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Adam C. Proffitt, Director

Laura Kelly, Governor

February 3, 2025

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 2086 by House Committee on Financial Institutions and Pensions

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2086 is respectfully submitted to your committee.

Under current law, the KPERS Tier 3 Plan is a cash-balance retirement design where members accrue notional account balances over their career. At retirement, those notional balances are converted into an annuity benefit.

Under KPERS Tier 3, a member has a contribution account and an employer pay credit account. These accounts earn annual interest at a guaranteed rate of 4.0 percent and potentially earn a dividend interest credit based upon a statutory formula. The current statutory dividend interest formula is 75.0 percent of the five-year average investment return of the KPERS Trust Fund above 6.0 percent. HB 2086 would increase this dividend interest formula from 75.0 percent to 80.0 percent of the five-year average investment return above 5.0 percent.

To administer the changes, KPERS indicates that the enactment of HB 2086 would have a negligible effect on the agency's operations. KPERS publications would have to be updated, but the agency reports that no additional staffing or information technology development would be required and could be implemented with the agency's current submitted budget for FY 2025 and FY 2026.

The enactment of the bill would provide increased retirement benefits for KPERS Tier 3 members. As of December 31, 2023, a total of 79,886 members of the State/School Group and the Local Group would receive this benefit enhancement, as well as all new members entering the KPERS Tier-3 Plan. The proposed changes would increase the overall funding risk to KPERS, as higher employer contributions would be needed over time to finance the higher benefits.

Although each individual KPERS Tier 3 retiree's situation would be different depending on many variables, KPERS has illustrated what the benefit increase may be for a career employee with 30 years of service. If this individual would retire making an annual salary of $60,000, HB 2086 would increase the replacement income ratio from 33.2 percent to 36.5 percent. Under current law, this KPERS Tier 3 member employee would receive approximately $19,920 annually from KPERS for retirement benefits. HB 2086 would increase this yearly amount by $1,980 to $21,900, an increase of 9.9 percent.

For the State/School Group, the KPERS actuary indicates that the bill would increase the KPERS unfunded actuarial liability (UAL) by $102.1 million. With current law, any benefit enhancement is required to be reflected in the fiscal year immediately following the enactment of the change. As a result, the state could either: (1) make an up front payment to KPERS from the State General Fund totaling $102.1 million, likely from the State General Fund, to pay for the cost; or (2) pay for the increased costs through increased employer contributions for the UAL. With the second option, the state's employer contributions (excluding death and disability contributions) would increase by 0.48 percent, going from 11.68 percent to 12.16 percent in FY 2026. This increase is estimated to cost $27.0 million from all funding sources for FY 2026. The Division of the Budget (DOB) notes that using an estimate of approximately 85.0 percent of the State/School Group's employer contributions being paid from the State General Fund, this would result in additional expenditures of $23.0 million from the State General Fund statewide for employer KPERS contributions, including KPERS-School payments.

KPERS notes that if the state would make the upfront UAL payment, the state would still incur an increase in KPERS employer contribution rate of 0.35 percent for the cost of the increased benefit. KPERS estimates that this would increase expenditures by $19.8 million from all funding sources, with $16.8 million from the State General Fund, using the DOB payroll funding split estimate. Any fiscal effect associated with HB 2086 is not reflected in *The FY 2026 Governor's Budget Report*.

For the Local Group, KPERS indicates that the bill would increase the UAL by $43.7 million. However, unlike the State/School Group, there is no mechanism to pay for the increase in the UAL up front by local employers. As a result, Local Group employers would experience an employer contribution rate increase during calendar year 2026 of 0.58 percent, going from 9.59 percent to 10.17 percent. This increase would cost local employers an estimated $12.9 million among approximately 1,400 Local Group KPERS employers. If the state would make the UAL payment up front for the Local Group, the employer contribution would increase by 0.41 percent in calendar year 2026 for the cost of the benefit increase, or approximately $9.1 million.

Sincerely,

Adam C. Proffitt
Director of the Budget

cc: Jarod Waltner, KPERS