KPERS Update
Overview, Governor’s Budget Proposal and Triennial Experience Study

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Kansas State University Support Staff Senate
February 8, 2017
Kansas Public Employees Retirement System

Dependable Benefits. Trusted Partner.

KPERS is a fiduciary providing retirement, disability and survivor benefits to our members and their beneficiaries with a 98-member staff.

KPERS administers three statewide, defined benefit plans for public employees.

• Kansas Public Employees Retirement System
• Kansas Police and Firemen's Retirement System
• Kansas Retirement System for Judges

KPERS partners with more than 1,500 state and local government employers.

• State of Kansas
• 286 school districts
• 105 counties
• 425 cities and townships
• Other employers include libraries, hospitals, community colleges and conservation districts
## KPERS Overview

### Board of Trustees

<table>
<thead>
<tr>
<th>Position</th>
<th>Name</th>
<th>Location</th>
<th>Appointment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chairperson</td>
<td>Lois Cox, CFA, CFP</td>
<td>Manhattan</td>
<td>Manhattan - Appointed by Governor</td>
</tr>
<tr>
<td>Vice-Chairperson</td>
<td>Kelly Arnold</td>
<td>Wichita</td>
<td>Wichita - Appointed by the Governor</td>
</tr>
<tr>
<td>Ernie Claudel</td>
<td>Olathe Retired teacher</td>
<td>Olathe</td>
<td>Elected - school</td>
</tr>
<tr>
<td>Shawn Creger</td>
<td>Prairie Village Financial Advisor</td>
<td>Topeka</td>
<td>Elected - non-school</td>
</tr>
<tr>
<td>Ron Estes</td>
<td>Wichita Kansas State Treasurer</td>
<td>Elected member - statutory member</td>
<td></td>
</tr>
<tr>
<td>Todd Hart</td>
<td>Olathe Deputy Chief, Olathe Fire Department</td>
<td>Elected member - non-school</td>
<td></td>
</tr>
<tr>
<td>Suresh Ramamurthi</td>
<td>Topeka Chairman, CBW Bank</td>
<td>Appointed by the President of the Senate</td>
<td></td>
</tr>
<tr>
<td>Michael Rogers</td>
<td>Manhattan Certified Public Accountant</td>
<td>Appointed by the Governor</td>
<td></td>
</tr>
<tr>
<td>Vacant Position</td>
<td></td>
<td>Governor’s Appointment</td>
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KPERS Overview

How KPERS Works

• Legislature defines benefits and funding
  – Membership eligibility
  – Vesting
  – Employee and employer contributions
  – Benefit formula
  – Service credit
  – Retirement eligibility

• Actuary estimates how much benefits will cost

• Employers and members make contributions

• KPERS invests the money over time

• KPERS pays benefits with contributions + investment earnings - expenses

• KPERS is not like Social Security
  – Social Security utilizes contributions from current employees to pay the benefits of current retirees
  – KPERS benefits are “pre-funded”; current contributions are invested to pay benefits down the road
Investments

• 7.75% long-term return assumption

• Calendar year 2016 return through 9/30 totals 7.1%* (not annualized)

• Earned 9.3%* for the trailing 5-year period ending 11/30/2016

• Earned 8.4%* over the last 25 years as of 11/30/2016

*Gross total return for all assets as of 11/30/2016
KPERS Overview

KPERS Contributions

- KPERS Employees Contribute 6% of pay.
- KPERS Employer Contributions
  - % of pay set by annual actuarial valuation.
  - Statutory cap on annual rate increase.
  - State pays for state and school employees.
- Delayed FY 2016 State/School employer contributions totaling $97.5 million and $1.5 million interest for FY 2016 was counted as long-term receivable.
- $1.0 billion in bond proceeds received in August 2015.
- Total Contributions for FY 2016: **$2.1 billion**
KPERS Overview

KPERS Benefits

• Final average salary \( \times \) years of service \( \times \) multiplier (1.85\%)*

• Lifetime retirement benefit and $4,000 death benefit for beneficiary of retiree

• After about three years in retirement, most KPERS 1 retirees begin receiving more in total benefits than they paid in contributions (if no lump-sum option)

KPERS paid about $1.67 billion in total benefits in FY 2016 (retirement, death benefits, disability benefits, withdrawals)

<table>
<thead>
<tr>
<th>Average KPERS 1 member</th>
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<tbody>
<tr>
<td>Final average salary</td>
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<tr>
<td>Service</td>
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<tr>
<td>Benefit</td>
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<table>
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<th>Long-term KPERS 1 member</th>
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<tr>
<td>Final average salary</td>
</tr>
<tr>
<td>Service</td>
</tr>
<tr>
<td>Benefit</td>
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</tbody>
</table>

*KPERS 1 multiplier is 1.75\% for all service prior to 2014
KPERS Overview

Active Membership on 12/31/2015

Total: 152,175

<table>
<thead>
<tr>
<th></th>
<th>Average Age</th>
<th>Average Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>KPERS-State</td>
<td>46.9</td>
<td>12.4</td>
</tr>
<tr>
<td>KPERS-School</td>
<td>45.0</td>
<td>11.3</td>
</tr>
<tr>
<td>KPERS-Local</td>
<td>45.3</td>
<td>10.2</td>
</tr>
<tr>
<td>KP&amp;F</td>
<td>39.5</td>
<td>11.7</td>
</tr>
<tr>
<td>Judges</td>
<td>58.4</td>
<td>12.0</td>
</tr>
</tbody>
</table>
## KPERS Overview

Retired Membership on 12/31/2015

### Average Retired Members and Beneficiaries

<table>
<thead>
<tr>
<th></th>
<th>Average Age</th>
<th>Average Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>KPERS-State</td>
<td>72.4</td>
<td>$13,797</td>
</tr>
<tr>
<td>KPERS-School</td>
<td>72.1</td>
<td>$14,932</td>
</tr>
<tr>
<td>KPERS-Local</td>
<td>72.1</td>
<td>$11,357</td>
</tr>
<tr>
<td>KP&amp;F</td>
<td>65.1</td>
<td>$31,445</td>
</tr>
<tr>
<td>Judges</td>
<td>74.7</td>
<td>$40,192</td>
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Total: 93,866
2015 Actuarial Valuation

• Continued Improvement
• Funding Status
• Trust Fund Assets
Continued improvement

• Generally, KPERS’ funding improved on an actuarial basis during calendar year 2015

• Calendar year rate of return on the market value of assets was 0.2%, below the 8% return assumption

• Due to asset smoothing, the rate of return on the actuarial value of assets for the calendar year was 7.6%

• Proceeds from the sale of bonds are reflected in this valuation
As a system, KPERS’ funded ratio and unfunded actuarial liability improved in the most recent valuation.

<table>
<thead>
<tr>
<th></th>
<th>12/31/2015</th>
<th>12/31/2014</th>
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</thead>
<tbody>
<tr>
<td>Funded Ratio</td>
<td>67%</td>
<td>62%</td>
</tr>
<tr>
<td>Unfunded Actuarial Liability</td>
<td>$8.54 billion</td>
<td>$9.47 billion</td>
</tr>
</tbody>
</table>

Statutory employer contribution rate increases for State/School Group until it reaches the actuarial required contribution rate, which was projected to happen in FY 2020.
2015 Valuation

Trust Fund Assets

• KPERS Trust Fund has nearly $17 billion on a market value basis, the highest the Trust Fund has ever been.
  – Since the 12/31/2015 valuation, assets have risen above $17 billion.

• Current assets reflect receipt of $1 billion of bond proceeds received in August, 2015.
  – Split $143.4M to State and $856.6M to School.
  – Increased the State/School funded ratio (to 65% from 59% last year) and decreased the unfunded actuarial liability (to $6.3B from $7.2B last year).

• The actuarial value of assets exceeds the market value of assets, which indicates the deferred losses yet to be recognized.
2015 Valuation

Historical asset level

$ Millions


Calendar Year End

Market Value
Actuarial Value
Governor’s Recommended Funding

• No Repayment of FY 2016 Contribution Reduction

• Lower Employer Contributions

• Re-amortization

• Long term effects
Governor’s Recommendation

No repayment of FY 2016 contribution reduction

• $97 million in employer contributions was deferred during the 4th quarter of FY 2016.

• Current statute requires repayment of the contributions plus 8% annual interest by the end of FY 2018.

• The Governor’s recommendation eliminates the repayment.

• The result is $97 million in lost contributions and another $18 million in lost interest payments ($115 million total).
Governor’s Recommendation

Contribution reduction in FYs 2017, 2018 and 2019

- Governor’s recommendation freezes the FY 2016 contribution amount for FY 2017, FY 2018 and FY 2019.
  - The FY 2016 contribution amount was already reduced by nearly $100 million.
    - Equates to losing four quarters, or 1 full year, of contributions over a four-year period.
  - For those years, also suspends 1.2% annual rate increase established by 2012 KPERS reform legislation to address underfunding dating to 1993
    - Does not reflect changes in payroll.
- Reduces employer contributions to KPERS by $596 million over three years (including the $115 million lost due to not repaying the deferred FY 2016 contributions).
Governor’s Recommendation

Total reduction over three years

**Projected 3-Year Total of KPERS Employer Contributions**

*State/School Group*

- **Current Statutory Contributions**
- **Governor’s Recommended Contributions**

$1,746

$1,150

$596 million reduction over 3 years

FY 2017, FY 2018 and FY 2019 Total

*The State pays the entire KPERS-School employer contribution as part of state aid to local districts.

**Current statutory projection of employer contributions includes $115 in delayed FY 16 employer contributions plus interest scheduled to be paid in FY 2018.
## Employer Contributions

### Year by year reductions

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Current Statutory Contributions</th>
<th>Governor’s Recommended Contributions</th>
</tr>
</thead>
<tbody>
<tr>
<td>2017</td>
<td>$480.8 million</td>
<td>$97.5 million reduction</td>
</tr>
<tr>
<td>2018</td>
<td>$657.1 million</td>
<td>$273.8 million reduction</td>
</tr>
<tr>
<td>2019</td>
<td>$607.7 million</td>
<td>$224.4 million reduction</td>
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</tbody>
</table>

*The State pays the entire KPERS-School employer contribution as part of state aid to local districts.

**FY 2018 employer contributions include $542 million in employer contributions and $115 in delayed FY 16 employer contributions plus interest.
Governor’s Recommendation

Adding 10 years to the amortization schedule

• The current 40-year amortization schedule was set in 1993
• Existing unfunded actuarial liability is scheduled to be paid by 2033.
• The Governor’s recommendation is to extend the end date by 10 years to 2043.
• Extending the amortization lowers required annual employer contribution rates. However, extending the amortization –
  – Does not impact FY 2017, FY 2018 or FY 2019 State/School employer contribution rates
  – Results in rates of 12% to 13% for an additional 10 years
  – Increases the overall payments for the State/School unfunded liability by $6.5 billion through 2045.
  – Decelerates improvement in the funded ratio, leaving the KPERS State/School group vulnerable to market downturns for many years (in the “cautionary” 60% range through 2030, 8 years longer than current statute)
  – Increases the peak State/School unfunded actuarial liability by $1.3 billion. The unfunded actuarial liability would not be expected to return to 12/31/2015 levels for 20 years.
• By statute, the KPERS Board sets the amortization schedule.
• Legislation is required for the Governor’s recommendation to take effect.
Governor’s Recommendation

Funded ratio projection

Projected State/School Funded Ratio
With 10 Year Amortization Extension

- Funded ratio remains below 70% through 2030, eight years longer than under current statute.
- Funded ratio remains below 80% through 2036, eight years longer than under current statute.
Governor’s Recommendation

Unfunded actuarial liability

Projected State/School Unfunded Actuarial Liability

Governor’s recommendation projection peaks at $8.6 billion in 2023.

Governor’s recommendation projection doesn’t go below $7.3 billion until 2033.

Current projection peaks at $7.3 billion in 2019.
The current State/School statutory employer contribution rate for FY 2018 is 12.01%.

Freezing contributions at the FY 2016 contribution amount lowers the FY 2018 State/School statutory contribution rate to 7.88%, about a third less than current law.

Extending the amortization period reduces the actuarial required contribution rate to about 13%. However –

- After the 3-year freeze, the statutory rate is lower than the actuarial rate until FY 2024
- Actuarial contribution rates remain around 13% through FY 2044, rather than falling below 2% beginning in FY 2036

The total cost to pay off the unfunded liability is projected to increase by $6,500,000,000 over the next 30 years.
Governor’s Recommendation

Long-term effects

• Effect on Funding
  – The State/School’s employer contribution rate will eventually settle at around 13% through FY 2045.
    • Local employer contribution rates are not affected
  – KPERS’ funded ratio will stay in the 60% “cautionary” range for many more years.
  – The State/School unfunded actuarial liability is projected to peak at $8.6 billion, $1.3 billion higher than the peak unfunded actuarial liability under current law.
  – The reduced contributions being recommended affect the cash flow projection and will require a higher cash allocation to meet cash flow needs.

• Effect on Members
  – Current retirees (and those thinking about retiring) are not affected.
  – Employee contributions are not affected. They are fixed by statute.
• Review of actuarial assumptions
• Investment return assumption
• Amortization method
• Impact of changing assumptions
Experience Study

Review of actuarial assumptions

- KPERS actuary and Board of Trustees review the actuarial experience of the System every three years as required by law.

- The current review covered calendar years 2012 to 2015.

- All economic and demographic actuarial assumptions were reviewed, as well as actuarial methods and the amortization period.

- Changes to actuarial assumptions will first be reflected in the 12/31/2016 valuation, which will be used for FY 2020 State/School employer contribution rates.

  - The experience study does not change previously certified rates in FY 2017 through FY 2019 – the years in which the Governor’s budget proposal would freeze KPERS contributions.
Experience Study

Review of actuarial assumptions

• The Board has a **fiduciary responsibility** to set the actuarial assumptions using their best judgement in light of available information.

• The assumptions are long-term in nature and try to anticipate what will happen over decades, not react to short-term trends.

• Having accurate assumptions is important so that costs aren’t too high today or passed on to future generations.
Experience Study

Investment return assumption

• The current trend among public pension plans is lowering of investment return assumptions.

• For many years the median investment return assumption for public plans was 8%, but is now 7.5%.

• The actuarial inflation assumption, which is a component of the investment return assumption, was reduced from 3.00% to 2.75%.

• Based on the recommendation of KPERS’ investment and actuarial consultants and the current environment of public pension plans, the Board voted to lower the long-term investment return assumption from 8% to 7.75%.
Experience Study

Impact of changing assumptions

• The changes do not impact benefits for current retirees.
• The changes do not impact employee contributions.
• The changes do not impact State/School employer contribution rates for FY 2017, FY 2018 or FY 2019.
• The changes will increase employer contributions in the future (starting in FY 2020 for State/School employers).
  – The initial increase in the actuarial rate was projected to be less than 1.5%
• The estimated unfunded actuarial liability for the total System increases $565 million, or 6.6%.
• The estimated funded ratio for the total System decreases from 67.1% to 65.7%.
• The 12/31/2016 valuation will reflect both the changes in the actuarial assumptions and the actual experience (investments, demographics, etc.) and the results will differ from the estimates.
Personal Savings

Critical for a Sound Retirement

• Pension benefits are just one part of retirement income

• KPERS and Social Security may not be enough

• Personal savings is critical to cover the gap
Personal Savings

Deferred Compensation Savings Plan

• KPERS 457 is a voluntary savings plan administered by KPERS for state employees
  – $660 million in assets saved by 14,321 participants (as of 9/30/2016)

• KPERS 457 also can be adopted by local employers as a savings vehicles for their employees
  – Over 300 local employers offer the plan
  – Additional $291 million in assets saved by 9,327 local participants (as of 9/30/2016)

• Employees choose to enroll in the savings program

• Pre-tax and Roth after-tax contribution options
Personal Savings

KPERS 457 Can Help

• No cost for employers

• In its fiduciary role, KPERS oversees investment options, the service provider and participant education

• Competitive cost to employees

• Free, online investment advice

• Local, dedicated counselors representatives across the state for on-site individual and group meetings
Board Election
2017 Elections

• Two members of the Board of Trustees are elected by KPERS members
• Retired and active members can run for an elected board position
• Candidates had until the end of November 2016 to collect signatures and turn in forms
  – 2 School Group candidates accepted
  – 3 Non-school Group candidates accepted
• Members will vote in April 2017
Questions?