Kansas Public Employees Retirement System Omnibus Bill (Including New Tier 3 Plan); Senate Sub. for Sub. for HB 2333

Senate Sub. for Sub. for HB 2333 is the designated Kansas Public Employees Retirement System (KPERS) Omnibus bill for 2012, containing numerous new provisions and modified provisions of the retirement as well as death and long-term disability statutes administered by the KPERS Board of Trustees (KPERS Board).

This year's KPERS omnibus legislation makes changes in retirement benefits, requires both employee and employer increased KPERS contributions, and makes numerous other adjustments to the plans. The KPERS legislation will enhance funding of the retirement plans; establish a new plan design and new tier for most future KPERS eligible employees; close Tier 2 to most new employees and limit KPERS Tier 2 to only certain specified future state correctional members; and give the Legislature additional power to modify the KPERS plan design features for the new tier.

Senate Sub. for Sub. for HB 2333 amends the current KPERS plan design (Tiers 1 and 2), including provisions for the correctional subclass of the state group. The bill also adds a new plan design (Tier 3—Cash Balance plan) for most future members of the state, school, and local public employee groups. Both employer and employee KPERS contributions for Tier 1 and Tier 2 will be increased to help address the unfunded actuarial liability. The bill generally does not address the Kansas Police and Firemen's Retirement System or the Retirement System for Judges, separate plans also administered by KPERS.

Making Major Changes in KPERS

The omnibus bill implements the following major changes:

- Adds a Cash Balance plan to be established as a new Tier 3 within the existing KPERS defined benefit plans, effective January 1, 2015;
- Provides for death and long-term disability insurance that would continue coverage as long as the active Tier 3 member is working for a participating employer;
- Includes revenue enhancing (increased employer and employee contributions) provisions to be implemented beginning July 1, 2014, to address the Tier 1 and Tier 2 unfunded actuarial liability;
- Requires use of a single, actuarially-determined employer contribution rate covering all three KPERS tiers and calculated for each KPERS group, subject to new, higher statutory annual caps on increased participating employer contributions;
- Extends for three years to July 1, 2015, a salary cap exemption for school professionals who go back to work after retiring from KPERS and are employed full time by the same KPERS participating employer who will continue to pay a special KPERS contribution rate for retired members;

- Changes the basis of calculation for legislator KPERS retirement benefits and contributions based on reducing the annual period from 372 days to 365 days; and

- Provides for a fourth quarter moratorium (April 1 to June 30) in FY 2012 for KPERS participating employers' contributions to the death and long-term disability program.

Establishing a Cash Balance Plan Design

The bill establishes a Cash Balance plan as Tier 3 within the existing KPERS structure for most future KPERS members. The Cash Balance plan is a type of Defined Benefit plan design under federal law. The components of the KPERS legislation include:

- Establishing Tier 3 in KPERS as a Cash Balance plan with the following design characteristics:
  - Tier 3 start date - January 1, 2015;
  - Normal retirement age - age 65 and five years of service, or age 60 and 30 years of service;
  - Minimum interest crediting rate during active years - 5.25 percent;
  - Discretionary Tier 3 dividends - 4.0 percent maximum; modified formula based on KPERS funded ratio for awarding discretionary credits, meaning when all plans reach an 80.0 percent funded ratio, then the KPERS Board must pay Tier 3 dividends;
  - Employee contribution - 6.0 percent;
  - Employer service credit - 3.0 percent for less than five years of service; 4.0 percent for at least five, but less than 12 years of service; 5.0 percent year for at least 12, but less than 24 years of service; and 6.0 percent for 24 or more years of service;
  - Vesting - five years;
  - Termination before vesting - interest would be paid for the first two years if employee contributions are not withdrawn;
  - Termination after vesting - option to leave contributions and draw retirement benefits when eligible, or withdraw employee contributions and interest, but forfeit all employer credits and service;
  - Death prior to retirement - five-year service requirement and, if spouse had been named primary beneficiary, provide retirement benefit for spouse when eligible;
  - Tier 3 early retirement - age 55 and ten years of service;
  - Default form of retirement distribution - single life with ten-year certain;
  - Annuity conversion factor - 6.0 percent;
  - Benefits option - partial lump sum paid in any percentage or dollar amount up to 30.0 percent maximum;

    - Post retirement benefit - cost-of-living adjustment (COLA) may be self-funded;
    - Electronic and written statements - KPERS Board shall provide information specified. Certain quarterly reporting will be required;
    - Powers reserved to adjust plan design - The Legislature may prospectively change interest credits, employer credits, and annuity interest rates. The KPERS Board may prospectively change mortality rates;
    - Actuarial cost of any legislation - fiscal impact assessment by KPERS Actuary required before and after any legislative enactments;
    - Divorce after retirement - allow a retirant, if divorced after retirement, and if the retirant had named the retirant's ex-spouse as a joint annuitant, to cancel the joint annuitant's benefit option in accordance with a court order;
    - If a member becomes disabled while actively working, such member shall be given participating service credit for the entire period of the member's disability. Such member's account shall be credited with both the employee contribution and the employer credit until the earliest of (i) death; (ii) attainment of normal retirement age; or (iii) the date the member is no longer entitled to receive disability benefits;
    - A benefit of $4,000 is payable upon a retired member's death; and
    - Require employer credits and the guaranteed interest crediting to be reported quarterly.

Modifying the Current KPERS Plans To Increase Revenue

Other components of the KPERS legislation include:

- Modifying Tier 1 and Tier 2 provisions in the current plan design for each, as follows:
    - Allow Tier 1 election (if the Internal Revenue [IRS] approves) in choosing changes in plan design - either continue employee contribution of 4.0 percent and have the multiplier reduced from 1.75 percent to 1.4 percent for future service, or increase the employee contribution from 4.0 percent to 6.0 percent and have the multiplier increased to 1.85 percent for future service (default option if IRS fails to approve election);
    - Eliminate Tier 2 COLA and provide an increase in the multiplier from 1.75 percent to 1.85 percent retroactive to July 1, 2009, (if eligible) as well as future service years;
    - Permit future new members to join Tier 2 after December 31, 2014, if they are eligible KPERS members in the correctional officer subclass, and
    - Increase caps on all participating KPERS employer contributions for the state, school, and local groups, with the cap increasing to 0.9 percent in FY 2014, 1.0 percent in FY 2015, 1.1 percent in FY 2016, and 1.2 percent in FY 2017.

Other Revenue Enhancing Measures and Expenditures

Additional components of the KPERS legislation include:

- Crediting 50.0 percent annually to the KPERS Trust Fund, commencing quarterly transfers in FY 2014, from the Expanded Lottery Act Reserve Fund, after other obligations totaling $10.5 million have been met;

- Transferring 80.0 percent from the sale of certain specified state property to the KPERS Trust Fund beginning July 1, 2012;

- Allowing investment returns after certain thresholds are met and which are not awarded as dividends in Tier 3 for be used in paying down the unfunded actuarial liability;

- Using a single, actuarially-determined employer contribution rate covering all three KPERS tiers and calculated for each KPERS group, subject to new, higher statutory annual caps on increased participating employer contributions; and

- Adding $2.75 million from the KPERS Fund and 11.0 FTE positions to begin implementing the new provisions in FY 2013.