Division of the Budget
Landon State Office Building
900 SW Jackson Street, Room 504
Topeka, KS 66612

Kansas
Division of the Budget

Phone: (785) 296-2436
adam.c.proffitt@ks.gov
http://budget.kansas.gov

Adam C. Proffitt, Director

Laura Kelly, Governor

February 15, 2024

The Honorable Nick Hoheisel, Chairperson
House Committee on Financial Institutions and Pensions
300 SW 10th Avenue, Room 582-N
Topeka, Kansas 66612

Dear Representative Hoheisel:

SUBJECT: Fiscal Note for HB 2659 by Representative Essex, et al.

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2659 is respectfully submitted to your committee.

Under current law, there are three KPERS retirement tiers: KPERS Tier 1 (members who started before July 1, 2009), KPERS Tier 2 (members who started from July 1, 2009, to December 31, 2014), and KPERS Tier 3 (members who started after January 1, 2015). Each group has a different plan design.

KPERS Tier 1 and Tier 2 are traditional defined benefit plans that are currently closed to new members, where benefits are calculated using the following benefit formula—Years of Service X Final Average Salary X multiplier = annual retirement benefit. KPERS Tier 1 and Tier 2 members contribute 6.0 percent of salary and employers contribute an amount calculated by the actuary to fund the normal retirement costs and the unfunded actuarial liability, which is currently 11.42 percent in FY 2025 for State/School Group employers.

KPERS Tier 3 is a cash balance plan where a member’s lifetime benefit is based on contributions and interest earned throughout the member’s career. Members contribute 6.0 percent of salary to a notional account that earns a guaranteed 4.0 percent interest each year and a possible dividend interest credit based on statutory formula coupled to the five-year net average rate of return. Members also have an employer pay credit account that is credited 3.0 percent to 6.0 percent of pay each year based on the number of years of service they have. This account also earns the guaranteed 4.0 percent interest plus a possible dividend. However, employers contribute the same actuarial contribution rate for KPERS Tier 3 members as for KPERS 1 and KPERS 2 members. At retirement, the member’s account balances are converted to a lifetime annuity.

HB 2659 would reopen the currently closed KPERS Tier 2 plan to certain teachers who would become members on July 1, 2024. In addition, teachers who are currently Tier 3 members would convert to KPERS Tier 2 members by January 1, 2025. Teachers would be defined as "any professional employee who is required to hold a certificate to teach in any school district and any teacher or instructor in any technical college, community college or the institute of technology at Washburn university." In addition, the bill would provide that if a current KPERS Tier 3 member would receive a higher benefit with KPERS Tier 3 than with KPERS Tier 2, the member would keep the KPERS Tier 3 benefits.

KPERS reports that in reviewing data from the December 31, 2022 actuarial valuation, the agency estimates there were about 40,000 teacher positions employed in Unified School Districts in Kansas, with about 15,500 being KPERS Tier 3 members. This total does not include the positions that would be considered "teachers" under HB 2659 at the Community and Technical colleges. In addition, the bill would convert inactive teacher members to KPERS Tier 2; however, the agency cannot estimate the number of inactive members that would be affected.

The enactment of HB 2659 would require both technical changes to the KPERS pension administration system as well as work to collect additional data on "teachers" that KPERS does not currently have in possession. In addition, there would need to be education and communication efforts for the affected members. KPERS 2 is a fundamentally different plan than the KPERS 3 cash balance plan. While the technical structure for KPERS Tier 2 remains in place in the pension administration system, the conversion of members from KPERS Tier 3 to KPERS Tier 2 would require substantial coding changes to calculate the proper salary and service time information that will be required for KPERS 2 benefit calculations. KPERS estimates the cost for the technical work on the pension administration system and testing to total approximately $950,000 from the KPERS Fund and would take approximately six months to complete.

Additional KPERS staffing would be required for the identification of teacher members and for providing education and resources to members. The agency would require 5.00 temporary FTE positions and salaries and wages expenditures totaling $362,111 (including fringe benefits) in FY 2025 for 3.00 temporary Benefit Analysts and 2.00 temporary Benefits Representatives. For FY 2026, expenditures for these 5.00 temporary positions would total $377,528 (including fringe benefits). KPERS indicates these temporary positions would no longer be needed two to three years after the changes in HB 2659 would be in effect.

For estimating the actuarial costs to KPERS associated with the enactment of the bill, the actuary reports that moving the KPERS Tier 3 teacher members to KPERS Tier 2 would increase the unfunded actuarial liability (UAL) for those members by $134.0 million as a result of the difference in the benefit plan design. The proposed changes affect the benefit amounts for future retirees, so the actuary used an amortization period of 20 years for the increase in the UAL. The amortization payments would be determined using the same methodology used in the actuarial valuation, which is the level-percent of payroll. The increase in the UAL, normal cost rate, and total actuarial contribution rate (which includes both the increase in the normal cost rate and the UAL rate), are summarized in the following table:

State/School Group
(Dollars in millions)

	Baseline	HB 2659	Change
Actuarial Liability	$24,290	$24,424	$134
Actuarial Value of Assets	18,029	18,029	--
UAL	$ 6,261	$ 6,395	$134
Funded Ratio	74.20 %	73.80 %	(0.40 %)
Normal Cost Rate	8.89 %	9.15 %	0.26 %
UAL Contribution Rate	8.53 %	8.73 %	0.20 %
Actuarial Contribution Rate	17.42 %	17.88 %	0.46 %
Member Rate	6.00 %	6.00 %	--
Employer Contribution Rate	11.42 %	11.88 %	0.46 %

As shown in the table above, HB 2659 would increase the normal cost rate by 0.26 percent of payroll for the State/School Group. In addition, there would also be a contribution rate increase to fund the increase in the UAL over 20 years totaling 0.20 percent for the State/School Group. The additional payment on the UAL would be over a fixed period and would stop after 20 years of payments. The increase of 0.46 percent in the State/School Group rate is estimated to increase expenditures by approximately $25.1 million in FY 2025 and $26.1 million in FY 2026. The Division of the Budget estimates that 85.0 percent of employer contributions for the State/School Group is funded from the State General Fund. As a result, of the total increased employer contributions, $21.3 million would be from the State General Fund in FY 2025 and $22.2 million in FY 2026.

KPERS notes that the bill does not include a funding mechanism for the plan design changes. Based on current law (KSA 74-4920) and with the enactment of the bill, KPERS would recertify the employer contribution rate to the Division of the Budget for FY 2025, which would increase the employer contribution rate from 11.42 percent to 11.88 percent, exclusive of the KPERS Death and Disability Insurance rate. KPERS would also note that the $134.0 million increase in the UAL could be funded with a one-time appropriation by the Legislature. Under this scenario, this would eliminate the 20-year amortization of the UAL increase, reducing the change in the FY 2025 employer contribution rate from 0.46 percent to 0.26 percent, or from an increase of $25.1 million to an increase of $14.2 million. From the State General Fund, the increase would be reduced from $21.3 million to $12.1 million, with the same assumption that 85.0 percent of employer contributions for the State/School Group is funded from the State General Fund. Any fiscal effect associated with HB 2659 is not reflected in *The FY 2025 Governor's Budget Report*.

Sincerely,

Adam C. Proffitt
Director of the Budget

cc: Jarod Waltner, KPERS