MINUTES

JOINT COMMITTEE ON PENSIONS, INVESTMENTS, AND BENEFITS

September 12, 2016
Room 548-S—Statehouse

Members Present

Senator Jeff King, Chairperson
Representative Steven Johnson, Vice-chairperson
Senator Anthony Hensley
Senator Mitch Holmes
Senator Laura Kelly
Senator Ty Masterson
Representative John Alcala
Representative Daniel Hawkins
Representative Jerry Henry
Representative Charles Macheers
Representative Ed Trimmer

Members Absent

Representative John Edmonds
Representative Gene Suellentrop

Staff Present

J.G. Scott, Kansas Legislative Research Department
Reed Holwegner, Kansas Legislative Research Department
Mark Dapp, Kansas Legislative Research Department
David Wiese, Office of Revisor of Statutes
Gordon Self, Office of Revisor of Statutes
Suzanne Nelson, Committee Assistant

Conferees

Alan Conroy, Executive Director, Kansas Public Employees Retirement System
David Wiese, Assistant Revisor, Office of the Revisor of Statutes
Faith Loretto, Planning and Research Officer, KPERS, and KPERS 457 Plan Manager
Jay Rowh, President, Kansas Silver Haired Legislature
Elaine Frisbie, Vice President for Finance and Administration, Kansas Board of Regents
Curt Kitson, Hays, Kansas, on behalf of his spouse, Jennifer Kitson
Ernie Claudel, Kansas Coalition of Public Retirees and member of the KPERS Board of Trustees
Dale Dennis, Deputy Commissioner for Fiscal and Administrative Services for Kansas Department of Education
Mirta M. Martin, President, Fort Hays State University

Others Attending

See Attached List.

Morning Session

Call to Order, Introductions, and Opening Remarks

Chairperson King called the meeting of the Joint Committee on Pensions, Investments and Benefits to order at 10:15 a.m. Chairperson King welcomed Committee members, conferees, and members of the audience. Senator Ty Masterson joined the meeting by telephone.

2015 Valuation of Kansas Public Employees Retirement System

Alan Conroy, Executive Director, Kansas Public Employees Retirement System (KPERS), provided a review of the 2015 actuarial valuation, which is an annual report of the assets and costs of KPERS as of December 31, 2015 (Attachment 1). The actuarial valuation, different from the market valuation, was $17.409 billion. Actuarial assets are calculated by “smoothing” investment gains and losses over a five-year period. A market value higher than the actuarial value means deferred investment gains will flow through valuations over the subsequent four years. The 2015 market valuation was $16.893 billion. It is the first estimation since 2011 in which the actuarial valuation exceeded the market valuation.

Mr. Conroy discussed legislation that affected the 2015 valuation. Legislation enacted in 2015 (SB 228) authorized the issuance of $1 billion in bonds to reduce the Unfunded Actuarial Liability (UAL) for the State and School group and reset the State and School employer contribution rates from 12.37 percent to 10.91 percent for FY 2016 and for FY 2017 from 13.57 percent to 10.81 percent. The impact of the bond proceeds and contribution rate changes are incorporated in the 2015 valuation and projections.

SB 161 and SB 249 provided for the delay of up to $100 million in State and School employer contributions to KPERS for FY 2016, with full repayment plus 8 percent interest to be made no later than June 30, 2018. Actual delayed contributions from last quarter of FY 2016 were $97.4 million. Valuation results and projections treat the delayed contributions as a long-term receivable on KPERS’ books and assume they are repaid as scheduled with 8 percent interest. The delayed FY 2016 contributions did not affect the 2015 valuation’s projections, but contribution rates in future years will be higher than projected if the contributions are not repaid as planned. Employer contribution rates for Local, KP&F, and Judges groups continue to be at the full actuarial required contribution (ARC) rate. Statute provides State contributions above the ARC rate will be used to fund the School group. The statutory employer rate for State and School FY 2017 is at 99.8 percent, which is only 0.02 percent below the ARC contribution rate.

SB 168 included working-after-retirement changes that will have some effect on future funding and will be discussed in the afternoon session.

Investment return on a market value basis in 2015 was 0.2 percent, but due to asset smoothing, return on an actuarial basis was 7.6 percent. The UAL decreased by $929 million from $9.467 billion to $8.539 billion, primarily due to bond proceeds. Funded status improved for all groups in KPERS with the total funded ratio increasing from 62.3 percent to 67.1 percent.

Assuming all actuarial assumptions and projections are met in the future, KPERS will be fully funded at the end of calendar year 2033.

Representative Ed Trimmer commented that the unfunded liability would increase because, historically, employers have used the excuse that they did not have the money to make the required payment. Mr. Conroy responded that about half of the unfunded liability was created because employers' contribution rates for the last 23 years were at a lower statutory rate, rather than at the ARC rates. The foundational, best practice is to pay the employer contribution rate as determined by the actuary.

Mr. Conroy responded to a question from Representative Steven Johnson regarding the ARC and statutory contribution rate for 2014 and 2015 being the same amounts in the KP&F Plan, advising that the changes were due to more retirees in this valuation period than what had been assumed.

Mr. Conroy answered a question from Senator Mitch Holmes regarding whether the amortization period should be adjusted, adding ten years to the end and who is responsible for that decision. He responded that the Legislature assigns the authority to the KPERS Board of Trustees, which monitors the volatility and other changes, and makes adjustments as the time line nears the end of the current amortization period.

Update on Performance of Bond Proceeds, 2004 and 2015 Series

Mr. Conroy explained that the bonds were invested within a few days after receipt in a mix of publicly-traded stocks and bonds according to KPERS' current target asset allocation mix. Some prudent adjustments were made over time to rebalance the asset mix in domestic equity, private equity, and real estate.

The first year period for August 2015 through August 2016 for investment of the bonds just ended, and the report has not been received yet. Chairperson King requested that Mr. Conroy distribute the report to the Joint Committee when it is complete. Mr. Conroy commented that the 2015 pension obligation bonds were issued at 4.688 percent; over the long term, anything over a 4.7 percent return would outperform the interest cost of the pension obligation bonds (Attachment 2).

Chairperson King asked for some details regarding the investment performance of the bonds during the first two quarters of 2016. Mr. Conroy stated the target range is for an 8 percent return, but so far this calendar year, the return is about 3 to 4 percent.

Overview of 2016 Legislation Enacted

David Wiese, Assistant Revisor, Office of Revisor of Statutes, provided an overview of the provisions of House Sub. for SB 168, which amended several provisions relating to working after retirement for KPERS retirants (Attachment 3).

Implementation of New Provisions: KPERS 457 Roth; 401 (a) Plans; and Data Sharing with KPERS Defined Benefit Plan

Mr. Conroy reminded the Committee members the KPERS 457 Plan is a deferred compensation plan for public employees, which consists of contributions from employees.

Faith Loretto, Planning and Research Officer, KPERS, and KPERS 457 Plan Manager, explained this plan is the "third leg" of the "retirement stool" which allows state and local employees to have a sound retirement consisting of their Social Security income, KPERS benefits, and personal savings. KPERS is currently working on three initiatives to enhance KPERS 457: a Roth 457(b) plan; a KPERS pension data sharing plan with Empower, the current record keeper; and a 401(a) plan option for local employers. KPERS' goal is to present these plans to the Board of Trustees at their September 30, 2016, meeting and to implement them in early calendar year 2017 (Attachment 4).

Recommendations from the Silver Haired Legislature

Jay Rowh, President, Silver Haired Legislator (SHL), from Mitchell County, Kansas, presented recommendations and requests from the SHL on behalf of the half-million Kansas seniors who comprise the highest voting age demographic group in the state. The SHL plans to recommend that the Kansas Legislature fully fund KPERS each year. Mr. Rowh asked that KPERS not be treated as a source of income to subsidize the State General Fund. The SHL also may request a cost of living increase be considered (Attachment 5).

The Committee recessed for lunch at 11:59 a.m.

Afternoon Session

Working After Retirement: Implementation of New Provisions and Related Issues

Mr. Conroy discussed the implementation of new provisions and related issues regarding KPERS working after retirement (WAR) (Attachment 6). He described the old rules effective until the end of FY 2016 (June 30, 2016) and explained that changes had been made because the "temporary" rules for licensed school professionals were initially scheduled to sunset on June 30, 2015, but were extended to June 30, 2016. The Legislature wanted to find a more permanent plan rather than continuing to extend the sunset. Mr. Conroy stressed that the IRS requires a *bona fide* retirement take place before distributions can occur. If an employer pre-arranges with an active member to retire and to return to work as a retiree, this is not a *bona fide* retirement in the eyes of the IRS. Other circumstances, such as reemployment of a retiree as an independent contractor or through a third party, may cause questions about whether a *bona fide* retirement occurred. Mr. Conroy responded to a question from Senator Laura Kelly and provided an example of a third party contractor, *e.g.*, Westar or an independent accountant.

Working after retirement rules permitting employees to simultaneously work and receive benefits encourage earlier retirements, which then have a cost to KPERS. There generally is a shorter period for contributions and a longer period of benefit payouts. In general, there is a higher actuarial liability for retirements occurring sooner after the initial eligibility for benefits.

Regarding provisions of the new WAR policy, Mr. Conroy highlighted the new earnings limitation, which increased from $20,000 to $25,000 beginning July 1, 2016. Employers must report all rehired retirees to KPERS. The employer and employee must certify that no pre-arrangement has occurred. The 60-day waiting period for retirement benefits has not changed. Mr. Conroy also discussed the provisions for grandfathered positions (*e.g.*, licensed school professionals and other retirees) and also great-grandfathered positions (non-licensed) pertaining to rules if rehired by a different employer or the same employer. After reviewing the law with KPERS' tax counsel, it was determined that all employees of KPERS-affiliated employers would be subject to the new WAR rules, even if the position was not a KPERS-covered position. Based on that determination, retirees who return to work for Board of Regents institutions are subject to WAR rules even if they are employed in a position covered by the Regents Mandatory Retirement Plan.

Mr. Conroy responded to a question from Chairperson King regarding the new overtime rule by the U.S. Department of Labor, effective in December 2016, and how it will apply to the $25,000 earnings cap. Mr. Conroy stated the topic has not yet been addressed.

Elaine Frisbie, Vice President for Finance and Administration, Kansas Board of Regents, discussed an impact on the Regents System created by the 2015 and 2016 KPERS WAR legislation (Attachment 7). Ms. Frisbie asked for legislative action creating an exemption to KSA 2016 Supp. 74-4914, so that if a KPERS retiree is hired into a position covered by the Regents Mandatory Retirement Plan, the employee is not impacted by the compensation limitation and the employer is not impacted by the new KPERS contribution requirement.

Curt Kitson, a citizen from Hays, Kansas, appeared on behalf of his wife, Jennifer Kitson. Mrs. Kitson is a Fort Hays State employee, who worked for 23.5 years under KPERS, then worked for 11 years for a non-KPERS employer. She returned to Fort Hays State in 2013, but maintained the TIAA retirement account from her previous employer and has not been a participant in the KPERS retirement system since 2002. Recent changes to WAR rules have had an impact on Mrs. Kitson and whether she can begin drawing her KPERS retirement benefits upon her next birthday in October 2016. This particular scenario has not previously been addressed in the WAR legislation. The Kitsons are seeking answers regarding this situation and asking if legislation can be submitted to the upcoming legislature to provide a waiver or exception for employees who are affected by these circumstances (Attachment 8).

Chairperson King asked if there were any other individuals who would like to ask a question or address the Joint Committee. Ernie Claudel, Kansas Coalition of Public Retirees, and member of the KPERS Board of Trustees (he clarified that he was not speaking on behalf of the Board), presented another issue that he believed has not been addressed. He stated that in the "emergency" section of the WAR legislation, there was a place specifying action when an employer has "emergency" circumstances, but there is no mention of actions for a retiree who might have to return to work because of some catastrophic family situation, such as terminal illness, death of a spouse, or a divorce. Mr. Claudel did not provide written testimony.

Dale M. Dennis, Deputy Commissioner for Fiscal and Administration Services, Kansas State Department of Education, presented an issue that surfaced during his recent talks with three different groups of school superintendents. The superintendents are having problems deciding which group and at what rate their employees should be categorized. Mr. Dennis suggested that the Joint Committee consider creating one category and one rate that would apply to everyone and would simplify the issue. Mr. Dennis did not provide written testimony.

Mirta Martin, President, Fort Hays State University (FHSU), discussed a problem surrounding the 40 individuals at FHSU who are critical for the College of Education and the system it has developed for secondary education. Eighty percent of the school superintendents in Kansas have been educated at FHSU, which has been ranked third in the nation for secondary education.

President Martin stated that while the number may seem small, these 40 individuals are very important to FHSU. This group represents school superintendents, who have attained their Ph.D.s, worked as teachers and superintendents, and have retired in their 50s with many years of their careers ahead of them. FHSU employs these retired superintendents to teach the future generation of teachers and superintendents of Kansas. She said FHSU could have declared an emergency and paid the 30 percent exception surcharge, but this translated to $500,000, which FHSU does not have. Their alternative was to let go of these individuals who have provided an important educational system for Kansas. Since FHSU is the primary university of western Kansas, it must meet the needs of of both western Kansas and the state. If this policy is allowed to continue as it is, it will have significant negative impact on the future of FHSU and the future of teachers in Kansas. FSHU is not in a position to meet the 30 percent exception. President Martin reiterated that while the numbers may seem small, they represent the corpus of an entire college. Strategic plans call for FHSU to continue to grow and to meet not only the needs of western Kansas, but all of Kansas. Resolving this issue is critical to FHSU's survival and success. President Martin did not provide written testimony.

Daniel Klucas, Interim Deputy Secretary of Operations, Kansas Department for Children and Families, submitted written-only testimony, explaining how changes to WAR policy could affect the agency. The Department is in the process of resolving matters with KPERS staff (Attachment 9).

Submission of KPERS Sudan Report

Mr. Conroy presented the Sudan Divestment Report, an annual report published since 2008, which must be filed with the Joint Committee on Pensions, Benefits, and Investments on or before June 30 each year (Attachment 10).

Committee Discussion and Report to the 2017 Legislature

Representative Daniel Hawkins moved to include in the Joint Committee's report to the Legislature a recommendation for a bill to be introduced with language similar to that contained in the Board of Regents' written testimony, which would exempt Regents' schools from certain provisions in Working After Retirement rules and also to give leeway to the Revisors to clarify the proposed language as necessary; seconded by Senator Kelly. The motion carried.

Senator Laura Kelly suggested the issue of emergency provisions for retirees brought by Mr. Claudel be included as a recommendation in the Joint Committee Report.

Representative Steven Johnson suggested a strong recommendation be included in the Joint Committee Report urging payment of the full KPERS ARC contribution, including the $97 million delay FY 2016 contributions plus 8 percent interest.

Chairperson King suggested a recommendation that would include setting a goal for the State to be contributing its scheduled ARC payment by FY 2020.

Adjourn

Chairperson King and Representative Johnson thanked the KPERS staff, the members of the Joint Committee, the visitors in the audience, and the conferees who have made contributions to get the Retirement System where it is today.

The meeting adjourned at 2:45 p.m.

Prepared by Suzanne Nelson
Edited by Reed Holwegner

Approved by the Committee on:

____December 23, 2016________
(Date)