benefits may not continue to teach. If the member works at any other job during his disability retirement his income cannot exceed one-half of his salary at time of retirement or \$3,500 whichever is the larger sum.

If a KTRS member dies while on disability retirement his beneficiaries may receive survivors benefits in lieu of a cash refund.

KTRS annuities are exempt from Kentucky income tax. Income from annuities must be reported to the U. S. Internal Revenue Service, and federal income taxes apply after the retired teacher has received an amount in benefits equal to his total contributions.

Recent Improvements

Among the numerous statutory changes made to KTRS in the last ten years, designed to increase the retirement allowance, are the following:

- (1) The minimum service for retirement after age 60 was reduced from 20 years to 10 years, and most recently to 5 years;
- (2) The formula for calculating retirement benefits for service since 1941 was increased from 1 1/2 percent to 2 percent per year;
- (3) The allowance for service prior to 1941 was increased from 1 percent of the \$2,000 of average salary to a flat sum of \$40 for each year of such service;
- (4) The minimum retirement benefit was increased from \$25 per year of service to \$40 per year of service, to \$45 per year of service, and finally in 1972 to \$60 times the years of service;
- (5) The normal retirement age was reduced from 70 years to 65 years, and then to 60 years, (normal retirement after 30 years of service or at age 60 was enacted in 1970 but has not been funded);

- (6) Increases were made in the maximum annuity from 50 percent of average salary to 75 percent, and finally the maximum limits were completely removed;
- (7) The definition of "average salary" was changed from "highest five consecutive years" to "highest five years";
- (8) Differentials in retirement annuities due to sex were removed from Option I;
- (9) The lump sum death benefit was increased from \$500 to \$1,000 and then to \$2,000;
- (10) Regular monthly benefits were offered to survivors in lieu of a refund of the member's contributions;
- (11) All limitations on a widow's outside income were removed;
- (12) Survivor benefits were made possible from the date of the member's entry into the retirement system, rather than after a minimum of three years' service;
- (13) All survivor benefits were increased;
- (14) The qualification for disability benefits was reduced from 20 to 10 years;
- (15) The maximum outside income for disability retirees was increased;
- (16) The period of service required for vesting was reduced from 20 years, to 15 years, to 10 years, and finally to 5 years;
- (17) Military service was recognized as creditable service;
- (18) A tax-sheltered annuities program was established;
- (19) "Pop-up" provisions were added to retirement Options III and IV, which would restore the retirement annuity to the level of Option I if the beneficiary dies before the member;

- (20) Changes made in the minimum retirement allowance were made applicable to those members already retired;
- (21) Comprehensive medical insurance was provided for all retired teachers over age 60 along with their spouses and eligible dependents, and to all disability retirees regardless of age;
- (22) Automatic one percent cost-of-living annuity increases were provided and the monthly retirement allowance of each teacher retired as of July 1, 1970 was increased in the amount of \$2 times the number of years which have elapsed since the effective date of the members' retirement and July 1, 1970 with a maximum of 20 years; and
- (23) Cost-of-living supplement payments amounting to 5 percent of the annual benefit not to exceed \$240 are to be paid in each year of the 1972-74 bienium.⁶

Actuarial Valuation

In 1971, the actuarial firm of Huggin & Company, Inc. completed the mandatory actuarial valuation of KTRS as of July 1, 1970. The problems which face KTRS in future years are pointed out in this valuation. It reveals that the retirement system is actuarially sound assuming that the total payroll continues to expand through salary and membership gains and that the state begins to make adequate annual provisions for funding the prior service liability.

KTRS was found to have a deficiency of \$279,964,848 in addition to an unfunded prior service liability of \$50,931,597. Benefit liberalizations since July 1, 1968, and rates of salary increases in excess of those assumed in calculating liabilities have contributed to the \$279,964,848 deficiency.⁷

The actuarial valuation recommends that no further benefit liberalizations be made due to (1) history of local boards of education increasing individual salaries, (2) the lack of payment by the state of required amounts toward the prior service liability, (3) the increasing deficiency, and (4) the small amount of assets.⁸ The current assets, as of July 1, 1970, are insufficient to cover the liabilities for refunds to present members of their own contributions with interest and for future benefit payments to present annuitants, thus leaving no assets available for present members. The actuarial report describes the situation in another way -

if the system had terminated as of July 1, 1970, the assets would not have been sufficient to both return the personal funds, including interest, paid in by the presently non-retired teachers and provide the remaining lifetime annuities to present annuitants. Thus, if the System had ceased operations on July 1, 1970, not one cent of State funds would have been available for any teacher who had not yet retired. A period of stability should enable the State to rebuild the assets so that active as well as retired members will have some funds on hand to undergird the liabilities for their accrued benefits.⁹

It seems clear that no benefit liberalizations should be considered until the assets are rebuilt unless properly planned and funded by the General Assembly.

The report further recommends that the state should resume direct appropriations in the full amount required as soon as possible in order to reduce the unfunded liability for prior service.¹⁰ As of July 1, 1970 the deficiency in the amount of \$50,931,597 represented the unfunded portion of prior service benefits. In 1960, KRS 161.550 was enacted to provide for supplemental appropriations by the state to discharge this prior service obligation with interest over a period of thirty years. In order to fund the prior service obligation over the 16 years remaining, it is estimated that would take \$3.5 million per year.¹¹

The use of federal revenue-sharing funds would be an excellent way to amortize this liability since the prior service obligation is not a recurring expense. Failure of the General Assembly to appropriate money which would enable KTRS to properly fund the prior service obligation could jeopardize its actuarial soundness.

Early Retirement Plan

Another problem confronting KTRS is the prospect that the Legislature will authorize teachers to retire after 30 years' service with full benefits without providing the appropriation necessary to finance the proposal.

The 1964 General Assembly authorized teachers to retire earlier than age 60, if they had 30 years' service, but with benefits actuarially reduced. The idea of early retirement without a reduction in benefits originated during the 1970 General Assembly. HB 52 was introduced which allowed full benefits to be paid after 30 years' of service regardless of age. The bill raised the contribution rate for members to 7 3/4 percent. Even though there was no other provision for funding other than the raised contribution rate, HB 52 passed and the effective date was set at July 1, 1972.¹²

HB 52 was set into motion and developed without any participation of KTRS. No long-range study was made to show the impact that the 30-year retirement plan without reduction in benefits would have on the actuarial soundness of the retirement system. KTRS did not implement the plan because of insufficient funding. During the 1972 General Assembly the law was returned to its original form of providing reduced benefits for early retirement.

KTRS estimates that the cost of funding the 30-year retirement provision without reduction in benefits, should it become effective July 1, 1974, would be approximately \$2,898,000 for 1974-75. This figure represents a projected 6 percent annual increase in teachers' salaries for the next biennium. The cost for funding the provision during 1975-76 would be \$3,072,000.¹³

The General Assembly, if it again enacts the full-benefit 30-year retirement provision, should make certain that it provides the necessary funding, else the financial soundness of KTRS could be endangered.

The most visible long-term objective facing KTRS is to find another means of obtaining employer contributions. Unlike the Kentucky Retirement Systems, KTRS receives the employer's share by direct appropriation of the General Assembly. The Kentucky Employees' Retirement System receives employer contributions from the employing department, commission, or agency. Since any retirement plan is a fringe benefit of employment, it seems logical that the true employer, in this case the local boards of education, should be responsible for the employer's share to KTRS.

However logical it may seem to place the entire burden of paying the employer's share on local boards of education, it may not be practical because of several factors. The local boards of education are limited in their ability to raise tax rates due to the rollback law of 1965. Funds for teachers retirement would still have to come from the state due to the frozen tax base and the inability of the local school boards to raise the necessary funds. The complexities of the Minimum Foundation Program would complicate the allocation of state funds to the local school boards to pay for teacher retirement. Study and development of a new method of meeting the employer's share to KTRS would seem to be a desirable goal.

III. RETIREMENT SYSTEMS FOR TEACHERS

Today more than a third of all state and local employees in the United States are not covered by Social Security. A major portion of these employees are public school teachers. Every state has established some form of a statewide retirement system in which teachers participate. Some states have constructed retirement systems for teachers to include Social Security. Others have not. There are four general types of retirement systems to which teachers are members: (See Table 3.)

- (1) State Teachers' Retirement System without Social Security;
- (2) State Teachers' Retirement System with Social Security;
- (3) Public Employees' Retirement System without Social Security; and
- (4) Public Employees' Retirement System with Social Security.

There are also at present, 25 local teachers' retirement systems in 18 states and the District of Columbia.¹ Some cities had established local systems long before the statewide systems were created. After the implementation of statewide systems many of the local systems were abandoned.

Statewide teachers' retirement systems usually limit membership to certified public school teachers, school administrators, and professional staff of the State Department of Education. Some states have allowed membership to teachers in public colleges and universities and to teachers working in special schools administered by the state.

Retirement funds for teachers had their origin in 1869 with formation of protective associations to provide aid and relief to former teachers. Initially, voluntary contributions were made by members of the teaching profession to retired teachers. Soon, however, these contributions proved inadequate and public funds were obtained. At first the pension plans were financed totally by the employer but gradually grew into the joint contributory system that is most frequently in use today. All public school teachers in the Nation have been covered under some form of a teachers' retirement system since 1946. Since 1954, when Congress amended the Social Security Act to extend coverage to state and local

TABLE 3

RETIREMENT SYSTEMS TO WHICH TEACHERS BELONG

	State-wide Teachers Systems		State-wide Public Employees Systems to which Teachers are Members	
	With Social Security	Without Social Security	With Social Security	Without Social Security
Alabama	*			
Alaska		*		
Arizona			*	
Arkansas	*			
California		*		
Colorado				*
Connecticut		*		
Delaware			*	
Florida			*	
Georgia	*			
Hawaii			*	
Idaho			*	
Illinois		*		
Indiana	*			
Iowa			*	
Kansas			*	
Kentucky		*		
Louisiana		*		
Maine				*
Maryland	*			
Massachusetts		*		
Michigan	*			
Minnesota	*			
Mississippi			*	
Missouri		*		
Montana	*			
Nebraska	*			
Nevada				*
New Hampshire			*	
New Jersey	*			
New Mexico	*			
New York	*			
North Carolina			*	
North Dakota	*			
Ohio		*		
Oklahoma	*			

TABLE 3 (Continued)

	State-wide Teachers Systems		State-wide Public Employees Systems to which Teachers are Members	
	With Social Security	Without Social Security	With Social Security	Without Social Security
Oregon			*	
Pennsylvania	*			
Rhode Island				*
South Carolina			*	
South Dakota	*			
Tennessee	*			
Texas	*			
Utah			*	
Vermont	*			
Virginia			*	
Washington	*			
West Virginia	*			
Wisconsin	*			
Wyoming			*	
Totals	23	9	15	4

Source: Derived from information found in National Education Association, Teacher Retirement Systems - A Summary of the 1971 Legal Provisions for Retirement to which Teachers Belong, 1972.

government employees who were already under a retirement system, 40 states have elected to have Social Security coverage for some or all of their employees.

Administration and Structure

Established and regulated by state law, teachers' retirement systems generally are administered under a board of trustees. Participation by teachers is mandatory. The main objective of a teachers' retirement plan is to provide benefits to replace former earnings.²

State retirement systems operate according to a savings plan, whereby reserves are accumulated to meet liabilities as they are incurred. Funds for a pension plan come from three sources: (1) contributions from members of the system; (2) contributions from employers; and (3) income on reserves held in trust to pay allowances. State systems receive a substantial income from earnings on investment of reserves.

In all but three states, benefits are financed jointly by the employee and the employer.³ The employer contributes total funding, partial funding or no funding. New York was the first state in which the public employee systems went from contributory to non-contributory bases. Under this system the employer pays the whole cost of the pension system. The employee contribution is 7 percent or more in 12 systems; from 5 percent through 6 percent in 22 systems; and from no contributions to 5 percent in the remaining systems.⁴

Retirement Benefits

Normal retirement benefits vary among the different statewide retirement systems. Some systems provide a pension, some an annuity, and some both a pension and an annuity. Contributions, by both employer and employee, made in the teacher's name are used to purchase an annuity. A variable annuity is similar except the amount of the annuity payments is dependent on the income earned by the invested contributions.

To compute a retirement benefit under an annuity-type system a fixed percent is applied to the teacher's final average salary and then multiplied by the number of years the teacher was in the retirement system. The fixed percent formula plan exists in 43 states and the trend is toward a fixed formula percent approaching 2 percent.⁵ Assuming a 2 percent formula, a final average salary of \$7,444 and 30 years' service, the benefit would be figured; 2 percent of \$7,444 x 30 years of service = \$4,440 per annum. The monthly retirement benefit would be \$370.

Since 1967 all but eleven states have changed their benefit formulas to provide greater benefits to members. Improvements in benefit formulas generally result in the need for higher contributions.

Benefits from state systems without Social Security coverage are generally higher than benefits in systems with Social Security coverage. However, when Social Security is supplemental to the retirement benefit, the total benefit from both exceeds the benefits from non-Social Security systems. The substantial Social Security increases made in 1972, and the outlook for future increases suggest that the philosophy of supplementing Social Security to the retirement system might be altered. This evidence indicates that statewide retirement systems might well be restructured around the basic Social Security program.

Unlike state retirement systems, Social Security does not have to accumulate large reserve funds to meet future financial commitments. The benefits paid today's retired are being financed largely by the contributions of today's work force. The financial soundness of the Social Security program depends primarily on the government's effective power of taxation.⁶

As Social Security benefits have increased, benefits under non-Social Security systems have been increased in an attempt to keep in line with the Social Security program. This situation is particularly unique in states where not all state employees are covered by Social Security. Statewide retirement systems will have difficulty keeping pace with the automatic increases in benefits scheduled to rise with the cost of living that are written into the Social Security Act. Keeping up with the future increases in the Social Security program can put quite a strain on a retirement system not using a pay-as-you-go method. It would be difficult for state legislatures to appropriate the funds necessary to keep up with Social Security benefits.

Presently 31 state retirement systems provide an adjustment in the benefit to allow for cost-of-living increases.⁷ Flat increases based on gains resulting from investments are provided in three systems. The most desirable solution, provided in 18 systems, is to fully gear the amount of the benefit adjustment to a price index such as the Consumer Price Index.

A comparison of contributions made by neighboring and southern states indicates that Kentucky, as employer, contributes the least amount to the teacher retirement system and ranks last, with Louisiana, in amount contributed by the teacher. It is interesting to note that several of the southern states pay the employer's contribution to Social Security through the local school board. Kentucky along with Illinois, Louisiana, Ohio, and Missouri does not have Social Security for teachers. There are 8 other states in the United States that do not have coverage for teachers.⁸ (See Table 4.)

TABLE 4

CONTRIBUTIONS TO TEACHER RETIREMENT MADE BY SOUTHERN AND NEIGHBORING STATES

	State's Contribution			Teacher's Contribution		
	Retirement System	F. I. C. A.	Total	Retirement System	F. I. C. A.	Total
Alabama	4.68%	5.85%	10.53%	4%	5.85%	9.85%
Arkansas	\$11,900 per year	5.85% (paid by local school district)		4%	5.85%	9.85%
Florida	Equal amount to the total of its member's contributions	5.85%		4%	5.85%	9.85%
Georgia*	7.65% (paid by state and local employer)	5.85%	13.5%	6%	5.85%	11.85%
Illinois	Matching contribution			8%		8%
Indiana	Normal contribution to amortize the accrued liability within 50 years (\$20,000,000 for 1971-72)	5.85%		3% to a maximum of \$8,500	5.85%	8.85%
Kentucky	7% (Approx.)		7%	7%		7%
Louisiana	8% (plus 1/2 of 1% of the taxes collectible by sheriffs)		8%	7%		7%

TABLE 4 (Continued)

	State's Contribution			Teacher's Contribution		
	Retirement System	F. I. C. A.	Total	Retirement System	F. I. C. A.	Total
Mississippi	4.5%	5.85% (paid by local school district)	10.35%	4.5% on earnings up to \$35,000	5.85%	10.35%
Missouri	8% (paid by local school district)		8%	8%		8%
North Carolina	8.95%	5.85%	14.8%	5% to \$5,600 6% to excess of \$5,600	5.85%	10.85% Minimum
Ohio	12.9%		12.9%	7.8%		7.8%
South Carolina	7.5%	5.85%	13.35%	4% to \$4,800 6% in excess of \$4,800	5.85%	9.85% Minimum
Tennessee*	3% on salaries under Social Security wage base 5% over wage base	5.85%	8.85% Minimum	same as state's contribution	5.85%	8.85% Minimum
Virginia	5.40%	5.85%	11.25%	5.5%	5.85%	11.35%
West Virginia	6% (paid by county school district)	5.85%	11.85%	6%	5.85%	11.85%

* Denotes states that obtained Social Security by the divisional method.

Source: National Education Association, Teacher Retirement Systems - A Summary of the 1971 Legal Provisions for Retirement to Which Teachers Belong, 1972.

Vesting

Vesting refers to the right of the teacher to the accrued contributions made in his behalf. When vesting occurs the teacher has earned a deferred retirement allowance. A deferred retirement allowance guarantees the teacher a benefit upon reaching retirement age. Eighteen states provide vesting rights with five years or less service; 15 states within 6 to 10 years service; 6 states in 15 years; 9 states in 20 years; and 2 states have an age and service provision.⁹ After vesting occurs the teacher is assured of receiving a benefit upon retirement.

Creditable Service

Credit allowed for out-of-state service is recognized in 25 states. In most cases the teacher pays for the credit.¹⁰ Many states are increasing the number of years of teaching that are creditable. To receive credit the teacher must compensate the system for past contributions plus interest for the years creditable. Military service credit is available in every state system but in many different forms.

Death and Survivor Benefits

Every state retirement system that involves teachers makes some provision for death and survivor benefits. The benefits are generally in lieu of a refund of the deceased member's accumulated contributions. In the states that are covered by Social Security, there is a tendency to rely on that coverage for a major portion of disability and survivor benefits. Retirement benefits are much greater due to the de-emphasis of disability and survivor benefits. Some states are studying the possibility of voluntary insurance for added survivor benefits.

Early Retirement

Recently pressure groups have been compelling retirement systems to consider early retirement provisions. In the last five years there has been a downward trend in age and the number of years service required for retirement. A substantial number of public employees, such as policemen and firefighters, are in hazardous occupations where age is a factor in the ability to perform the occupation. It would not be a serious problem to retirement systems if only hazardous positions were offered early retirement opportunities. The New York Permanent Commission on Public Employee Pension and Retirement Systems, however, found that when one employee group is granted more liberal benefits

because of the risk inherent in the profession, other groups - not subject to the same risks - nevertheless demand and have been granted the same or similar benefits.¹¹

It is quite likely that an employee who retires at age 55 could find other employment and end up with three retirement benefits - his public employee's benefit, Social Security, and one from his most recent employer. If the employee is successful in finding employment at age 55, his retirement benefits at age 65 could equal his salary at retirement while in the labor force. In such situations early retirement provisions cause the employee to lose sight of the basic concept of retirement.

The cost of providing early retirement also must be considered. Many employees would be retiring earlier and benefits paid over a longer period of time. Adequate funding needs to be provided to allow the retirement system to recover the contributions that previously would have been paid had the member remained active for an additional 7 to 10 years. A long-range study would seem to be essential before any state adopts such an adjustment to its retirement system. Any consideration of early retirement provisions must be properly financed.

Consolidation of Retirement Systems

Current legislative action involving public employee retirement systems has been directed toward consolidation. Various existing retirement systems for teachers have been merged with the statewide public employees' system to eliminate duplication within state agencies. Three southern states have recently initiated such a change. Maryland reorganized all the public employees' retirement plans and placed the systems under the Department of Personnel. The merger was done mainly for administrative purposes.

The Florida Retirement System was established December 1, 1970. The new system created a statewide public employees' retirement system which, with respect to teachers, virtually replaced the Florida Teachers' Retirement System. Individual teachers were given the option of electing to remain in the Teachers' Retirement System. Membership in the Teachers' Retirement System has been sharply reduced by the creation of the new system. No further new membership in the Teachers' Retirement System is possible as it is compulsory for all new employees to become members of the Florida Retirement System. The Teachers' Retirement System has no Social Security coverage for its members. The Florida Retirement System provides mandatory Social Security coverage for its members. Teachers electing to join the Florida Retirement System pay a smaller contribution to the state system than they would pay as members of the Teachers' Retirement System.

As of July 1, 1972 Tennessee created the Tennessee Consolidated Retirement System that brought together under one board of trustees all the public employees' retirement systems in Tennessee. Employed teachers, prior to July 1, 1972, were allowed to remain covered by the benefits and contribution provisions of the superseded Teachers' Retirement System. The teachers also had the option, within 90 days of the establishment, to join the Tennessee Consolidated Retirement System. Any teacher who begins service after July 1, 1972 becomes a member of the new retirement system as a condition of employment. Teachers are covered by Social Security in both systems.

IV. BASIC PROVISIONS OF SOCIAL SECURITY

Social Security, broadly defined, covers a number of programs which have the basic objective of keeping families and individuals from becoming destitute due to the loss of earnings. Though the Social Security System is complex and few workers understand its provisions, it has become a major factor in meeting the contingencies of life for nine out of ten Americans.¹

Even though the Social Security Act is federal law, the United States Government operates only the national social insurance program, commonly referred to as OASDHI (old-age, survivors, disability, and health insurance). Unemployment insurance and public assistance are part of the Social Security Act but are administered by the states with federal cooperation. However, for the purposes of this study we will be concerned only with the OASDHI program.

OASDHI provides monthly cash benefits when earnings are cut off by old-age, severe disability or death, and provides protection against hospital and medical costs. Contrary to popular opinion, Social Security is not just an old-age pension but a basic national social insurance program. Payments made under the OASDHI program are known as "Social Security benefits."

The Social Security Act was signed into law August 14, 1935. Born during the Depression, the original planners attempted to solve the problem of achieving economic security in the face of risks to earned income and total loss of lifetime savings due to old age, disability, and premature death of the family head.² Since the Depression, the Social Security program has been marked by expansion, improvements and wide-spread public acceptance. Congress has often revised benefit schedules, tax rates, and medical benefits to keep OASDHI up to date.

OASDHI is financed by an earnings tax (F. I. C. A. deduction) which is levied on covered workers, with matching contributions by employer. The self-employed also pay an earnings tax at a higher rate. Social Security is a pay-as-you-go system. The tax contribution paid today is then paid out to beneficiaries and the balance is invested. The payroll taxes levied on current earnings of workers finance benefit payments based on past earnings of insured workers. Eligibility for OASDHI benefit grows out of work in covered employment.

Social Security taxes are deposited in the four following accounts: (1) Federal Old-Age and Survivors Insurance Trust Fund; (2) Federal Disability

Insurance Trust Fund; (3) Federal Hospital Insurance Trust Fund; and (4) Federal Supplementary Medical Insurance Trust Fund which consists of collected premiums and funds appropriated from the general revenue fund to cover the federal government's matching share.

Changes in the name of the tax reflect the growth of benefits. From 1937 to 1955 the tax was known as OASI - Old-age and Survivors Insurance. Disability insurance was added in 1956 and the name changed to OASDI. Since 1966 when health insurance (Medicare) was introduced it has been known as OASDHI. As the benefits were improved the portion of the worker's covered wage which goes for the tax has also been increased. Initially a one percent contribution by the employee and the employer was levied on salaries up to \$3,000 a year. The law has always placed an annual limit on the amount of earnings subject to the tax and which count toward Social Security benefits. If the worker earns more than this amount, he does not pay the tax on his total yearly salary but only on the limited portion, called a wage base. In 1973 the tax rate is 5.85 percent on a wage base of \$10,800 for both employer and employee. The wage base will rise to \$12,600 in 1974.

Monthly retirement benefits are payable at age 65, or at age 62 at a reduced amount, to the wife or dependent husband of a retired worker. Retirement benefits are also payable to: (1) the wife of a covered worker at any age if she has in her care a child under 18; (2) an unmarried child under age 18 or from age 18 to 22 if he is a full-time student; and (3) a child, regardless of age, who has been continuously disabled since before age 18. Payments also can be made in certain situations to a worker's divorced wife. The amount of the monthly retirement benefit for the worker and his dependents is based on the average earnings of the worker under Social Security over a period of years. Under the provisions of the Equal Rights Amendment Social Security benefits now provided only to widows of covered male workers would be extended to widowers of covered women workers. The formula used to compute a benefit for a woman at age 62 would be the same for a man retiring at age 62. Normally a male would receive reduced benefits at any age before 65. This inequity in the Social Security Act is to be corrected by a bill currently before Congress.

Insured workers who choose to receive early retirement benefits at age 62 for men and age 60 for women, receive a reduced amount of the Primary Insurance Amount. Actually, workers who retire at an early age will collect about the same value in total benefits, but in smaller installments to compensate for the longer period during which the benefits are likely to be paid.

To receive full retirement benefits the worker must be fully insured. Having a fully insured status means only that certain kinds of cash benefits may be payable; it does not determine the amount of the benefits which is based on average earnings. The period of time a worker must have spent in a covered occupation to be fully insured for benefits is measured in three-month units of work called "quarters of coverage." Over the years, changes have been made in the amount of work required to obtain a fully insured status. Currently no one is fully insured with credit for less than 1 1/2 years of work and no one needs more than 10 years of work to be fully insured.³

The exact amount of the worker's benefit cannot be figured until the worker applies for Social Security benefits. Monthly earnings are averaged between ages 22 to 65 beginning with 1951. The five years of lowest earnings are thrown out when computing the average. When the worker's average monthly covered earnings not exceeding the wage base have been figured, the monthly amount payable at age 65 (the Primary Insurance Amount or PIA) is then obtained from a table in the law. Workers whose contributions are modest but enough to qualify are awarded a minimum benefit. Benefits for dependents and survivors are calculated as a percentage of the worker's PIA.

Legislation in July 1972 increased most Social Security benefits by 20 percent. The reserves in the Social Security funds were so large that this could be accomplished. No general revenues were used to pay for this increase. Currently the average monthly check for a retired worker is \$156 and the average monthly check for a retired couple is \$271.⁴ (Table 5 reflects the changes made to Social Security benefits).

Recently Congress enacted across-the-board increases in Social Security benefits. Effective with benefit checks to be received July 3, 1974 benefits will be raised by 5.6 percent. The taxable wage base that was scheduled to rise to \$12,000 in 1974 was increased to \$12,600. The increase in the wage base raises the maximum tax on employers and employees in 1974 from \$702 to \$738. The new legislation does not increase the rate of the Social Security payroll tax.

Social Security not only provides income at retirement, but also gives families survivor protection. A fact not always recognized. Survivor benefits are available to the following dependents: (1) Unmarried children under 18, or between 18 and 22 if they are full-time students; (2) unmarried children 18 or over who were severely disabled before they reached 18; (3) widows, regardless of age, who are caring for a child under 18 or any disabled child; (4) widows 50 or older (or dependent widowers 50 or older) who becomes disabled not later than 7 years after the end of their entitlement to benefits as a widow with a child; (5) a dependent husbands or widowers 62 or over; (6) dependent parents 62 or over after a working child dies; and (7) surviving divorced wives in certain situations.

TABLE 5

SCHEDULE OF SOCIAL SECURITY PAYMENTS

Average yearly earnings after 1950*	\$923 or less	\$3,000	\$4,200	\$5,400	\$6,600	\$7,800	\$9,000
Retired worker 65 or older	\$ 84.50	\$174.80	\$213.30	\$250.60	\$288.40	\$331.00	\$354.50
Disabled worker under 65							
Wife 65 or older	42.30	87.40	106.70	125.30	144.20	165.50	177.30
Retired worker at 62	67.60	139.90	170.70	200.50	230.80	264.80	283.60
Wife at 62, no child	31.80	65.60	80.10	94.00	108.20	124.20	133.00
Widow at 60	73.30	125.10	152.60	179.30	206.30	236.70	253.50
Widow or widower at 62	84.50	144.30	176.00	206.80	238.00	273.10	292.50
Disabled widow at 50	51.30	87.50	106.80	125.50	144.30	165.60	177.30
Wife under 65 and one child	42.30	92.50	157.40	217.30	233.90	248.30	265.90
Widowed mother and one child	126.80	262.20	320.00	376.60	432.60	496.60	531.80
Widowed mother and two children	126.80	267.30	370.70	467.90	522.30	579.30	620.40
One child of retired or disabled worker	42.30	87.40	106.70	125.30	144.20	165.50	177.30
One surviving child	84.50	131.10	160.00	188.00	216.30	248.30	265.90
Maximum family payment	126.80	267.30	370.70	467.90	522.30	579.30	620.40

*Generally, average earnings covered by social security are figured from 1951 until the worker reaches retirement age, becomes disabled, or dies. The maximum benefit for a retired worker in 1972 is \$259.40 a month, based on average

yearly earnings of \$5,652. The higher benefits shown in the chart, based on average earnings shown in the columns on the right, generally will not be payable until later.

Source: Social Security Administration. Higher Social Security Payments, 1972.

Note: This table does not reflect the 5.6 percent increase in benefits that becomes effective with benefit checks paid on July 3, 1974.

Unlike regular life insurance, survivor insurance is not a fixed sum. The benefits are figured as a percentage of the Primary Insurance Amount of the worker. Survivor benefits may be paid to each child until he reaches 18, marries, or reaches 22 if he stays in school. When the child stops receiving benefits, the mother does also, but at age 60 she can begin drawing a widow's pension which will continue for the rest of her life. The value of survivor benefits can total more than \$100,000 for a worker's family.

A lump-sum death payment may be paid to a widow or widower who was living in the same household with the insured worker at the time of the worker's death. This lump-sum death payment is equivalent to three times the Primary Insurance Amount with a \$255 maximum.

Disability insurance is widely misunderstood. Disability, for the purposes of entitlement to monthly benefits, is defined as "inability to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months."⁵ A disability benefit is not paid to a worker because he is sick, or injured; it is paid to him because his earnings have stopped. Once it has been determined that the worker is disabled and meets all requirements he waits four months before he will receive his first check. This is to insure that the disability is apparent and allows time for the worker to recover and return to work. The amount of time it takes to become eligible for disability benefits depends on how old he is and when he became disabled. The amount of the worker's monthly disability payment is generally the same as he would receive in retirement benefits at age 65.

The health insurance program, commonly known as Medicare, provides comprehensive health insurance protection to the aged. After years of controversy, Medicare was incorporated into the Social Security Amendments of 1965. All people 65 and over are eligible for Medicare.

Medicare provides two separate kinds of protection: (1) hospital insurance that covers inpatient hospital care and certain follow-up care, and (2) voluntary medical insurance that covers physicians' services and certain other medical services and supplies. One half of the money necessary to support the voluntary medical insurance comes from premiums paid by people who choose to sign up and the other half is paid by the federal government. The portion paid by the government comes from general revenues. The current monthly premium for the voluntary medical insurance is \$5.80; it is scheduled to rise to \$6.30 in July 1973.

The Secretary of Health, Education and Welfare contracts with non-profit and private insurance companies to handle the payment of Medicare benefits.

Major changes in Medicare came about in 1972 in the Social Security reform bill. Coverage was then extended to some people under 65 who are disabled. Treatment for sufferers of chronic kidney disease who need either dialysis with kidney machines or transplants is now covered by Medicare. This provision is a step toward federal coverage of the costs of catastrophic illnesses for everyone in the United States. Also people who first become entitled to Medicare coverage in July 1973 or later will automatically be covered by the medical insurance plan unless they refuse the coverage.

The problem of benefits depreciating in value due to inflation has always been serious. Changes in the Social Security program voted by Congress in 1972 tied Social Security benefits to cost-of-living increases. In future years, benefits are scheduled to rise automatically when consumer prices increase substantially. This "escalator clause" is intended to guarantee workers that inflation will not seriously erode the value of their benefits. Social Security benefits are not subject to federal income tax or to the state income tax in Kentucky.

After two years of debate and serious study Congress passed the significant public health and welfare bill, HR 1, that caused sweeping changes in the Social Security system. Included in the Social Security package are more liberalized benefits for widows, the disabled, and those who work after retirement. All these changes mean more than \$5 billion in increased benefits. To pay for the new benefits Congress approved an increase in payroll taxes for 1973 from 5.65 percent to 5.85 percent. A worker in 1973 making the wage base \$10,800 a year or higher will pay \$631.80 in payroll taxes; \$163.80 more than the \$468 he paid in 1972.

Under the new amendments some workers who previously would have been receiving minimal benefits may draw more in retirement than they had paid during their working years. A departure from the original concept of Social Security guarantees a minimum pension of \$170 to any worker who has worked for 30 years or more in a covered position no matter what he paid into the system.

The Social Security Act is full of special rules that apply to certain situations. To find out how the new amendments affect particular workers one should call the local Social Security office.

While OASDHI is no substitute for private investments and private retirement funds, it does provide assurance of a modest income and protection at a lower cost than can be obtained any other way. In January 1970, about 106 million people were insured by OASDHI for cash benefits. Through the years the system has experienced numerous growing pains but now it seems that Social Security coverage will keep getting better.

With the exception of federal employees,⁷ and some state and local government employees, virtually all gainfully employed workers in the United States are now covered by OASDHI.⁸ Amendments in 1950 to the Social Security Act allowed elective coverage by state and local government employees not under a retirement system. In 1951, an Extraordinary Session of the Kentucky General Assembly was called to enact legislation establishing Social Security eligibility for Kentucky state and local government employees. Congress further amended the Social Security Act in 1954 to allow coverage to state and local government employees (except firemen and policemen) already under a retirement system.

Most types of employment in the United States are covered by Social Security. Some work is specifically excluded by the law, and other types of work are covered only under certain conditions. Employees of state and local governments can be brought under federal Social Security only by means of voluntary agreements entered into by the state with the Secretary of Health, Education and Welfare. Once an agreement has been entered into with a particular state, employees of the state are brought under the agreement in groups known as "coverage groups."⁹ The federal law gives each state the right to decide which coverage groups are to be included under its agreement and may modify the agreement to include additional coverage groups.¹⁰

Coverage of employment by state and local governments was not made compulsory due to the constitutional questions involved.¹¹ There is some question whether the federal government has the power to levy a tax on the governmental functions of states and localities.

Presently three-fifths of all full-time state and local employees are covered by both OASDHI and a state and local retirement system.¹²

V. SOCIAL SECURITY AND THE TEACHER

History

Currently more than 90 percent of American workers are covered by Social Security. However, among American public school teachers only 60 percent are covered.¹ Many arguments have prevented public school teachers in Kentucky from obtaining coverage. At the state level, education administrators and state professional organizations have long feared that Social Security would weaken the already established KTRS. As a result, for many years they produced studies and newspaper interviews showing how Social Security would be a "bad buy" for the teaching profession. On the local level, Boards of Education have opposed Social Security for teachers due to the cost factor. School boards do not have to pay the employer's matching share of KTRS; the state pays it all with a direct appropriation. In spite of this opposition, many school boards employ their superintendents as secretary to the board, a position covered under Social Security. The superintendent thus is covered under the Kentucky Teachers' Retirement System for his salary as superintendent; he also is covered under Social Security for his salary as secretary, and is eligible for benefits from both systems. At the national level, the National Education Association, at times, has been very vocal in its opposition to Social Security. However, in 1972 NEA was lobbying for Medicare coverage to be made available to the 40 percent of teachers who are not covered by Social Security. Many teachers, it seems, have not always been fully informed of the benefits offered by Social Security coverage.

A joint committee composed of representatives of the State Department of Education and the Kentucky Education Association prepared a study in 1954 which concluded that Social Security was not in the best interests of Kentucky's public school teachers.² The committee's conclusions were that KTRS should be strengthened by (1) adding survivor benefits equal to those available under Social Security, (2) adding a provision for a death benefit and (3) providing disability benefits after ten years of service. They also suggested raising the benefits of the older members who otherwise would derive little from other improvements in the system.

In 1958 the Legislative Research Commission recommended retention of KTRS with the addition of survivor benefits. The LRC study found that a plan to bring teachers under coverage of Social Security would cost the state \$19,050,186 the first two years. The provision for adding survivor benefits would cost \$12,723,687 for first two years.³ The addition of survivor benefits

was approved. The other areas studied were: (1) merger of the KTRS into the Kentucky Employees' Retirement System; and (2) preserving the existing KTRS with contributions for the teachers on the same basis as in the Kentucky Employees' Retirement System. The high cost of implementing the addition of Social Security Security and the other plans erased the likelihood of consideration by the General Assembly.

Perennially, legislation has been introduced at each regular session of the General Assembly since 1956 that would enable teachers to obtain Social Security coverage. Two major efforts from organized teachers occurred in the 1960's. During the 1962 Regular Session a bill allowing teachers to vote on whether they wanted to be covered by Social Security in addition to KTRS passed the House but died in the Senate. At that time officials of KTRS asserted that Social Security would only benefit 10 percent of the teachers and the estimated cost would be \$3,200,000.⁴

Teachers from Jefferson County organized in 1966 and formed the Louisville Professional Teacher's Association. A bill was introduced in their behalf that would have made teachers in school systems in counties containing first and second class cities eligible to participate in Social Security. Again, the idea proved too costly for serious consideration and the bill was tabled.

Method to Obtain Coverage

State law now expressly excludes members of KTRS from coverage under the Social Security system. If teachers are to be covered under the federal program, a first step would be to amend the various sections of KRS Chapter 61 to remove this exclusion.

After amending KRS Chapter 61, Social Security coverage could be extended to teachers in any or all of the 189 local school districts under provisions of KRS 61.435, which requires:

- (1) Each local board of education to request the governor to authorize a referendum vote among its teachers, as required under provisions of the federal Social Security Act.
- (2) The opportunity to vote in the referendum must be given to all persons who occupy positions covered by KTRS in the local school district requesting the referendum on the date the notice of referendum is held.

(3) Voting in secret on written ballots.

(4) Notice of the vote to be given at least 90 days before the vote is taken.

If a majority of all persons eligible to vote is in the affirmative, all teachers would qualify for Social Security coverage, provided the local school board also agreed to pay the employer's share of the Social Security tax.

It is important to note that under existing law, each of the 189 local school systems is deemed to have a separate retirement system, insofar as the referendum provisions are concerned. Kentucky law provides no means whereby all members of KTRS can simultaneously vote in a single referendum to gain Social Security coverage.

The Social Security amendments of 1954 also allowed coverage by the divisional method. To obtain Social Security coverage by the divisional method, after amending KRS Chapter 61, it would be necessary to request Congress to amend the Social Security Act to permit Kentucky to be included among the states that are allowed to divide their retirement coverage.⁶ The General Assembly would make this request in the form of a concurrent resolution. The local school districts would then petition the governor in the same manner previously outlined.

Divisional method coverage is granted on an individual basis. Only those teachers voting in favor of Social Security coverage would qualify for coverage. In the event that a teacher who gains coverage by the divisional method changes positions to a school district without Social Security coverage he would still obtain his coverage as it is transferable. Those teachers voting against coverage would not be required to be covered as in the other method. Social Security would be mandatory for all new teachers in the school districts adopting Social Security by the divisional method.

Currently there is a bill in Congress that would allow public school teachers (and other public school employees) who do not have coverage pursuant to state agreement under OASDHI to elect coverage as self-employed individuals.⁷ Under provisions of this bill the individual teacher would file a certificate verifying that he elects to have OASDHI system extended to service performed by him as a teacher. This bill would allow the teacher to make his own decision and take the responsibility from the states that do not have OASDHI coverage for teachers.

Benefit Payments - General Facts

Since there are many variables in the Social Security program it is difficult to estimate individual benefits. As with any other pension plan, the benefits from Social Security vary among individuals. Benefits are figured on the amount of the average earnings of the teacher. Other factors influencing the benefit are age, marital status and number of dependents.

It is possible to make some general statements concerning teachers and how the coverage would benefit certain age groups. Older teachers would receive the greatest benefit from added Social Security coverage. They still must fulfill their required quarters of coverage to be fully insured but would have to pay less in contributions than the younger teachers to receive comparable benefits.

Since Social Security can be said to favor families, individual protection is rather limited. Many argue that Social Security discriminates against the single teacher. The unmarried teacher, widows, and widowers with no children under 18 contribute at the same rate as the married teacher with dependents but receive only the primary benefit. The married teacher, in contrast, is eligible for primary benefits for himself and secondary benefits for his wife and children. According to NEA and KEA statistics, 19.2 percent of all male teachers are single, widowed or divorced; and 25.7 percent of female teachers fall in this category.⁸

There are also cases where both the husband and wife teach. Both teachers would pay the full tax but the benefits would only be 33 percent greater than if just one were covered. The benefits to the children would be the same as if only one parent were covered.

Many teachers are already covered by Social Security through a previous job or their spouse's coverage. In the 1955 study conducted by the State Department of Education and the Kentucky Education Association a sample survey of Kentucky public school teachers showed that 67.8 percent of the teachers had some form of Social Security coverage.⁹

Social Security is most definitely a "family plan." Unfortunately for the young teacher, the tax payment due now is all that he can see and feel most clearly; retirement seems so far in the future and the prospect of a pension has little meaning. If a young teacher with a family is disabled or dies at an early age, his survivors would draw benefits far in excess of his tax contribution. Social Security is clearly a better bargain for those teachers with dependents than those without.

The Social Security death and survivor benefits are excellent from the standpoint of cost. Robert J. Myers, the Social Security Administration actuary, states that today's average young worker will contribute 80 to 85 percent of the total value of his benefit protection and the new worker just entering the labor force could not possibly buy a private annuity that would pay as much as his expected Social Security benefits.¹⁰

Under Social Security certain savings accrue that reduce the cost of OASDHI coverage. There is a broad diffusion of risk among its more than 106 million heterogeneous participants, as compared with a very homogeneous group of teachers.¹¹ There are no refunds of contributions made to workers who never qualify for payments and there is no compulsory retirement.

As important as Social Security can be to teachers it cannot do the entire job. A reasonably adequate state retirement plan must be provided. Social Security should be made supplemental to the teacher retirement system. In a recent study of the private pensions in the United States Ralph Nader stated that Social Security pays only about 1/3 of the amount the worker earns before he retires, but the Social Security supplementary benefit means the difference between a less than modest and a reasonably comfortable level of living.¹²

The survivor benefits under Social Security are excellent from the standpoint of cost. In the states that have Social Security coverage for teachers there is a strong tendency to rely on the Social Security program to handle the survivor benefits.¹³ KTRS survivor benefits are in lieu of a refund of the deceased member's accumulated contributions but are in addition to a generous additional death benefit.

As previously indicated, single teachers would be victims of a form of discrimination if all teachers were required to belong to a survivor benefit plan. The state retirement systems should not add to this discrimination by requiring single teachers to pay for coverage they do not need. The ideal situation would be for the state retirement system to provide a voluntary survivor plan thereby allowing teachers who need the coverage to obtain it without forcing the single teacher to pay for unwanted protection.

Social Security's greatest asset is that the quarters of coverage earned are portable. Social Security places no barrier on the teacher. He may move to another state or even change professions without losing his coverage. Unlike the teacher retirement system where the teacher's contributions must vest before he receives credit, his Social Security contributions move with him.

Social Security benefits are exempt from federal income taxes and Kentucky income taxes. Taxes must be paid on KTRS benefits in excess of the teacher's contributions.

Cost of Implementation

Based upon 1971-72 figures supplied by KTRS the 42,793 active members received total salaries of \$327,240,143; of the total members, approximately 39,924 made less than \$12,600 and 2,869 members made more than \$12,600--the Social Security wage base for 1974. If Social Security were to be adopted statewide in teacher referenda, the total projected aggregate cost to the employer would be \$18,698,459. This is a projected figure as it would be the maximum cost of implementing Social Security coverage for all Kentucky teachers. It also does not allow for new teachers since 1971-72 and teacher salary increases.

Under the divisional method only those teachers voting in favor of Social Security in the referendums with an affirmative vote would gain coverage. Teachers who elected not to have coverage would have the option to remain without Social Security coverage. All new teachers would automatically obtain coverage. The cost to the employer would be less as fewer teachers would be participating and total coverage would be gradual.

The state will be contributing \$21,000,000 for Social Security coverage for other state employees in 1973.¹⁴

The 1972-73 estimated average salary for all public school teachers is \$7,825.¹⁵ If Social Security coverage was provided the public school teacher's contribution, based on the estimated average salary, would be \$457 a year.

TABLE 6

PROJECTED COST OF ADDING OASDHI TO KTRS
 BASED UPON KTRS 1971-72 FIGURES

Member's Salaries

39,924 - Under \$12,600	\$283,482,394
<u>2,869 - Over \$12,600</u>	<u>43,757,749</u>
42,793 - Active members	

Total Wages Paid \$327,240,143

F.I.C.A. Contribution

Wages under \$12,600	
283,482,394 x 5.85%	\$ 16,583,720
36,149,400 x 5.85%*	<u>2,114,739</u>

Total of Employer's Contribution
 to F.I.C.A. \$ 18,698,459

* The total was derived by multiplying \$12,600 (the wage base for 1974) x 2,869 (the number of members making more then wage base) = 36,149,400.

VI. PUBLIC EMPLOYEES' RETIREMENT IN KENTUCKY

It is the responsibility of the Kentucky Retirement Systems to administer the Kentucky Employees' Retirement System,¹ the County Employees' Retirement System,² and the State Police Retirement System.³ Each system is a separate legal and financial entity but is administered by a single Board of Trustees headed by a General Manager. The nine-member board of trustees consists of one member elected by the membership of the County Employees' Retirement System, one member elected by the State Police Retirement System, two members elected by the Kentucky Employees' Retirement System, three members appointed by the Governor, and the Attorney General and the Commissioner of Personnel, who serve as ex-officio members.

The total active, inactive and retired membership of the combined systems was 55,546 as of June 30, 1972.⁴

The 1972 General Assembly passed House Bill 327 which increased Kentucky Retirement Systems' benefits substantially.⁵ The retirement benefits of the Kentucky Employees' Retirement System and the County Employees' Retirement System were increased 6 2/3 percent. The benefits of the State Police Retirement System were increased 7 1/2 percent. The benefit increases were financed one-half from improved investment performance of the three funds and one-half from an increase in the employer's contribution rate for the state and county retirement systems from 7 percent to 7 1/4 percent.⁶ The member contribution of the three systems is 4 percent.

Funds for the retirement systems are derived from three sources: member's contributions, employer contributions, and investment income. Unlike KTRS the employer contribution comes directly from the employing agency, department or commission.

Every year the retirement funds are audited by a certified public accountant. The actuary found in his 1971-72 valuation that the retirement systems have excellent financial strength and are able to pay adequate benefits without deferring the cost to future generations.⁷

Although the Kentucky Retirement Systems has sole authority to administer three different retirement systems, each system has maintained its separate philosophy. Each program has benefitted from a single investment structure. The trust funds of the three groups are kept separate.

TABLE 7

KERS-CERS MONTHLY NORMAL RETIREMENT BENEFITS (AGE 65)
Based on 1.6% Formula with Salary and Service as Indicated¹

Final Compensation	Annual Cost											
	Member 4%	State 7 1/4%	4 yrs.	8 yrs.	12 yrs.	16 yrs.	20 yrs.	24 yrs.	28 yrs.	32 yrs.	36 yrs.	40 yrs.
\$ 4,000	\$ 160	\$ 290	\$ 21	\$ 43	\$ 64	\$ 85	\$107	\$128	\$ 149	\$ 171	\$ 192	\$ 213
5,000	200	363	27	53	80	107	133	160	187	213	240	267
6,000	240	435	32	64	96	128	160	192	224	256	288	320
7,000	280	508	37	75	112	149	187	224	261	299	336	373
8,000	320	580	43	85	128	171	213	256	299	341	384	427
9,000	360	653	48	96	144	192	240	288	336	384	432	480
10,000	400	725	53	107	160	213	267	320	373	427	480	533
12,000	480	870	64	128	192	256	320	384	448	512	576	640
14,000	560	1,015	75	149	224	299	373	448	523	597	672	747
16,000	640	1,160	85	171	256	341	427	512	597	683	768	853
18,000	720	1,305	96	192	288	384	480	576	672	768	864	960
20,000	800	1,450	107	213	320	427	533	640	747	853	960	1,067
25,000	1,000	1,813	133	267	400	533	667	800	933	1,067	1,200	1,333
30,000	1,200	2,175	160	320	480	640	800	960	1,120	1,280	1,440	1,600

¹General Information County Employees Retirement System, Frankfort, Ky., October 15, 1972, p. 10.

The 1968 Kentucky Efficiency Task Force Report recommended the consolidation of administrative functions of the Kentucky Retirement Systems with KTRS. The study made by the Task Force found the nature of the work in both units to be essentially the same. Combining the administrative functions of the retirement systems would result in a savings of \$30,000 to \$40,000 per year in personnel and approximately \$20,000 in data processing equipment.⁸ Organizational charts of the two systems reprinted from the Task Force Report appear in Tables 8 and 9.

The Task Force recommendation pertains only to the administrative functions of the systems. The study stressed that the trust funds should not be merged and must be operated as separate entities. It is important to keep the trust funds separate because of the differences in schedules of contributions and benefits from each of the systems. Even if the administrative functions would be under one administrative officer the integrity of each system's trust fund would be maintained.

Comparison - The State's Contributions Toward Retirement Funds

In December 1972 the Research Division of the Kentucky Education Association prepared a study showing that benefits paid to other state employees are higher than benefits paid to the members of KTRS.⁹ This report compared case studies of benefits under the Kentucky Employees' Retirement System and KTRS and concluded that the combined benefits from the Kentucky Employees' Retirement System and Social Security are more favorable than KTRS benefits.

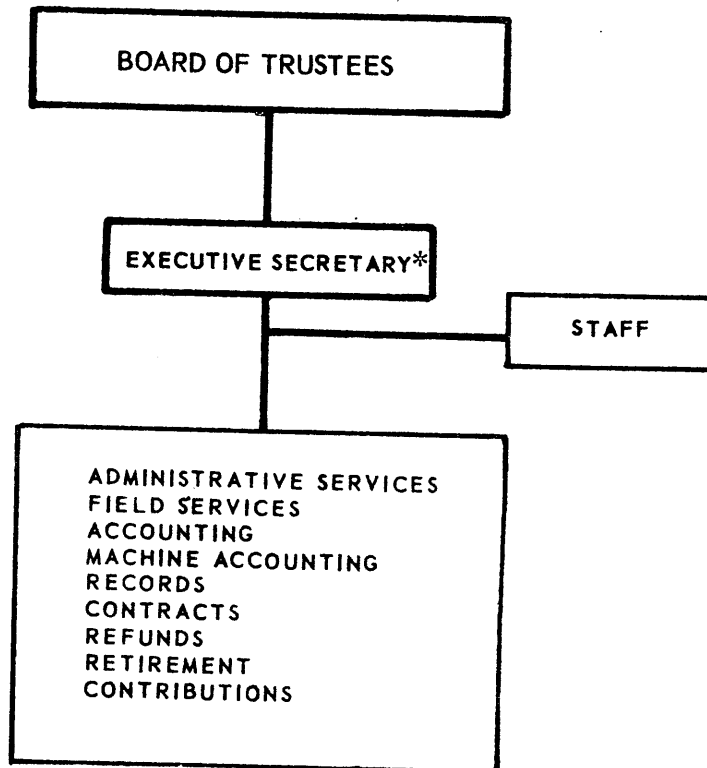
In this report a chart was prepared to show the wide gap between the state's contribution to KTRS and other retirement systems. This chart is reproduced and brought up to date to show the rate change of the F.I.C.A. contribution in Table 10.

The amount of funds paid toward retirement to KERS for public employees' retirement is approximately the same as the total appropriation made to match the member's contribution to KTRS. However, the percentage of contributions made by the state for public employees differs greatly as compared to the contribution made for teachers. To the Kentucky Employees' Retirement System the state contributes 7 1/4 percent of the total salary and pays 5.85 percent up to the Social Security wage base for a total of 13.10 percent of the state employee's salary. The inequity is also evident by comparing 12.85 percent that the state contributes to regional universities certified personnel and 15.85 percent to the certified personnel at the University of Kentucky, University of Louisville and Northern Kentucky State College. The state's contribution to KTRS is 7 percent. Since teachers are not eligible for Social

TABLE 8

STATE AND COUNTY EMPLOYEES' RETIREMENT SYSTEMS

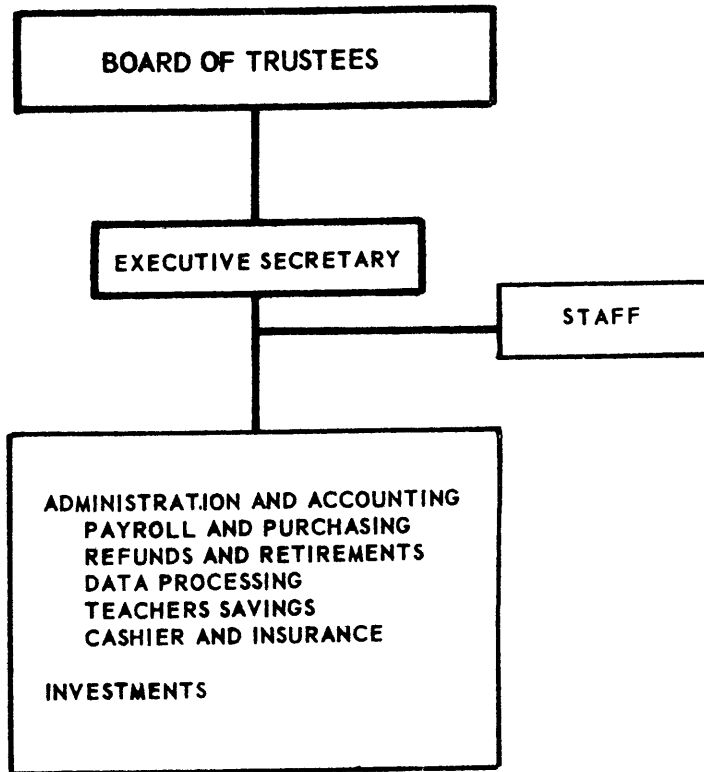
Kentucky Employees' Retirement System
County Employees' Retirement System
State Police Retirement System



Source: The Kentucky Efficiency Task Force, Report and Recommendations, 1968, (Frankfort, May 15, 1968), Exhibit 12.

* Effective 1973 the Executive Secretary is known as the General Manager.

TABLE 9
TEACHERS' RETIREMENT SYSTEM



Source: The Kentucky Efficiency Task Force, Report and Recommendations, 1968, (Frankfort, May 15, 1968), Exhibit 13.

TABLE 10

COMPARISON OF K. T. R. S. CONTRIBUTIONS
WITH THOSE OF OTHER STATE EMPLOYEES

Employer	Members	State	Members	State	Members	State
	Contribution to Retirement	Contribution to Retirement	Contribution to F. I. C. A.	Contribution to F. I. C. A.	Contribution to F. I. C. A.	Contribution to F. I. C. A.
	%	%	%	%	%	%
Local boards of education and State Department of Education	7%	7 %			7 %	7 %
State of Kentucky	4%	7.25%	5.85%	5.85%	9.85%	13.10%
Regional universities	7%	7 %	5.85%	5.85%	12.85%	12.85%
University of Kentucky, University of Louisville, and Northern Kentucky State College	5%	10 %	5.85%	5.85%	10.85%	15.85%

Security this means that the state contributes almost twice as much money to other public employees than to teachers. The state appropriates a sum every biennium to match the KTRS members' contributions.

In 1951 KRS Chapter 61 was created to provide Social Security coverage to the members of the Kentucky Employees' Retirement System. At that time Social Security only provided minimal benefits. Due to numerous amendments to the Social Security Act, Social Security has been made a comprehensive program for retirees, survivors, disability victims and provides a broad medical insurance plan. The state has twice amended KRS 61.430 to provide coverage for groups of state employees. All public employees in a retirement system except those covered in KRS Chapter 161 were granted coverage in 1962. With the exception of teachers, all Kentucky state retirement systems benefits are supplemented by Social Security.

The KEA report did not suggest providing Social Security coverage for teachers but supported finding a supplement for Social Security.

With the evidence that other state employees draw a larger proportion in employer contributions from the state, teachers should be given the opportunity to choose in a referendum held in each local school district whether or not they desire to add Social Security coverage.

VII. RECOMMENDATIONS

Much care must be exercised when making any major changes to a retirement system. Once an employee has acquired certain rights in a retirement system, those rights or benefits can never be taken away or reduced. If any benefit liberalizations made to a retirement system prove to be overly generous the only course of action would be to change the program with respect to future employees. All current employees would still profit from the liberalization.

Due to the highly technical structural organization of a retirement system much attention should be given to its financial soundness. Only an actuary can ascertain the effect of liberalizations and the future needs of a retirement system. Therefore, a professional study of a retirement system by a knowledgeable committee with the aid of an actuary should be used to formulate the essential modifications.

The 1974 General Assembly should establish a special committee to explore the entire retirement program for teachers. The membership of this special committee should include the Executive Director of the Teachers' Retirement System of the State of Kentucky; the General Manager of the Kentucky Retirement Systems; members of the General Assembly; representatives of the Kentucky Education Association, local boards of education, and the State Department of Education; and a representative of an actuarial firm. Funds must be appropriated by the General Assembly to employ an actuarial firm to aid the committee in making recommendations.

Areas that should be studied by this committee are:

--The desirability of local school boards of education requesting referendums to gain Social Security coverage.

--The state's role in helping local school districts finance the employer's contribution to Social Security.

--The feasibility of merging KTRS with the Kentucky Retirement Systems.

--The present teachers' retirement system to determine whether the state should go to an overmatching plan in contributions similar to KERS.

--The situation for older teachers who would not desire Social Security coverage.

--The formulation of the steps necessary to reorganize the teachers' retirement system if supplemented by Social Security coverage.

This committee should report its findings to the next regular session of the General Assembly.

FOOTNOTES

Chapter II

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8. Ibid.
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2. Ibid., p. 118.
3. Teachers' Retirement System of the State of Kentucky, "Overview of Retirement Provisions in State Teacher Retirement Systems, 1972, [1972], p. 3.
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7. Teachers' Retirement System of the State of Kentucky, "Overview," p. 1.
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6. "More Social Security: Tax You Pay, Aid You Get," U.S. News & World Report, Vol. LXXIII, No. 18, (October 30, 1972), p. 16.
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9. Social Security Handbook, p. 181.
10. Ibid., p. 182.
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12. Ibid., p. 13.

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1. Day, p. 15.
2. Kentucky State Department of Education and Kentucky Education Association, Teacher Retirement & Social Security, [Louisville: KEA, 1955], p. 2.
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4. "Sublett Lists Arguments Against Social Security For Kentucky's Teacher", The Courier-Journal, (January 28, 1962).
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