

KPERS Overview



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House Pensions and Benefits Committee



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KPERS Overview

KPERS is a fiduciary providing retirement, disability and survivor benefits to our members and their beneficiaries with about 100 staff.

KPERS is governed by a 9-member Board of Trustees.

Terry Matlack, Chairperson (Appointed by Governor)

Lois Cox, Vice-Chairperson (Appointed by Governor)

Kelly Arnold (Appointed by Governor)

Ernie Claudel (Elected Member – School)

Ron Estes (State Treasurer – Statutory Member)

Todd Hart (Elected Member – Non-school)

Chris Long (Appointed by Governor)

Doug Mays (Appointed by Speaker of the House)

Suresh Ramamurthi (Appointed by President of the Senate)

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

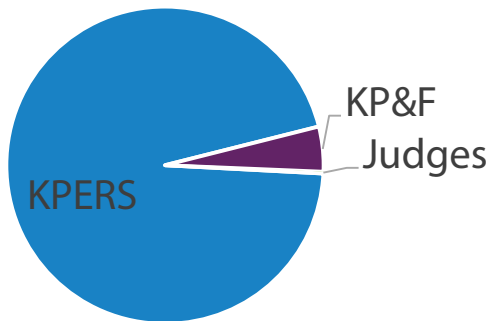
- Kansas Public Employees Retirement System (KPERS)
- Kansas Police and Firemen's Retirement System (KP&F)
- Kansas Retirement System for Judges (Judges)



KPERS Overview

Membership Information

Total Membership
Calendar Year 2013



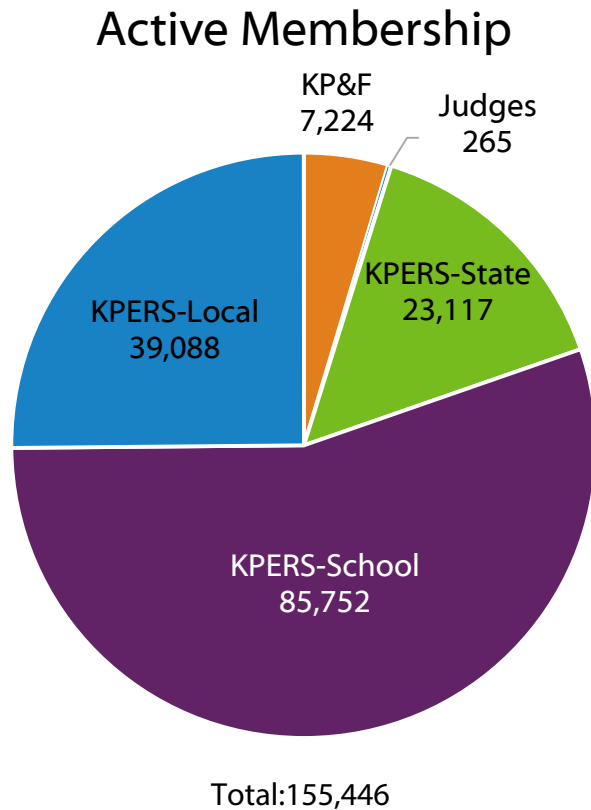
	KPERS	KP&F	Judges
Active	147,957	7,224	265
Retired	81,930	4,670	243
Inactive	46,096	1,382	6
TOTAL	275,983	13,109	494

KPERS Serves

- More than 289,000 members
 - More than 155,000 active employees
 - Approximately 10% of Kansans are members of a KPERS retirement plan
- More than 1,500 employers
 - State of Kansas
 - Every county
 - Over 400 cities and townships
 - All 286 school districts

KPERS Overview

Active Membership



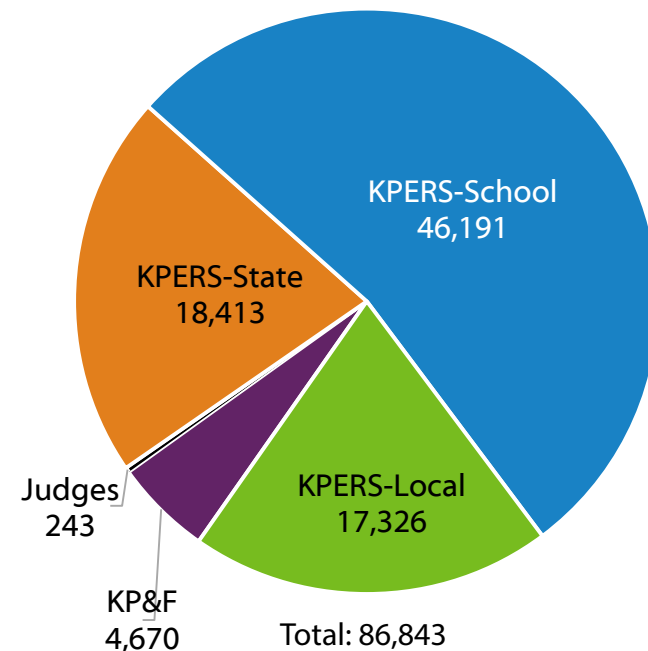
- More than half of active members employed by school districts
- Average current age
 - KPERS – 45.5
 - KP&F – 39.6
 - Judges – 57.8
- Average years of service
 - KPERS – 11.3 years
 - KP&F – 11.8 years
 - Judges – 11.7 years

KPERS Overview

Retirees and Beneficiaries

- Average age
 - KPERS – 72.0
 - KP&F – 66.3
 - Judges – 74.2
- Average annual benefit
 - KPERS – \$13,325
 - KP&F – \$29,721
 - Judges – \$39,809
- More than 88% of benefit payments are made to Kansas residents
- KPERS paid about \$1.48 billion in total benefits in FY 2013

Retirees and Beneficiaries



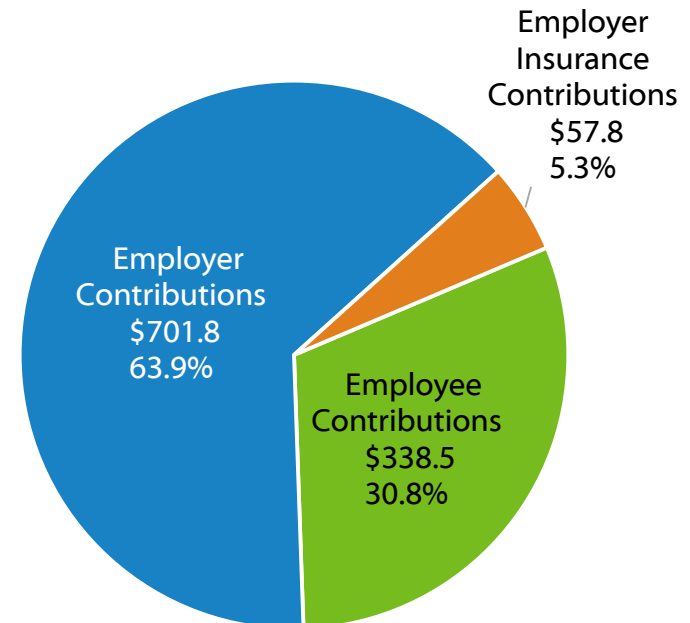
KPERS Overview

How Benefits Are Funded

$$\text{Contributions} + \text{Investments} - \text{Expenses} = \text{Benefits}$$

- KPERS Employee Contributions
 - KPERS 1 = 6% of pay (as of 1/1/15)
 - KPERS 2 = 6% of pay
 - KPERS 3 = 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
- Total Contributions for FY 2014:
\$1.1 billion

KPERS Contributions by Source (in millions)
FY 2014



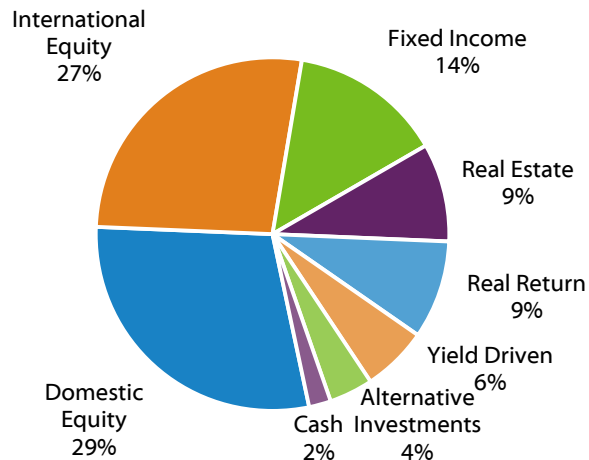
KPERS Overview

How Benefits Are Funded

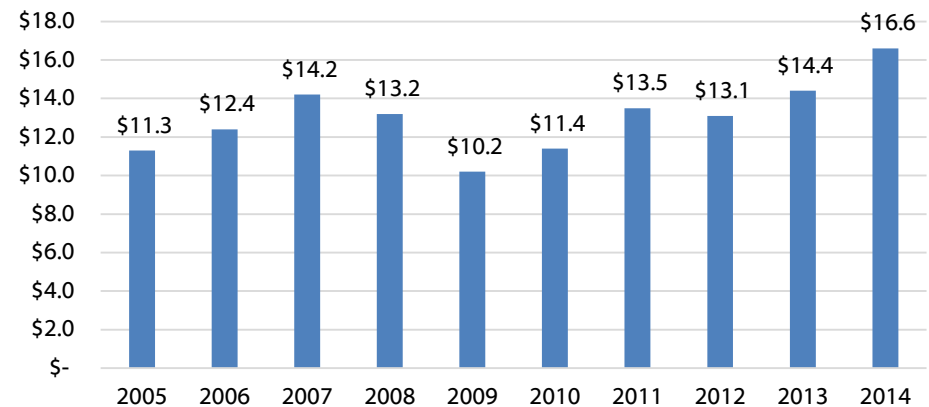
$$\text{Contributions} + \text{Investments} - \text{Expenses} = \text{Benefits}$$

- Over the past 20 fiscal years, investment returns made up 59% of revenues
- Staff of 8 internal investment professionals, over 100 years of combined experience
- 3 investment consultants and 26 investment managers
- Work together with disciplined, diversified and long-term investment approach
- Manage investments of more than \$16 billion of trust fund assets (as of 9/30/14) in the U.S. and international markets

Interim Target Allocation



Net Asset Value: FY 2005 - FY 2014 (in billions)



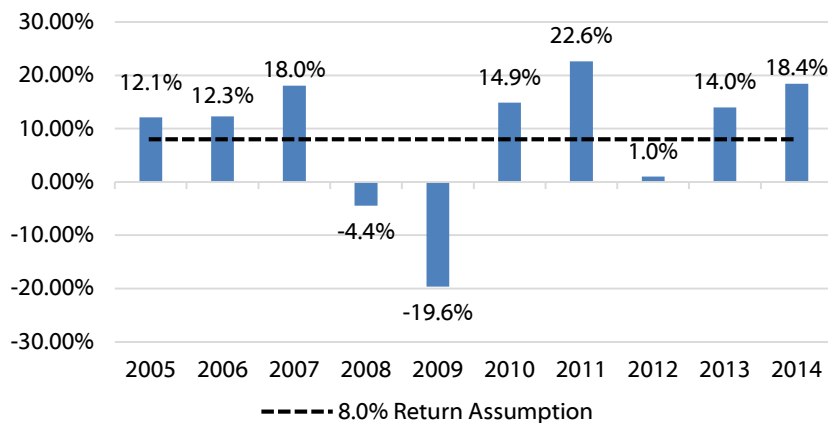
KPERS Overview

How Benefits Are Funded

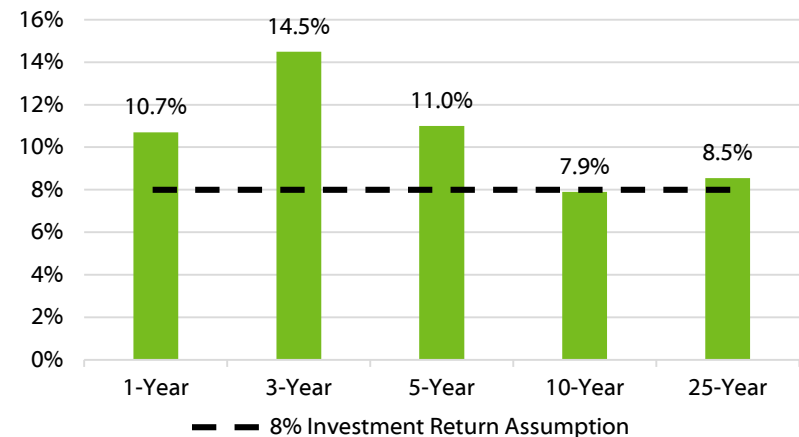
$$\text{Contributions} + \text{Investments} - \text{Expenses} = \text{Benefits}$$

- FY 2014 return: 18.4%
- CY 2014 return to date: 4.9% (as of 09/30/14)
- 8.0% long-term return assumption
- Earned 8.5% over the last 25 years (as of 09/30/14)
- Recent returns were exceptionally robust. We expect returns to normalize going forward.

Total Returns by Fiscal Year



Annualized Total Return through 9/30/2014



KPERS Overview

How Benefits Are Funded

Contributions + Investments – Expenses = Benefits

- Total investment management fees for FY 2013: \$30.9 million
 - 18.6 basis points on \$16.6 billion in assets
- Total benefit administration expenses for FY 2013: \$10.1 million

KPERS Overview

How Benefits Are Funded

$$\text{Contributions} + \text{Investments} - \text{Expenses} = \text{Benefits}$$

- Final average salary x years of service x 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 **\$1.48 billion** in total benefits in FY 2013 (retirement, death benefits, disability benefits, withdrawals)

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

Average KPERS 1 member

Final average salary	\$40,000
Service	20 years
Benefit	\$14,800 a year

Long-term KPERS 1 member

Final average salary	\$40,000
Service	30 years
Benefit	\$22,200 a year

KPERS Legislation

2012 KPERS Reform

- The Legislature implemented a three-pronged approach to improving KPERS' funding status
 1. Increased employer contributions by raising the cap on annual contribution increases (0.9% in FY 2014, 1.0% in FY 2015, 1.1% in FY 2016 and 1.2% in FY 2017 and future years)
 2. Increased employee contributions from 4% to 6% over a two-year period for KPERS 1 members
 3. A new cash balance plan design for all new hires on and after 1/1/2015

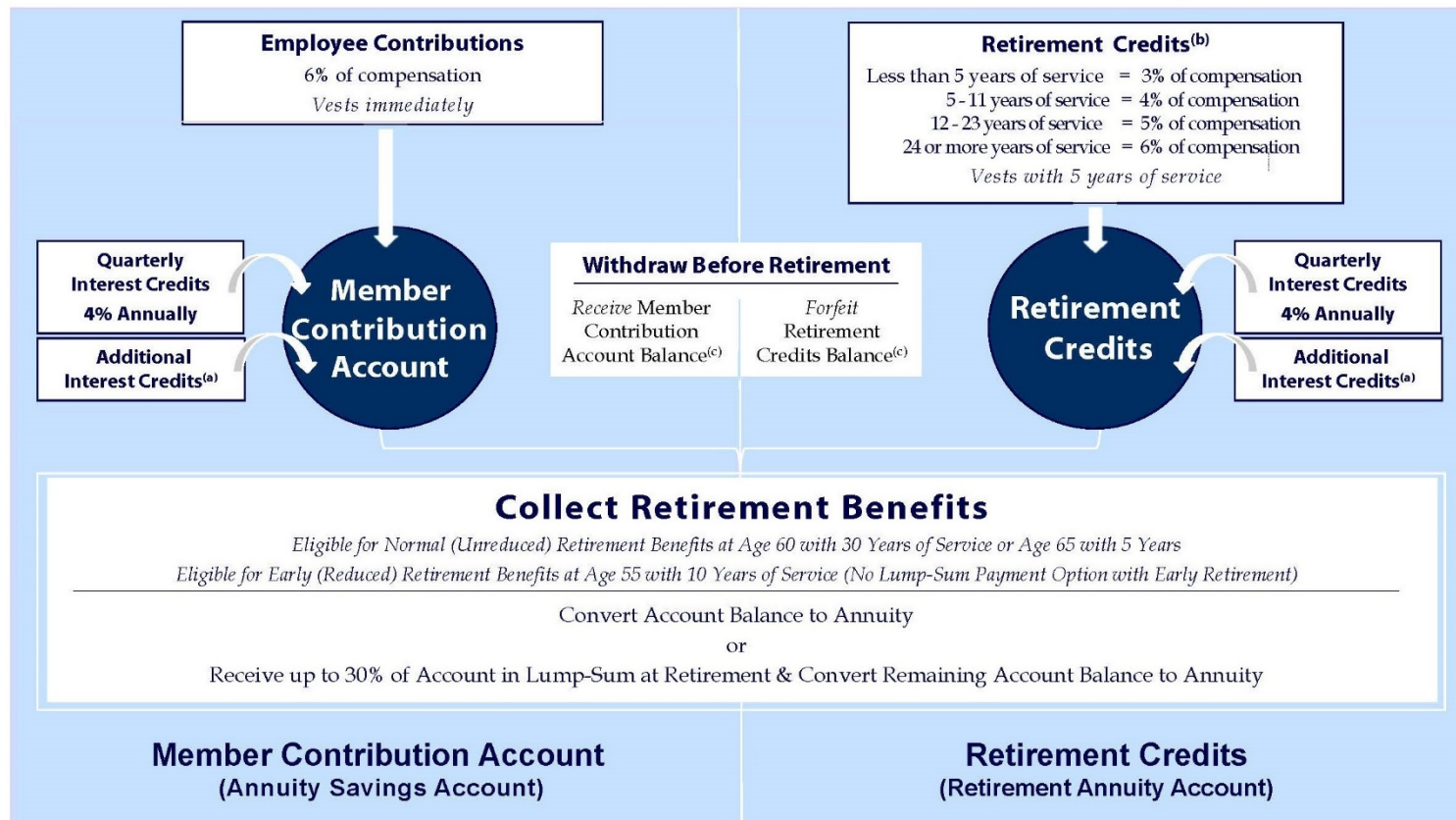
KPERS Legislation

2014 Plan Design Adjustments

- Legislation enacted in 2014 made adjustments to the KPERS 3 cash balance plan design:
 - Changed the guaranteed interest crediting rate from 5.25% to 4.0%;
 - Struck the provisions pertaining to a discretionary dividend;
 - Added language establishing a formulaic dividend equal to 75% of the five-year average net compound rate of return on the market value of the system's assets above 6% on a rolling 5-year average, except that between calendar year 2015 and calendar year 2018, the average return begins in 2015 and includes all years up to the current year, and the dividend is capped at 1.5%. The rolling 5-year average begins 2019, at which point, there is no cap; and
 - Changed the annuity rate from a set 6% to the actuarially assumed investment rate of return minus 2%. Currently that amount equals 6%.

KPERS 3 Cash Balance Plan

Plan Design



(a) Members will receive additional interest credits according to a statutory formula based on the Retirement System's investment returns (credits capped at 1.5% through the end of calendar year 2018).

(b) Retirement credits are posted to Retirement Annuity Accounts but only available to members at retirement.

(c) Interest will be credited for two plan years only for members terminating with non-vested accounts.

10/14

2013 Actuarial Valuation



- An actuarial valuation is a “snapshot” of the system’s financial condition
- Shows cash flows that have already occurred versus those that are expected to occur in the future

2013 Valuation

Purpose of Actuarial Valuation

- Measure Assets and Liabilities
 - Prepare Best Estimate of Ultimate Costs
 - Project future benefits using actuarial assumptions
 - Calculate present value of future benefits
 - Apply cost method to allocate to periods of service
- Calculate Employer Contribution Rates
 - **FY 2017** for State/School Group
 - **CY 2016** for Local Group
- Prepare Disclosures for Financial Report
- Provide Baseline for Legislative Changes in 2015

2013 Valuation

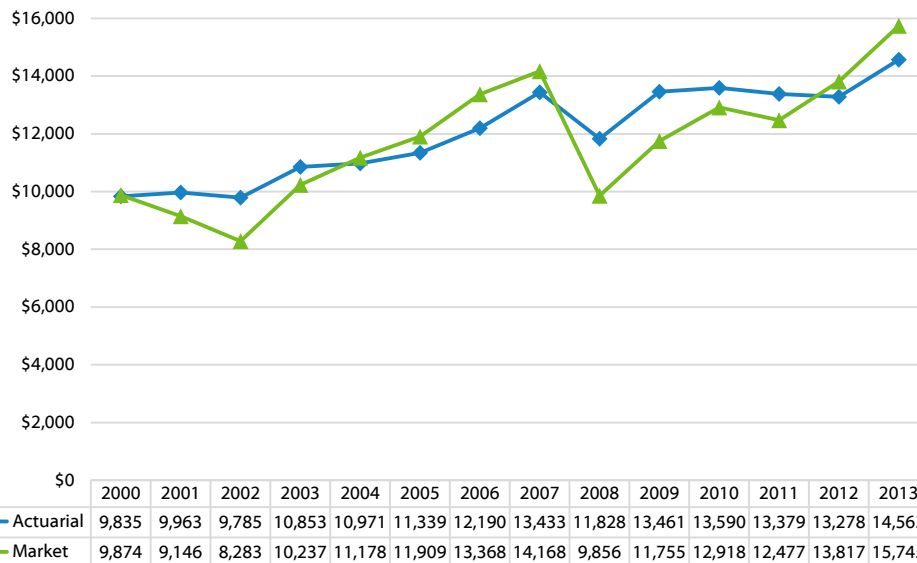
December 31, 2013 Valuation

- No changes in assumptions or methods
- Reflects many of 2012 HB 2333's provisions
 - Higher statutory caps on employer contribution increases
 - Expanded Lottery Act Revenue Fund transfers (except for FY 2014 and FY 2015)
 - KPERS 1 and 2 active member changes in contributions and benefits
 - KPERS 3 members (cash balance plan) do not yet affect valuation – just projections.

2013 Valuation

Assets and Liabilities as of 12/31/2013

- KPERS' Unfunded Actuarial Liability (UAL) decreased from \$10.3 billion to \$9.8 billion. The funded ratio improved from 56% to 60%.
- The UAL represents benefits already accrued by members and cannot be eliminated by future plan design changes. It is a debt that must be paid.



- The market value of assets exceeds the actuarial value of assets
- Investment gains and losses are averaged in over five years to calculate actuarial value
- A higher market value of assets indicates deferred gains yet to be averaged in
- More than a **billion dollars** in deferred investment gains are yet to be realized

2013 Valuation

Employer Contribution Rates

- The actuarial valuation sets employer contribution rates for future years
- Employer contribution rates for State/School and Local may be subject to statutory caps (1.1% in FY 2016, 1.2% in FY 2017)

Valuation Year	Apply to Fiscal Year Beginning In	State/School Employer Contribution Rate	Local Employer Contribution Rate	KP&F Employer Contribution Rate	Judges Employer Contribution Rate
2011	2014	11.27%	8.84%	19.92%	22.59%
2012	2015	12.37%	9.48%	21.36%	23.98%
2013	2016	13.57%	9.18%	20.42%	21.36%

2013 Valuation

Employer Contribution Rates

- Actuarially Required Contribution (ARC) rates are made up of two parts:
 1. Normal cost – the amount needed to fund the benefit liability accrued by a member in the valuation year
 2. Unfunded Actuarial Liability (UAL) – the actuarial present value of retirement system benefits allocated to the current year by the actuarial cost method
- The statutory cap on employer contribution rates have kept contributions for the State/School Group below the ARC rate for the last 20 years

State/School Group Employer Contribution Rates		
	FY 2016	FY 2017
Employer Normal Cost	2.26%	2.22%
UAL Payment	12.69%	12.63%
Total ARC Rate	14.95%	14.85%
Statutory Employer Contribution	12.37%	13.57%

2013 Valuation

12/31/2013 Valuation - Employer Contribution Rates

- For fiscal years beginning in 2016, all groups other than School Group will be at the Actuarially Required Contribution (ARC) Rate.
- The ARC rate went down for all four funding groups compared to the 2012 valuation

System	Actuarial Rate (ARC as % of Pay)		Statutory Rate		% of ARC Contributed
	12/31/2012	12/31/2013	12/31/2012	12/31/2013	12/31/2013
State	11.44%	10.77%	12.37%	13.57% *	126%
School	16.00%	16.03%	12.37%	13.57%	85%
State/School	14.95%	14.85%	12.37%	13.57%	91%
Local	9.48%	9.18%	9.48%	9.18%	100%
KP&F	21.36%	20.42%	21.36%	20.42%	100%
Judges	23.98%	21.36%	23.98%	21.36%	100%

*The excess of the statutory over the actuarial contribution rate on State payroll is contributed to the School Group.

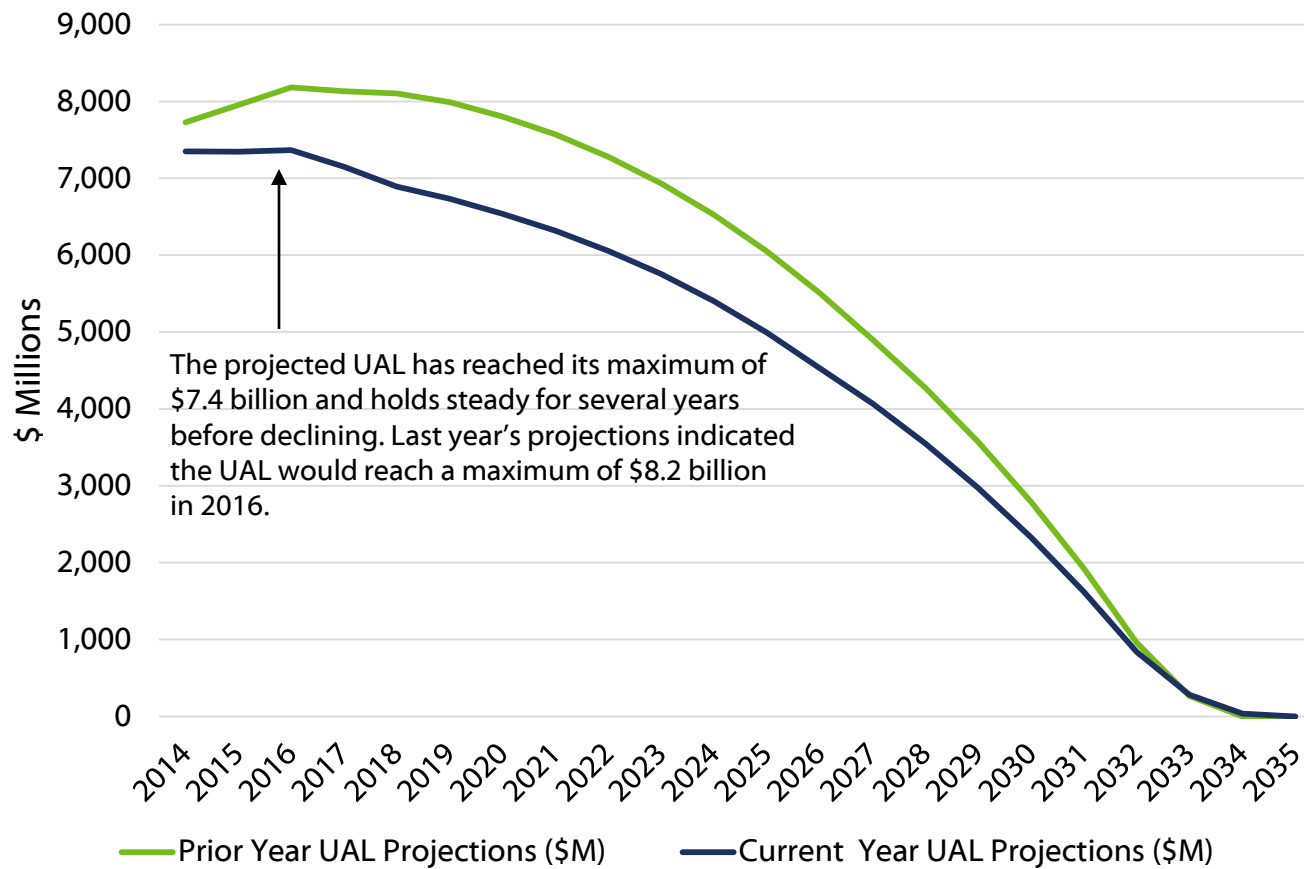
KPERS' Funding Status

Long-Term Funding Outlook

- Long-term funding outlook improving
- Funded ratio projected to continue improving and unfunded actuarial liability (UAL) projected to continue decreasing as long as future assumptions are met
- KPERS is projected to be 100% funded by end of amortization period (FY 2033)

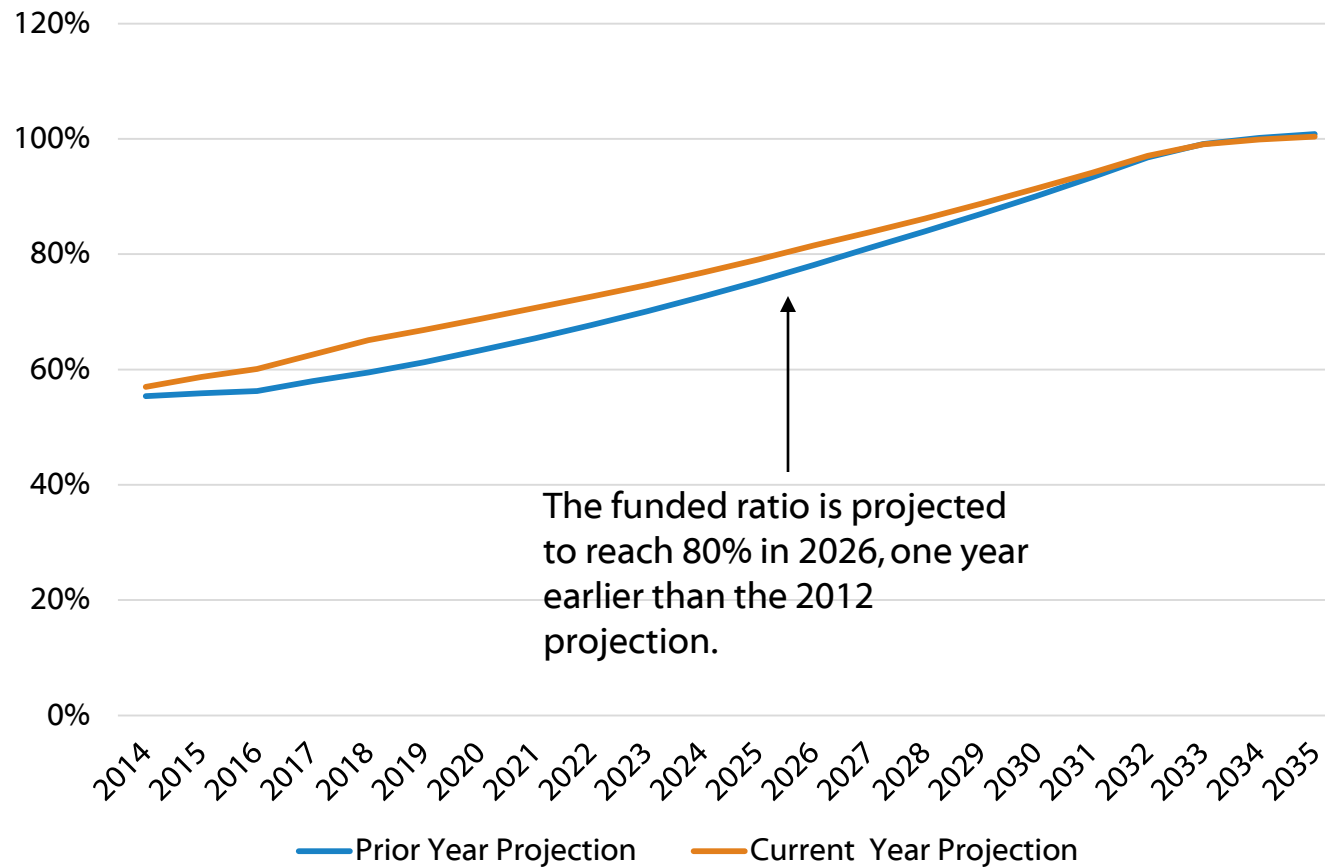
2013 Valuation

Projected State/School Unfunded Actuarial Liability



2013 Valuation

Projected State/School Funded Ratio



Governor's Allotments

How KPERS is Affected

- The Governor's December 2014 allotments included reducing the employer contribution rate from 11.27% to 8.65% for the last 6 months of FY 2015
- \$40.7 million in State General Fund reductions, approximately \$58 million total reduction in contributions to the KPERS Trust Fund
- Lower contributions in FY 2015 are not projected to keep KPERS from being fully funded by the end of the amortization period (FY 2033), but do slow the rate at which KPERS' funded ratio improves and increase total future contributions
- The dollars were removed through the Governor's allotment authority, the Legislature will have to enact the rate change

Pension Obligation Bonds

Additional Assets to Improve Funding

- Referring to the formula $C+I=B+E$, bond proceeds:
 - Increase the C (contributions) in a single year, which immediately improves the System's funded ratio and lowers the unfunded actuarial liability (UAL)
 - Can increase investment income (I) as more assets are available to be invested in the short-term
- Assuming the UAL's current amortization period is not changed, the additional contributions:
 - Do not shorten the time until System is fully funded (currently FY 2033)
 - Have the affect of lowering future employer contribution rates if all assumptions are met in the future
- Debt service from a source other than KPERS is assumed
- With current bond rates relatively low, the opportunity for KPERS' investment returns exceeding the bond rate exists (arbitrage)

Pension Obligation Bonds

2004 Bonds

- The 2003 Legislature authorized \$500 million in pension obligation bonds to increase the System's assets
- KPERS received about \$440 million in additional assets in March of 2004
- Debt service on the bonds (about \$33 million annually) is appropriated from the State General Fund to the Department of Administration
- As of 9/30/2014, the investment return on the proceeds of the 2004 pension obligation bonds (7.45% return) has exceeded the bond rate (5.39%) by more than \$174 million

Pension Obligation Bonds

How Bond Proceeds Could Affect KPERS

- If \$1.0 billion in bond proceeds were added to the KPERS Trust fund during 2015, actuarial projections show:
 - An immediate increase of nearly 6% in the funded ratio, from 60.7% to 66.3%
 - A decrease of 1.84% in the FY 2019 employer contribution rate, from 14.83% to 12.99%
 - An overall reduction of \$2.2 billion in total contributions over the next 20 years
- Because employer contribution rates are certified for future fiscal years, the rates are not affected until FY 2019
 - Lower contribution rates in earlier fiscal years could be enacted by the Legislature
- Reductions in employer contributions do not reflect the debt service that the state would have to pay for the pension obligation bonds

Pay Period Reporting

Beginning in January 2015



- Employer reporting will change from annual reporting to pay period reporting
- The change is necessary to meet KPERS 3 cash balance plan requirements

Pay Period Reporting

Making the Move to Pay Period Reporting

- Old Process
 - For each pay period, employers paid lump sums for total covered payroll, including both employee and employer contributions
 - Employers later reconciled by individual employee with annual reporting
- With the New Process:
 - Employers report wage information by employee with each pay period
 - KPERS' system calculates an invoice
 - Employers remit based on their invoice
 - KPERS will no longer need annual reports; reporting and reconciliation will essentially be part of the remittance process
- Began in January 2015
- Employers will still do 2014 annual contribution reporting in January/February 2015

Pay Period Reporting

Why the Change?

- The KPERS 3 Cash Balance Plan for new hires began January 1, 2015
- Although still a defined benefit plan, a cash balance plan has many features of a defined contribution plan - like a 457(b)
- KPERS 3 benefits are based on account balance, and members receive regular, up-to-date information
- The law requires at least quarterly account balance crediting

KPERS

Questions?