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Laura Kelly, Governor

May 5, 2021

The Honorable Steven Johnson, Chairperson
House Committee on Insurance and Pensions
Statehouse, Room 276A-W
Topeka, Kansas 66612

Dear Representative Johnson:

SUBJECT: Fiscal Note for HB 2289 by Representative Miller

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2289 is respectfully submitted to your committee.

HB 2289 would authorize the Kansas Development Finance Authority (KDFA) to issue pension obligation bonds, in one or more series, in an amount not to exceed $1.0 billion, plus all amounts required to pay the costs of issuance. Proceeds from those bonds must be applied to the unfunded actuarial pension liability (UAL) of the Kansas Public Employees Retirement System (KPERS) School Group. The interest rate of those bonds could not exceed 5.0 percent. No bonds could be issued without the approval of the State Finance Council, which could give approval while the Legislature is in session. The bonds issued and interest owed would be an obligation of KDFA and not KPERS. The bonds issued would not be considered a debt or obligation of the State for purposes of the *Kansas Constitution*. The Department of Administration and the KDFA would be permitted to enter into contracts to implement the payment arrangements after the bonds are issued.

In addition, the bill would provide that investment earnings above the debt service payment on the bonds would be used to fund a 13th check benefit for eligible retirees and beneficiaries retired as of July 1, 2011, and the retirement benefit could not exceed $2,000 before considering any reductions for lump sum and survivor benefit options. The additional payment would be made by KPERS from the KPERS Trust Fund beginning October 1, 2023, and on October 1 of each subsequent year. The following steps would outline the calculation of the annual dividend:

1. Calculate the net investment earnings on the bond proceeds for the immediately preceding fiscal year;
2. Subtract the debt service cost for the same fiscal year from step 1;
3. Divide the amount in step 2 by the total number of eligible retirants and beneficiaries;
4. If the retirant dividend calculation in step 3 is less than $25 per person, no dividend would be payable for that year.

According to KDFA, current interest rates for a $1.0 billion 30-year bond issue are approximately 3.0 percent. When factoring all costs associated with the bonds and giving KPERS net proceeds of $1.0 billion, annual debt service payments totaling $49.8 million would be required with a 3.0 percent interest rate. KDFA notes that a 4.0 percent interest rate would require annual debt service payments of $55.9 million. The bill would cap the interest rate of the bonds at 5.0 percent. The Division of the Budget notes that depending on the timing of the bond issuance, an appropriation from the State General Fund would be required in FY 2022 for the full amount, or for a partial amount if the bonds are issued after July 1, 2021.

For its calculations, KPERS estimates that bond proceeds would be received in December 2021 and would immediately increase the system's assets. KPERS notes that the bill provides for a stream of future dividends to be paid to eligible members beginning in October 2023. The liabilities attributable to the future payments would be reflected in the actuarial valuations. The increase in actuarial liability of the future dividends partially offsets the reduction in the UAL from the bond proceeds. The following estimates have accounted for this reduction.

With the $1.0 billion in bond proceeds deposited in December 2021, KPERS estimates the State/School Group funded ratio would improve by 2.8 percent in the 2021 KPERS Actuarial Valuation (increased from 71.9 percent to 74.7 percent). The funded ratio would stay approximately 2.5 percent above the current baseline until the UAL is fully funded in calendar year 2024. The State/School Group employer contribution rate is expected to decrease by approximately 1.21 percent in FY 2024, reducing from 13.69 percent to 12.48 percent. KPERS estimates the total State/School Group employer contributions would reduce by approximately $63.0 million. Using the Division of the Budget's projected current State General Fund ratio of FY 2024 employer contribution of 84.5 percent, this would be a savings of approximately $53.2 million from the State General Fund.

The amount of the dividend check to KPERS retirees and beneficiaries would depend on the market performance above the debt service of the bonds and cannot be estimated. Any fiscal effect associated with HB 2289 is not reflected in *The FY 2022 Governor's Budget Report*.

Sincerely,

Adam Proffitt
Director of the Budget

cc: Jarod Waltner, KPERS
Jeff Scannell, Department of Administration
Bonnie Hawkins, KDFA