MEMORANDUM

To: House Financial Institutions and Pensions Committee

From: Alan D. Conroy, Executive Director

Date: February 5, 2025

Subject: Informational Testimony on House Bill 2129

House Bill 2129 modifies the retirement plan design for teachers at local school districts, community colleges, and technical colleges. The changes will affect plan funding and require additional administrative resources.

Current Plan Design

KPERS has three membership groups:

1. KPERS 1 – Members started before July 1, 2009.
2. KPERS 2 – Members started from July 1, 2009, to December 31, 2014.
3. KPERS 3 – Members started after January 1, 2015.

KPERS 1 and KPERS 2 are traditional defined benefit plans, where retirement benefits are calculated using a formula:

Years of Service × Final Average Salary × Multiplier

Members contribute 6% of pay, while employers contribute an actuarially determined rate to fund benefits (11.68% in FY 2026 for State/School employers).

KPERS 3 is a cash balance plan. Members contribute 6% of pay to notional accounts that earn a guaranteed 4% interest annually, with potential dividend interest based on a five-year net average return formula. Members also earn employer pay credits totaling 3%–6% of pay based on years of service, and these contributions also earn the 4% guaranteed interest plus potential dividends. At retirement, KPERS 3 account balances are converted to a lifetime annuity.

The employer contribution rate is the same across KPERS 1, KPERS 2, and KPERS 3.

KPERS

House Bill 2129

HB 2129 would reopen the KPERS 2 plan to teachers on July 1, 2025. The bill defines teachers as:

- Any certified professional employee who is required to hold a certificate to teach in any school district.
- Any teacher or instructor in any technical college or community college.

Teachers currently enrolled in KPERS 3 would transfer to KPERS 2 by January 1, 2026. Their retirement benefit would be calculated under KPERS 2 rules, but if their KPERS 3 benefit would have been higher, they would receive the greater amount.

KPERS 2 and KPERS 3 Benefit Comparison

The KPERS 2 and KPERS 3 plan designs are not expected to provide the same level of benefits. The ultimate benefit a member earns is highly dependent on individual circumstances (e.g., starting salary, salary progression, years of service), so it is not possible to provide a single comparison that can be applied to every member's scenario.

Using a simplified set of assumptions and calculations, we estimated the benefit for a 30-year teacher who retires at age 60 under KPERS 2 and KPERS 3. The results are summarized in the following table:

KPERS 2 and KPERS 3 Benefit Comparison 30-year Teacher, Retiring at Age 60			
	KPERS 2	KPERS 3 4% guarantee only	KPERS 3 4% guarantee + 2% dividend
Retirement Benefit 10-Year Life Certain Benefit Option	$45,015	$26,978	$36,866
Difference from KPERS 2 Benefit	$ -	$(18,037)	$(8,149)

In this example, KPERS 2 provides a higher benefit than KPERS 3. However, different assumptions may yield different results. While KPERS 2 is expected to provide higher benefits in most cases, there are situations where KPERS 3 could result in a greater benefit.

Replacement Ratio Comparison
Another way to compare benefits is through a replacement ratio, which expresses a retiree's expected benefit as a percentage of their final salary before retirement.

KPERS' actuary analyzed replacement ratios under four scenarios:
- Career employee (30 years of service, age 35-65)
- Early career employee (10 years of service, age 25-35)
- Mid-career employee (20 years of service, age 30-50)
- Late career employee (20 years of service, age 45-65)

These four scenarios all have the same set of underlying assumptions, except for the period worked as a public employee.

Like the earlier example, KPERS 2 generally provides a higher benefit than KPERS 3. However, for members who leave KPERS-covered employment early in their careers, KPERS 3 may provide a higher benefit. In such cases, the KPERS benefit would likely be a smaller part of their overall retirement planning compared to career public employees.

A replacement ratio comparison graph is attached to this memorandum.

Actuarial Costs
Changing the benefit plan design for teachers impacts KPERS funding in two key ways:

1. Increase in Unfunded Actuarial Liability (UAL) – The total liability increases without a corresponding increase in assets.
2. Increase in Normal Cost – The cost of benefits allocated to each fiscal year rises.

Unfunded Actuarial Liability
Moving KPERS 3 teacher members to KPERS 2 increases the unfunded actuarial liability by $220 million. This reflects the higher total liability expected for this group under the KPERS 2 benefit design.

The increase can be funded in two ways:
- **One-time payment:** A lump sum of $220 million eliminates any unfunded actuarial liability.
- **Amortization:** Spreading the cost over multiple years results in an increase in the employer contribution rate. KPERS' consulting actuary estimates that a 20-year amortization would increase the employer contribution rate by 0.31%, or approximately $18.3 million annually based on the current State/School payroll.

Normal Cost
The normal cost represents the total cost of benefits allocated to each year by the actuary. If benefits increase, the normal cost is expected to increase as well.

Under HB 2129, the normal cost increases due to the shift to KPERS 2, which has a higher expected benefit than KPERS 3. The estimated increase is in the normal cost is 0.42%, which translates to an additional $24.8 million in FY 2026 based on the current State/School payroll. This increase is permanent and separate from the UAL funding impact.

The following table summarizes the expected impact on State/School funding and State/School employer contribution rates based on the provisions of HB 2129:

HB 2129 Actuarial Impact - State/School Group ($ millions)				
	Baseline	HB 2129	Change	Additional FY 2026 Contributions
Actuarial Liability	$24,956	$25,176	$220	
Actuarial Value of Assets	18,755	18,755	0	
Unfunded Actuarial Liability	$6,201	$6,421	$220	
Funded Ratio	75.2%	74.5%	(0.7%)	
Employer Normal Cost Rate	2.83%	3.25%	0.42%	$24.8
Unfunded Actuarial Liability Contribution Rate	8.85%	9.16%	0.31%	$18.3
Actuarial Contribution Rate	11.68%	12.41%	0.73%	$43.0

HB 2129 does not include a funding mechanism for these plan design changes. Under current law, the employer contribution rates for FY 2026 would increase as outlined above to cover the cost of these changes.

Administrative Costs
Reopening the KPERS 2 plan for teachers will have a significant impact on plan administration. Because KPERS does not track position data, the total number of affected teachers is unknown. Using teacher counts from Department of Education data, KPERS estimates 43,593 "teachers" including 19,096 current KPERS 3 members. This does not include inactive teacher members who would also convert to KPERS 2.

Implementing HB 2129 requires both technical updates to the pension administration system and extensive data collection on teachers, information KPERS does not currently track. Additionally, the transition will involve educational and communication efforts for affected members.

KPERS 2 is a fundamentally different plan than the KPERS 3 cash balance plan. While the KPERS 2 technical structure remains in the pension administration system, converting members from KPERS 3 to KPERS 2 requires major system changes to accurately establish salary and service time for KPERS 2 benefit calculations. The system must also be modified to allow KPERS to compare KPERS 2 and KPERS 3 benefits, ensuring that no member receives a lower benefit due to this transition.

KPERS estimates $1.0 million in technical system updates and testing, requiring six months to complete. Additional staffing is needed for identifying teacher members and assisting with member education:

- 5.0 temporary FTE (staffing in Benefits & Member Services Division)
    - 3.0 temporary benefits analysts
    - 2.0 temporary benefits representatives

- Estimated salary and benefits costs for these five positions totals:
    - $373,158 in FY 2026
    - $389,211 in FY 2027

Implementation Timing
HB 2129 establishes two key implementation dates:
- July 1, 2025 – All new teacher members will be enrolled in KPERS 2.
- January 1, 2026 – All existing KPERS 3 teacher members will be converted to KPERS 2.

Given the significant development, testing, and manual data efforts required to identify eligible active and inactive members, this timeline will be challenging to meet.

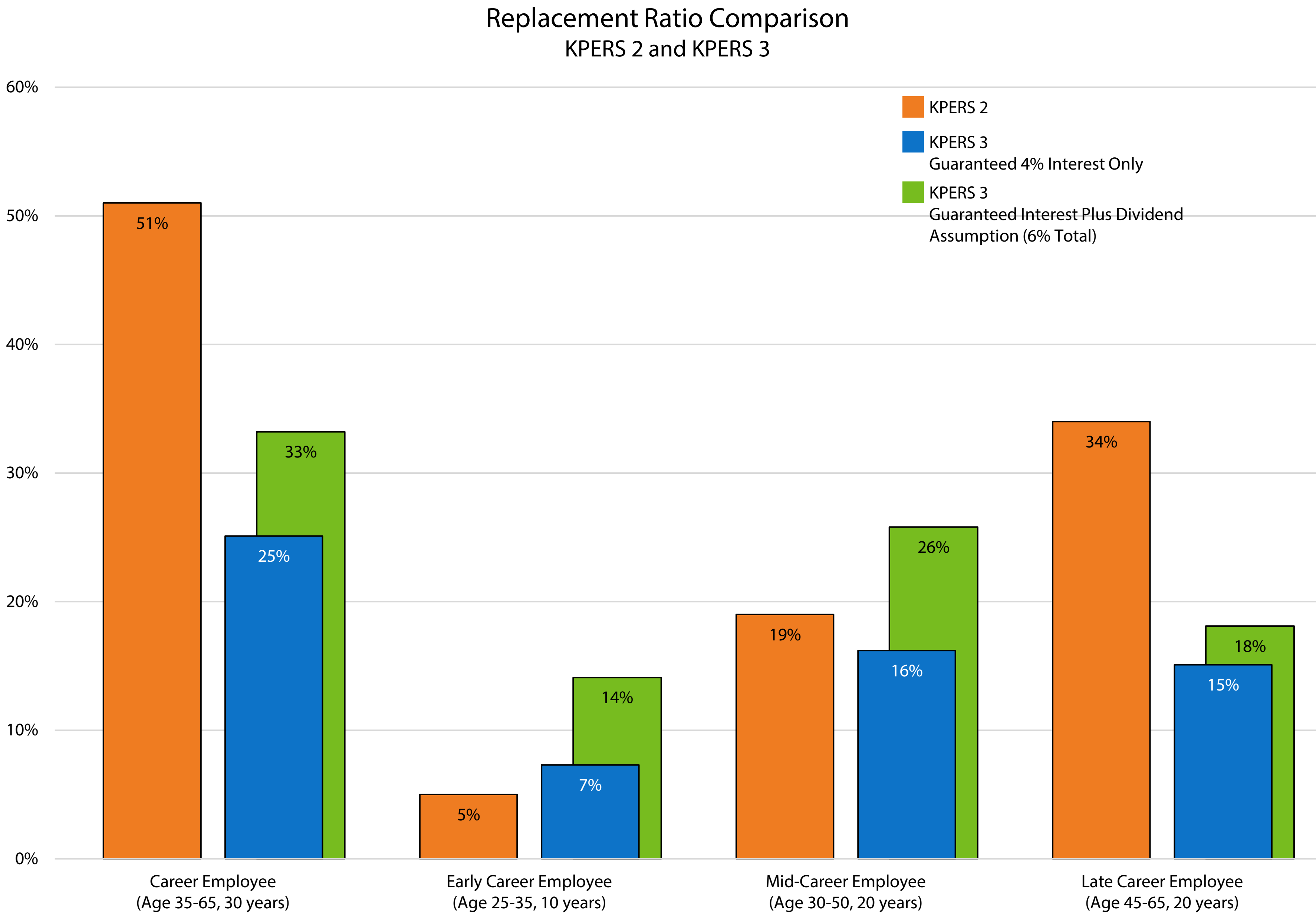
If HB 2129 moves forward, we request delaying the conversion of existing KPERS 3 members by six months (to July 1, 2026) to allow sufficient time for proper implementation.

Additionally, HB 2129 could be amended to include a provision ensuring that any teacher member retiring after a specified date (e.g., July 1, 2025, or January 1, 2026) would have their benefit calculated under KPERS 2, if that aligns with the Legislature's intent.

I would be pleased to respond to any questions the Committee may have.

Attachment

Attachment A



All scenarios assume that the member retires at age 65 and reflects the current set of actuarial assumption, including the 7.0% investment return assumption.

February 2025