KPERS SINCE 2004

Since my election to the KPERS Board of Trustees I have a new disclaimer that I must include in my comments from now on: "The views expressed in this update represent my views and/or the views of the Coalition & KARSP. They do not in any way represent the views of the KPERS Board of Trustees nor do I speak for them." Ernie Claudel

"THE HISTORY"

My name is Ernie Claudel. I am an Army Veteran and a retired teacher and building administrator with over 30 years of experience in the State of Kansas.

I began what I call chasing KPERS in 2004. Since that time, I have been involved with KARSP (Kansas Association of Retired School Personnel) which I presently lobby for as well as KCPR (Kansas Collision of Public Retirees) for which I also lobby. I began 'officially' lobbying two years ago. I am also the legislative chair for KARSP and the Co-chair for KCPR as well as my local KARSP Unit in Olathe. In 2013 I was elected to the KPERS Board of Trustees as a representative of KPERS School. <u>I am presently in my third term in this position.</u> The reason I can be a lobbyist and still serve on the KPERS Board is that the organizations I lobby for do not budget to contribute to or on behalf of our elected representatives.

I have put this history together because the gentleman who used to do this for the committees, Dr. Julian Efird, has retired. While I do not have the precise technical information, he had available, I am confident that the chronology is correct.

KCPR was established in 2006 to support the push for a COLA. Prior to this time there were a number of groups and professional organizations made up of KPERS retirees that were seeking a COLA, but there was no unified front or spokespeople for the idea. We began attending every committee meeting when KPERS was on the agenda. We wore black T-Shirts with a State of Kansas outline and KCPR boldly displayed. We became known as the "black shirts."

The last COLA (K.S.A.74-4950i) was enacted by the Legislature in 1998 and the statute called for the benefit to reach back to 1997. It has, therefore, been 25 years since the last COLA. Out of this group lobbying effort 'likely' came the following benefit increases. (I use the word likely because we were never informed that our efforts were the cause, because we were the ones lobbying for a benefit increase.) The following improvements were noted:

1. $300 onetime bonus – 2007 (K.S.A. 79,114b)
2. $300 onetime bonus – 2008 (K.S.A. 79,114c)
3. Tier II Effective July 2009 (KPERS 2 was created by 2007 SB 362, effective for members on or after July 1, 2009. It is now K.S.A. 74-49,201 through 74-49,212)

In 2011, the House Committee on Insurance and Pensions became very interested in KPERS and how its members were benefiting. KCPR was asked to contribute much information, much as they have been now. It is fair to say that out of this information came the 2011 KPERS Commission. We believed that the goal of all this research and testimony was to find a way to reduce the annual cost of KPERS. More precisely, we felt there was an attempt to do away with it, and certainly turn it into a Defined Contribution Plan, as opposed to the present Defined Benefit program.

The cause of this move was at least three main reasons:

1. The so called 'CRASH' of 2008.
2. The reduced funding level of the KPERS Trust Fund which followed this economic event.
3. The level of unfunded actuarial liability.

Upon the election of Governor Brownback, from our perspective, several things began to happen. There was a heightened interest in KPERS. The goals were the following:

1. Finding a way to reduce the UAL or do away with it.
2. Convert KPERS to a 401K type of pension system or some other type of retirement system that was thought to be surely less expensive.
3. Later consideration of privatizing KPERS was also explored.

To attempt to achieve the above began with committee hearings and later the KPERS Commission of 2011. Out of this commission came KPERS 3 that was created by 2012 HB 2333, effective for members on and after January 1, 2015. It is now K.S.A. 74-49,301 through 74-49,318.

A. The legal review that occurred, as part of the KPERS Commission of 2011, established the fact that the Unfunded Actuarial Liability (UAL) would have to be paid because it was indeed State Debt.
B. Because of Contract law stating that the benefit must be paid as promised to the employee at time of employment.
C. It was further indicated that this requirement applied to vested members of the retirement system and those already retired.
D. The Legislative Efficiency Report of January 12, 2016, recommended the payment to the KPERS Trust Fund to be the ACTUARIAL amount, not the statutory amount which was being used. (K.S.A.74-4920(8)
E. KPERS, as any U.S. retirement plan, public or private, must be approved by the IRS. KPERS, as some have suggested on occasion, is <u>not</u> a Ponzi Scheme.

The outcome was the development of Tier 3 and the changing of Tier 2. The following should be noted:

A. Tier 2 was altered because it had a built in COLA for all new hires.
B. The employee contribution rate for all KPERS employees was raised to 6% from the longstanding 4%.
    a. To compensate for removing the built in COLA in Tier 2 and increasing the employee contribution rate, the multiplier for any contributing the higher rate, was increased from 1.75 to 1.85.
    b. Because of the legal finding presented at the KPERS Commission, only the not yet hired could be required to be enrolled in Tier 3. (Study of public pension systems around the country is noted that 'drastic' changes in the pension systems have been made only regarding new employees.)
    c. All under the KPERS umbrella were changed to Tier 3 except for KP&F and the Judges.
        1. I have learned that the reason these were not changed was because of the shorter time these groups had to accumulate retirement funds because of physical requirements and age of appointment. Since these groups were more near fully funded and no one could figure out a solution to the challenge of fund contribution over reduced years of employment, both groups remained in Tier 1.

The UAL (unfunded actuarial liability) combined with the funded level of KPERS was the concern. In our mind, there were two main contributors to this:

1. When the original Kansas School Retirement System (KSRS) was consolidated with KPERS in 1971 by K.S.A. 74-4934. The Legislature authorized this move but did not fully fund the consolidation. The Kansas Statute reads that if any program was consolidated with KPERS it must be fully funded. The statute was never totally complied with by the legislature. (Related Statute K.S.A. 74-4935, 74-4935a & 74-4935b)
   A. <u>This has led us to use the mantra that KPERS School has been underfunded twice. Once when consolidated in KPERS and then secondly, along with the rest of KPERS by the legislature.</u>
   B. It should be noted that the legislature was very edgy regarding these years of underfunding. The main cause of the UAL is the years of underfunding. Prior to Governor Brownback publicly stating this fact, we were very careful how and where we used this fact.
   C. If the actuarial calculated amount would have been <u>annually</u> contributed for the 25 years from 1994 to 2019, the present funded level would be more than 80% and the UAL would be reduced by at least 50%.
2. Senator Kerr was responsible for K.S.A. 74-4920(8) which provided for the following:
   A. The limit of funding could not exceed a certain % over the previous year. This led to continued underfunding for 25 years which kept the UAL from seriously being addressed until 2019.
      a. The first bonding was a request from the KPERS Board.
   B. When the financial statement on any COLA bill was prepared for the legislature, the total cost has to be calculated and reported. (We will address this later in this presentation.)
3. Move toward proper funding:
   A. BOND ISSUE # 1. "In February 2004, the State of Kansas issued $500 Million in pension obligation bonds, and KPERS received net proceeds of $440.2 Million in March of 2004. The proceeds have been invested to assist with financing the State and School group's unfunded actuarial liability. The debt service on the bonds will be paid by the State of Kansas in addition to the State's regular employer contribution." (This bond was requested/suggested by the KPERS Board. The UAL raised this concern.)
   B. BOND ISSUE # 2. Again in 2015, underfunding became such a concern that the Legislature approved the issue of $1 Billion in revenue bonds. The cost of the bonds to be paid by the General Fund, not the KPERS Trust Fund.

   C. Recent Annual Contributions to the KPERS Trust Fund, authorized by the Kansas Legislature, are as follows:
      a. In 2019 the Actuarial Determined Contribution (ADC) for Legislative contribution $656.1 Million.
      b. The actual Legislative contribution was $858.5 Million. *(+$202.4 Million over the ADC.)*
      c. In 2020 that Actuarial Determined Contribution for Legislative contribution was $704.3 Million.
      d. The actual Legislative contribution was $765.3 Million. *(+$61 Million over the*

ADC.)

e. In 2021 a $500 Million Bond – This was the outcome of proposed HB2289 which called for a 13th check to be funded by a $1 Billion bond issue. The 13th check proposal was removed from the bill.
f. 2022 Legislature authorized a $1.1 Billion Contribution to the KPERS Trust Fund. Breakdown of 2022, $1.125 Billion Contribution:
    1. $ 553.9 Million May 19
    2. $ 300.0 Million on June 1
    3. $ 146.1 Million on August 1
    4. $ 125.0 Million on December 1

D. According to the KPERS actuary, these amounts represent the first time since 1994 (25 years) that the Actuarial Determined Contribution have been met or exceeded.
E. In the 2021 through 2023 budget, the actuarial calculated amount has been included in the State budget.

4. History of COLA proposals are as follows: (The Benefit increases proposed by KCPR and KARSP are coded with a *.)
    A. In 2008, Governor Sebelius placed in her budget a 1%, 1%, 1% COLA to be implemented over a three-year period. It passed the Kansas House but not the Senate.
    B. Under Tier 2, <u>New Hires</u> had a COLA. This COLA was discontinued by the Tier III Legislation.
    C. KCPR & KARSP first attempt at a COLA following 2011 Legislation was in 2014, HB 2539. This was a 3% request. *
    D. In 2015 Harvey Ludwick worked through Sen. Hensley, Alan Conroy, and Gordon Self. After consultation with them and the actuary, KCPR elected to try the 3,2,1 % COLA. *
    E. That concept was submitted in January 2016 as HB 2542. *(Died, no bill rollover.)
    F. Resubmitted in 2017 as HB2023. *
    G. HB2023 was carried over to 2018. Could not get it out of committee.
    H. KCPR and KARSP Resubmitted in 2019 as HB2100. * Representative Miller introduced HB2289 which called for a 13th check to be funded by a $ 1 Billion bond issue. The 13th check proposal was removed from the bill. (Final outcome is listed in C, e at the top of this page.
    I. In the 2019 legislative session, Representatives Benson and Frownfelter submitted COLA amendment proposals. These were defeated on the floor of the House.
    J. HB2100 Carried over to 2020 and again died because we could not get it out of committee. *
    K. KCPR and KARSP did not submit in 2021. However.
    L. In 2022, two concepts were introduced in both the Senate and the House as identical bills
        a. An indexed, automatic COLA Bill SB401, HB2583*
        b. A 1,2,3,4,5% COLA SB402, HB2584*
        c. Neither Bill was heard in committee.
        d. HB 2584 was introduced in the House as an amendment. This attempt failed to pass.
        e. There was also a 13th check amendment introduced in the Senate by Sen. Pat Pettey which failed to pass.

f. The 13th check concept was also introduced in the House Appropriations Committee with no follow-up action.

H. There was a misunderstanding regarding the cost of SB402 and HB2584. The KERR Amendment (K.S.A. 74-4920(8) requires that the total cost of a bill be shown. There was confusion over the financial statement. Many thought the $317.4 Million cost was an annual expense. (This 'total' reporting is different than is typically used in bill financial statements.) In this case the cost is an annuity amount. The total cost could be impacted negatively or positively *only* in the fluctuation in the investment returns.

APPENDIX

The Statute Establishing KPERS is K.S.A. 74-4901.

"The purpose of this act is to provide an orderly means whereby employees of the participating employers who have attained retirement age as herein set forth may be retired from active service without prejudice and without inflicting a hardship upon the employees retired and to enable such employees to accumulate reserves for themselves and their dependents to provide for old age, death and termination of employment, and for the purpose of effecting economy and efficiency in the administration of governmental affairs."

KPERS Plan Dates:

A. Tier 1 dates run through 2009.
B. Tier 2 runs July 1, 2009, through December 31, 2014.
C. Tier 3 began January 1, 2015 – Present.

KPERS FACTS as of 12/31/2021:

A. 88% retirees remain in Kansas (# unchanged)
B. 70% of Active KPERS Group is KPERS School
C. State, School, Local make up 95% of the total KPERS #'s

History of Multipliers:

A. 1.4, (2.0 for legislators only. [used very briefly] *),1.75, 1.85.
B. Tier 1 multiplier is 1.75 in years served before 2014. Because of the increase in contribution rate, the multiplier is 1.85 after 2014.
C. The so called "California Rule" comes into play here – Changes to a pension plan that result in disadvantage to employees must be accompanied by comparable new advantages to avoid impairing the contract between the pension system and the employee. [Employee contribution rate raised from 4 to 6%.]

KPERS FUNDING LEVELS

As of July 23, 2021, the balance in the KPERS Trust Fund was $24.8 Billion. Ten years ago, the balance was just over $13 Billion. The record of 25 Billion was set on July 12, 2021. (This is a single day record, all time!)

Investment Assumption History

8% 1986 to 2016
7.75% from 2016 to 2022

7% from 2022 until changed.

<u>2022 Reamortization Rates in conjunction with lowering assumption rate to 7%.</u>
KPERS State/School extended 6 years (17 years remaining)
KPERS Local extended 6 years (17 Years Remaining)
KP&F extended 11 years (22 years remaining)
Judges extended 9 years (20 Years Remaining)

<u>THE UNDER FUNDING CHALLENGE</u>

1. Director Conroy always testifies that KPERS is very solid. Benefits will be paid!
2. This is true, but there is the caution:
   A. When the Legislature Appropriates moneys for future contributions, the actuary must assume that the dollars will be contributed when promised.
   B. Because of contract law and IRS requirements, those retired or their beneficiaries plus those members vested will have to be paid.
   C. 80% Funding or above is the goal.
   D. Contributions on an annual basis pay the present year benefits. If there is not cash on hand, investments would have to be closed out to make the monthly benefit payments. This would reduce the probability of investment income and begin the slide in the funded levels. Any underfunding increases the probability of this type of slide happening.
      a. Further, if the contributions promised in statute are not forth coming, the actuaries' calculations are no longer valid.
   E. KPERS serves over 300,000 individuals and 1,500 employers.
      a. No member of the KPERS staff will ever make an estimate on the result of any change in the system because KPERS has many, many moving parts!
      b. I have witnessed numerous instances when legislators and others, usually involving the thought that they had a better idea for saving money, be embarrassed when the cost analysis was calculated by the actuary and the cost FAR exceeded their estimate.

Ernie Claudel
KARSP Lobbyist and Legislative Chair
KCPR Lobbyist and Co-Chair
KPERS Board – Elected School
1109 W. Wabash St.
Olathe, KS 66061
eclaudel1@comcast.net
913-481-6923

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