

# New Legislation Is Meaningful Step Toward Retirement Funding Solution

*KPERS has worked to address a fundamental long-term funding shortfall over the last decade. Legislation passed in 2011 will be a meaningful and cooperative step toward long-term sustainability, shared between employers and public employees. While the shortfall will continue to grow in the near-term, projections show funding should begin to improve after several years of increased contributions and lower benefit liabilities.*

## Funding Outlook and Projections

The Retirement System's most recent actuarial valuation shows an \$8.3 billion unfunded actuarial liability (UAL), returning it to the same level as in the 2008 valuation. KPERS' new funded ratio is 62 percent, down somewhat from 64 percent the year before. The UAL is the gap between the actuarial value of assets and the actuarial liability for service already earned by public employees. This UAL is amortized over a 40-year period, which began in 1993. The funded ratio is the ratio of assets to future liabilities. For public pension plans like KPERS, funding over 80 percent and rising is good. Funding below 60 percent is poor and needs prompt attention.

The modest decline in funding is in spite of recent strong investment performance. KPERS' portfolio returned 13 percent for calendar year 2010. Preliminary numbers show the System is on target for a 22 percent return for fiscal year 2011.

This continues to demonstrate KPERS' fundamental, long-term shortfall. Even with a yearly 8 percent return, the UAL will continue to increase in the coming years.

- KPERS will continue to absorb significant 2008 losses over the next two years.
- Employers are not contributing at the required rate.

## Reasons for the Funding Shortfall

- Benefit increases in the 1990s, funded mostly through actuarial changes that put off paying for them until later.
- Employers haven't contributed at the required rate for over 16 years.
- The recession caused large investment losses.
- Members living longer and members retiring earlier under the 85 point rule have increased liabilities.



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## KPERS at a Glance

Total Members	279,000
retirees	77,000
actives	161,000
inactives	41,000
Ave Monthly Benefit	\$1,024
Annual Benefits Paid	\$1.3 billion
Annual Contributions	\$870 million
Assets	\$11.9 billion 9/30/11
1-yr Investment Return Ave	13% (CY 2010)  22.6% (FY 2011)
25-yr Investment Return Ave	8.5%

## Earlier Efforts

Over the last decade, addressing the long-term funding shortfall has been KPERS' highest priority. We partnered with the Legislature and Governor to develop and implement a long-term plan. Key steps included a series of employer contribution rate increases, issuing pension obligation bonds, making actuarial changes, and adopting a new plan design for new members starting July 1, 2009.

These efforts began to improve KPERS' funding projections. However, unprecedented investment market declines in 2008 due to the financial crisis had a substantial negative impact, reversing the progress made in previous years. In the aftermath, KPERS again worked with the Legislature's Joint Committee on Pensions, Investments and Benefits and other committees to develop a range of options to address the continuing problem.

## 2011 Legislation Passed and Signed

In response to KPERS' long-term funding shortfall, the 2011 Legislature made changes to future benefits and contributions, affecting both working members and employers. Beginning in 2014, employers will have a series of contribution increases until they reach the actuarially required rate. Members (depending on tier and a possible option election), will have contribution increases or benefit decreases. These changes are a major step toward making KPERS more sustainable and helping to pay promised benefits long-term.

The Governor signed Senate Substitute for HB 2194 into law, but there are still steps to complete before the changes can take effect in 2014, including a KPERS study commission during the legislative interim and legislation for consideration during the 2012 session. Without these steps completed, the law will not take effect.

## Funding Projections With New Legislation

If the 2011 legislation is fully implemented, the KPERS consulting actuary estimates the funded ratio will begin to improve in the coming years.

The School group will be in actuarial balance sooner. Employer contribution rates will eventually be lower than they would have been otherwise, providing significant savings over the UAL amortization period.

The cumulative effect of higher employer and employee contribution rates, along with lower liabilities from benefit decreases, are projected to begin lowering the UAL in the next several years. It will then continue to decrease until it is paid in full by 2033, when actuarial projections show KPERS with

a 100 percent funded ratio. The new legislation will not affect the length of the UAL's amortization period, but it does lower the long-term cost of full funding.

- State/School group saves \$2.9 billion
- Local group saves \$636 million

To meet these projections, long-term investment returns are crucial. KPERS has used an 8 percent return assumption since 1986 and has achieved an 8.5 percent average over those 25 years. However, over the next decade the System will be especially vulnerable to future economic downturns that could cause investment returns to decline.

## KPERS Study Commission

Substitute for HB 2194 established a 13-member study commission to consider alternative plan designs and to recommend a plan to the Legislature for the long-term sustainability of the System. The study commission will review various options including defined contribution plans, hybrid plans that could include a defined contribution component, and other possible plans.

Of the 13 members, five are appointed by the Governor, four are to be legislators, and the remaining four are at-large members appointed by the Legislature.

KPERS staff, board and actuary will continue to provide timely information and analysis to support the Legislature and the KPERS Study Commission in their consideration of various policy options. As a fiduciary devoted to the best long-term financial interest of members, we will also continue to advocate for policies that promote the financial health of the Retirement System.