Bill number: HB 2656 Due date: 2/13/2016

Responding agency: Kansas Public Employees Retirement System

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Fiscal Impact

State—Would this bill have a fiscal effect on your agency? Yes ☒ No ☐

Local—Would this bill have a fiscal effect on local government? Yes ☐ No ☒

Tax Revenue—Would this bill affect State General Fund revenues? Yes ☐ No ☒

Fee or Other Revenue—Would this bill affect revenues to other state funds? Yes ☒ No ☐

Expenditures	FY 2016	FY 2017
State General Fund	$0	$0
Fee Fund(s)	$0	$0
Federal Fund	$0	$0
Total Expenditures	$0	$0
Revenues		
State General Fund	$0	$0
Fee Fund(s)	$0	Unable to Calculate
Federal Fund	$0	$0
Total Revenues	$0	$0
FTE Positions	0.0	0.0

Bill Description

Briefly describe what the legislation does. Describe the change(s) from current law that would drive an increase or decrease in expenditures or revenues. If federal funds are affected by the bill in some way, explain that relationship as well. Note any technical or mechanical defects with the bill (bill drafting errors only, do not include commentary as to whether the bill should be enacted or not).

From 2009 through June 30, 2016, retirees employed in licensed school professional positions have not had an earnings limitation. However, beginning July 1, 2016, these retirees will have an earnings limitation of $25,000 unless the position qualifies for a hardship, special education, or hard-to-fill exemption or the retiree is grandfathered through June 30, 2017.

HB 2656 creates a new exemption from the working after retirement rules in K.S.A. 74-4914. Any retiree who retired at or after age 62 and who is subsequently employed by a school district in a position that requires a license under K.S.A 72-1388 would be exempt from any earnings limitation while receiving their retirement benefit and working for a school district. The employing school district would be required to contribute the full actuarial required contribution rate plus 8%. For FY 2017 that rate totals 24.03%.

Assumptions for Fiscal Effect Estimate

Expenditures: *Detail the assumptions made in preparing the cost estimate. Describe agency expenditures that would become necessary with passage of the bill and how workload assumptions translate into the cost estimates. The estimate for any new position should be detailed to show the salary, benefits and associated other operating costs (such as a computer or other equipment). Distinguish between one-time and ongoing costs.*

Revenues: *Describe the assumptions and methods used in estimating the bill's effect on revenues. Detail the source of the revenue—is it a tax, agency earning, fee income or a federal reimbursement—and the fund that would receive the revenue. Distinguish between one-time and ongoing revenue changes estimated to result from passage of the bill.*

Expenditures:
The changes in HB 2654 would require some modifications to KPERS' information technology systems to update existing functions to accommodate the new exemption. However, the estimated cost to complete these upgrades could be accomplished within existing resources.

Additional staff responsibilities for communications and services to retirees and employers subject to working after retirement provisions, reporting and payment functions, and other administrative duties are expected with HB 2656. In combination with 2015 HB 2095, the administration of working after retirement rules is growing in complexity. While KPERS anticipates absorbing the additional workload, further consideration of appropriate staffing levels may be required in the future as KPERS' gains experience with the administrative impact of the new rules.

Revenues:
Under 2015 HB 2095, employers who hire a KPERS retiree who would pay the statutory employer contribution rate for active members, unless the retiree is hired under an exemption from the earnings limitation or has grandfathered status under 2015 HB 2095. In FY 2017, that rate would be 10.81% for State/School Group employers. Under HB 2653, employers using the new earnings limit exemption for age 62+ retirees would pay the actuarial rate plus 8% (24.03% in FY 2017 for School employers).

KPERS is not able to anticipate how these new rules would impact working after retirement patterns and, therefore, cannot estimate how the rate changes may impact expected revenues into the KPERS trust fund.

Long-Term Fiscal Considerations

If the bill affects future years, beyond those shown in the table above, explain the long-term fiscal effect—are the revenues stable over the long term or would there be a phase-in of costs or revenues; if the bill ends at a specific future date, indicate this as well.

Exemptions from the earnings limitation for retirees returning to work can impact the cost of retirement benefits, with the degree of the impact dependent on the number of retirees affected and the demographic characteristics of the employees (e.g., age, earnings, gender, and years of service). The potential for an impact results primarily from two factors:

<u>Changes in retirement patterns and behavior</u> stemming from incentives for members to retire later or earlier than they would have absent the exemption.

Actuarial assumptions are set regarding rates of retirement by age. For example, current actuarial assumptions regarding retirement rates for KPERS School Group members age 59 and above are as follows:

Of those School Group members eligible for full retirement who are age –	The percent are expected to retire at that age is –
59 and in first year of eligibility under 85 point rule	25%
59 and after first year of eligibility under 85 point rules	23%
61 and in first year of eligibility under 85 point rule	30%
61 and after first year of eligibility under 85 point rules	30%
62	30%
63	25%
64	35%
65	35%
66-71	25%
72-74	20%
75	100%

These retirement rates are heavily influenced by actual School Group retirement patterns and behavior in past years. Projections of actuarial liabilities and calculations of the actuarial contribution rates needed to fund those liabilities are built on the assumption that School Group members will retire at these rates. To the extent the proportion of members retiring is higher than the assumptions, actuarial liabilities and the actuarial contribution rate may increase. Likewise, if members delay retirement so that the proportion of members retiring is lower than the assumed rates, actuarial liabilities and the actuarial contribution rate may trend lower.

Members can be expected to act in their own financial interest. Retirees who can continue receiving pension benefits while earning all or a significant portion of their pre-retirement salary through employment with a KPERS-affiliated employer can realize a significant increase in their income. This potential financial benefit can be a significant incentive for members to modify the timing of their retirement. Therefore, an age-based exemption from the $25,000 earnings limit could be expected to become a material factor in members' decisions about when to retire.

To the extent members delay retirement for a period of time, their actuarial liability may be lower than had they retired before age 62. From 2009-2016, licensed school professionals have been able to work without an earnings limitation. Based on employer reports of retirees working after retirement in 2009 through 2014, there were 192 retirees returning to work in licensed school professional positions who had retired at age 59, 179 at age 60, and 130 at age 61. Similarly situated members could be incented in the future to delay retirement to age 62 in order to qualify for the earnings limit exemption in HB 2656 – particularly in light of the broader applicability of a $25,000 earnings limitation to retirees in licensed school professional positions beginning July 1, 2016.

On the other hand, some portion of those members who would otherwise have waited to retire after age 62 would have a new incentive to retire at age 62 in order to receive benefits while continuing to work, due to the potential for a significant increase in their income. This, in turn, increases the liability for their benefits above that anticipated under current actuarial assumptions, which reflect historical retirement patterns where an earnings limit applies to working after retirement.

However, there is no precise way to quantify with any certainty the cost impact of permitting KPERS members in licensed school positions to retire at age 62 and return to work without an earnings limitation. Because we know that financial incentives such as the proposed removal of the earnings limitation for retirements at or after age 62, members can be expected to take advantage of the exemption if it is in their best financial interests. Therefore, it is prudent to have some idea of what KPERS' exposure to adverse experience is if this change to the Working After Retirement provisions is passed by the Legislature.

In order to provide some sense for the potential exposure associated with such a shift toward earlier retirements at age 62, KPERS' consulting actuary completed an analysis that combined data from the annual valuation and information from the State Department of Education. The actuary estimated the number of licensed teacher positions and the number of members who would be eligible to return to work without an earnings limit under HB 2656, as well as inferring how the pay and service of licensed professionals may vary from the School Group as a whole.

The actuary then assumed that all members who were age 62 and had 20 years of service would retire to calculate a maximum exposure to adverse experience if active licensed school professionals shifted to retirements at age 62 rather than at later ages. The analysis suggested that, under those circumstances, the unfunded actuarial liability would increase $204 million and the actuarial contribution rate would increase by 0.41% for the State/School group. The estimate of $204 million is not a projected cost. Instead, it serves only as a reasonable upper boundary for the increase in liability if there is an increase in the percentage of members retiring at age 62 in the future. Other factors, including any corresponding delays in retirement to age 62, could offset some share of this liability.

<u>Reductions in employee and employer contributions</u> that occur when positions historically filled by active, contributing members are instead filled by noncontributing retirees.

Because the affected employers are paying contributions on the compensation of retired licensed professionals at the actuarial rate plus 8%, KPERS is continuing to receive contributions on the position filled by a retiree. However, it is not possible to project the extent or impact of changes in retirement patterns among the group of employees eligible for reemployment without an earnings limit under HB 2656. Therefore, a precise cost cannot be calculated, and it is unclear whether the actuarial rate plus 8% is sufficient to cover the increased liability of any change in retirement patterns. Therefore, there is also likely to be a long-term cost associated with changes in retirement patterns and behaviors.

To the extent that employer contribution rates are changed in future years due to a changes in actuarial experience, the revenues received by the Trust Fund will change. However, it is not possible to calculate the change in revenue due to the issues noted above.

Local Government Fiscal Effect

If the bill affects local governments, identify which local governments would be affected (e.g., cities, counties, school districts, water districts, etc.). Describe the bill's fiscal effect to the local governments.

As introduced, HB 2656 applies only to school districts and would not have a fiscal effect on Local employer KPERS contributions.

References/Sources

If there are supporting documents or spreadsheets explaining calculations or assumptions, please attach them.