# Amortizing KPERS’ Unfunded Actuarial Liability

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KPERS

Kansas Association of School Boards

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# KPERS Funding

- Steady Progress
- Current funding plan

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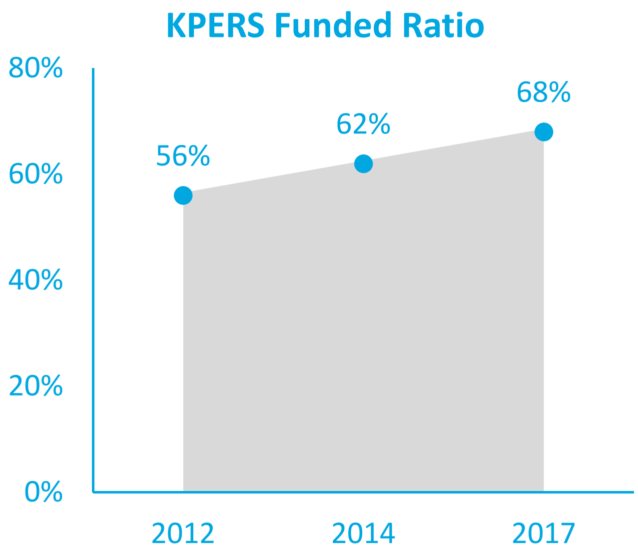
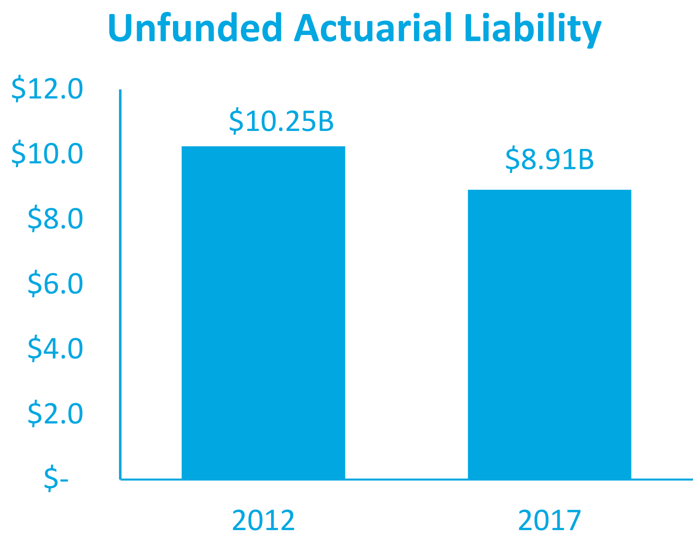
# KPERS Funding

## Steady Funding Progress

- Generally, KPERS funding is slowly improving and headed in the right direction.
- KPERS is on target to pay off the legacy unfunded liability in 2033.
- The Board of Trustees adopted a more conservative investment return assumption in 2016, moving from 8% to 7.75%. This change caused an increase in the calculation of liabilities, but positive investment returns kept the funded ratio stable.



# KPERS Funding

## Funding the unfunded liability

- The System has a funding plan to fully fund the System.
- The Legislature set a 40-year, closed amortization period in 1993.
- The Board of Trustees approved a layered amortization approach as part of the last triennial experience study.
  - The existing unfunded liability (legacy unfunded liability) remains on the 40-year amortization schedule, ending in 2033.
  - Each year any experience different than the actuarial assumptions (either positive or negative) will be realized in separate 20-year amortization periods.
  - Each layer will have an annual "payment" calculated and each layer's payment is added together to calculate a single unfunded liability payment.

# KPERS Funding

## Funding the unfunded liability

- "Level percent of pay" amortization methodology results in an increase in the dollar amount of unfunded actuarial liability over more than half of amortization period, even if full actuarial required contribution rate is paid.

- The current amortization schedule on the legacy unfunded actuarial liability has 15 years remaining and is at the point where contributions are paying the principle of the unfunded liability.

- The legacy unfunded actuarial liability is projected to continue declining each year if full actuarial required contribution rate is paid and all assumptions are met.

# Governor’s Budget Recommendation

- Current amortization policy
- Re-amortized unfunded actuarial liability
- Eliminate additional payments
- Actuarial cost projections

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# Governor’s Budget

## Current amortization policy

- The Legislature set the original 40-year, closed period amortization schedule in 1993.

- Amortization policy was subsequently delegated to the KPERS Board of Trustees.

- In 1993, longer amortization periods were more common.
  - Over time, actuarial standards have recommended shorter amortization periods.
  - The current best practice is a layered amortization approach, which the Board of Trustees adopted starting in the 12/31/2016 actuarial valuation.

# Governor's Budget

## Re-amortize the unfunded actuarial liability

- 15 years remain on the original 40-year amortization schedule that was set in 1993 (ending in 2033) on the legacy unfunded actuarial liability.

- The Governor is recommend re-amortizing the legacy unfunded actuarial liability to 30-year as of 12/31/2016.
  - By statute, the 12/31/2016 valuation set employer contribution rates for FY 2020.

- KPERS understanding is that the layered amortization established in the 12/31/2016 actuarial valuation and going forward remains in place.

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# Governor’s Budget

## Eliminate additional payments

- The Governor’s recommendation includes eliminating the additional contributions that have been created in the past two legislative sessions.
  - No payment of the remaining 18 payments on the 20-year payment of $64 million in delayed FY 2017 contributions ($51.2 million).
  - No payment of the $194 million delay approved for FY 2019.
  - No payment of the $56 million contingent contribution passed in FY 2019.
- $301 million in total recommended contribution reductions.
- The payments are accounted for in the current actuarial valuation and funding projections because the payment language was included in budget bills passed by the Legislature and signed by the Governor.

# Governor's Budget

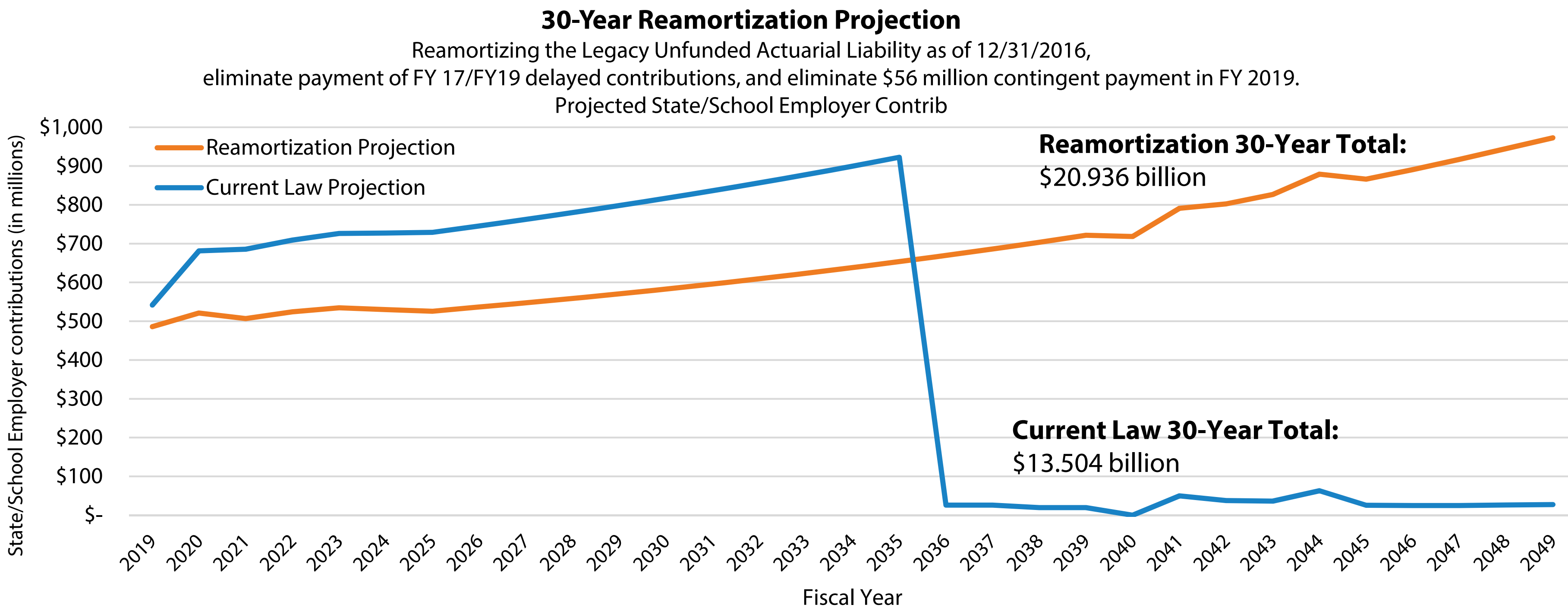
## Actuarial cost projections

- An extension of the amortization period lowers the actuarial required contributions in the near term, but requires much higher contributions in future years.

- The Governor's recommendation, as KPERS understands it, is projected to:
  - Reduce required contributions by approximately $770 million in the first five years, but increase total required employer contributions over 30-years by $7.4 billion ($13.5 billion under the baseline, $20.9 billion with re-amortization).
  - Keep KPERS State/School funded ratio below 80% for an additional 12 years (2026 under the baseline, 2038 with re-amortization).
  - Keep the unfunded actuarial liability above $6 billion until 2036, two year after the unfunded actuarial liability is schedule to be fully paid under current law.

# Governor's Budget

## Actuarial cost projections

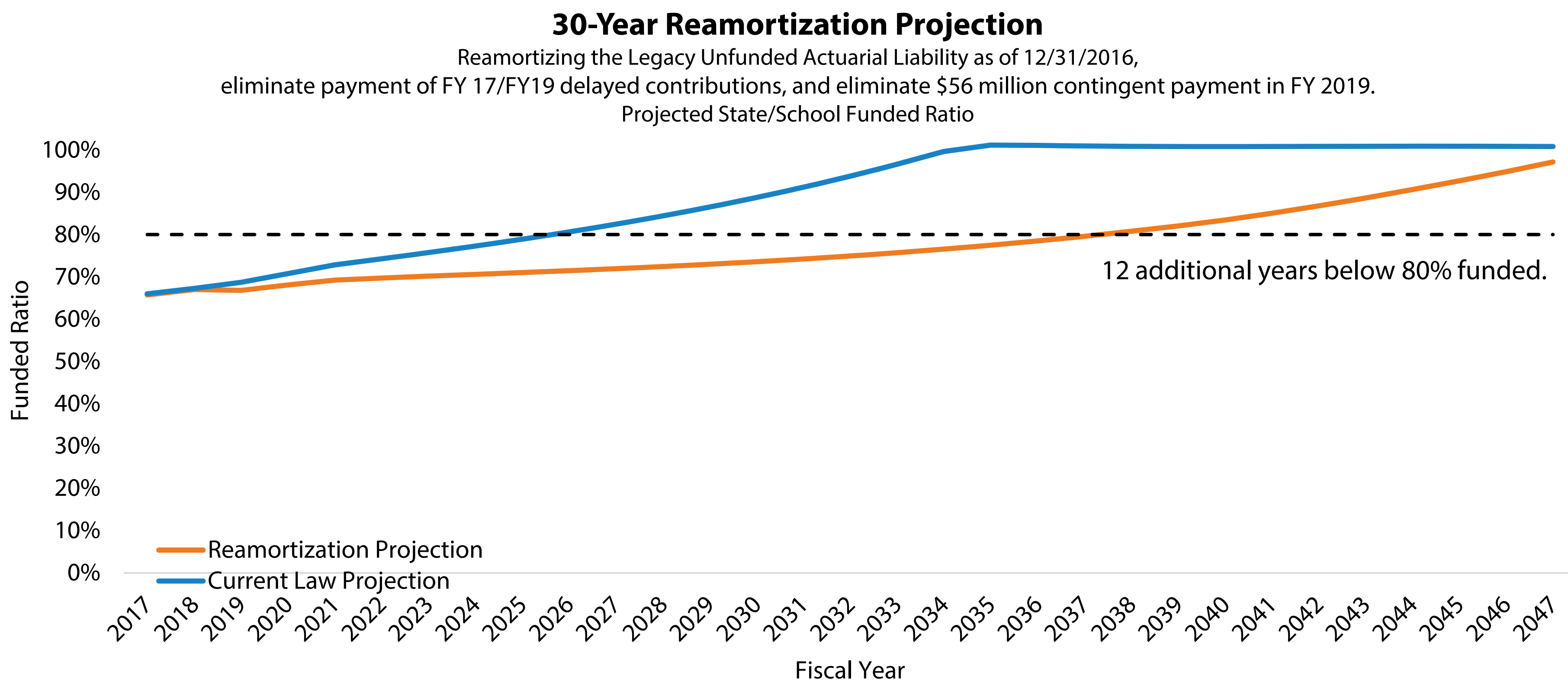



Current law employer contributions include:
1. The payment of delayed contributions in FY 2017 ($6.4 million annually from FY 2018-FY 2038) and FY 2019 ($19.4 million from FY 2020-FY 2040).
2. Additional payments of $56 million in FY 2018 (already received), $82 million in FY 2019 (already received) and $56 million in FY 2019 (contingent on actual receipts).

The reamortization projection is based on a 30-year amortization (FY 2020-FY 2050) of the legacy unfunded actuarial liability that existed on 12/31/2016. Changes to the unfunded actuarial liability due to actual experience since 12/31/2015 are given an annual 20-year amortization "layer" based on the amortization method approved by the KPERS Board of Trustees as part of the most recent Triennial Experience Study.

# Governor's Budget

## Actuarial cost projections

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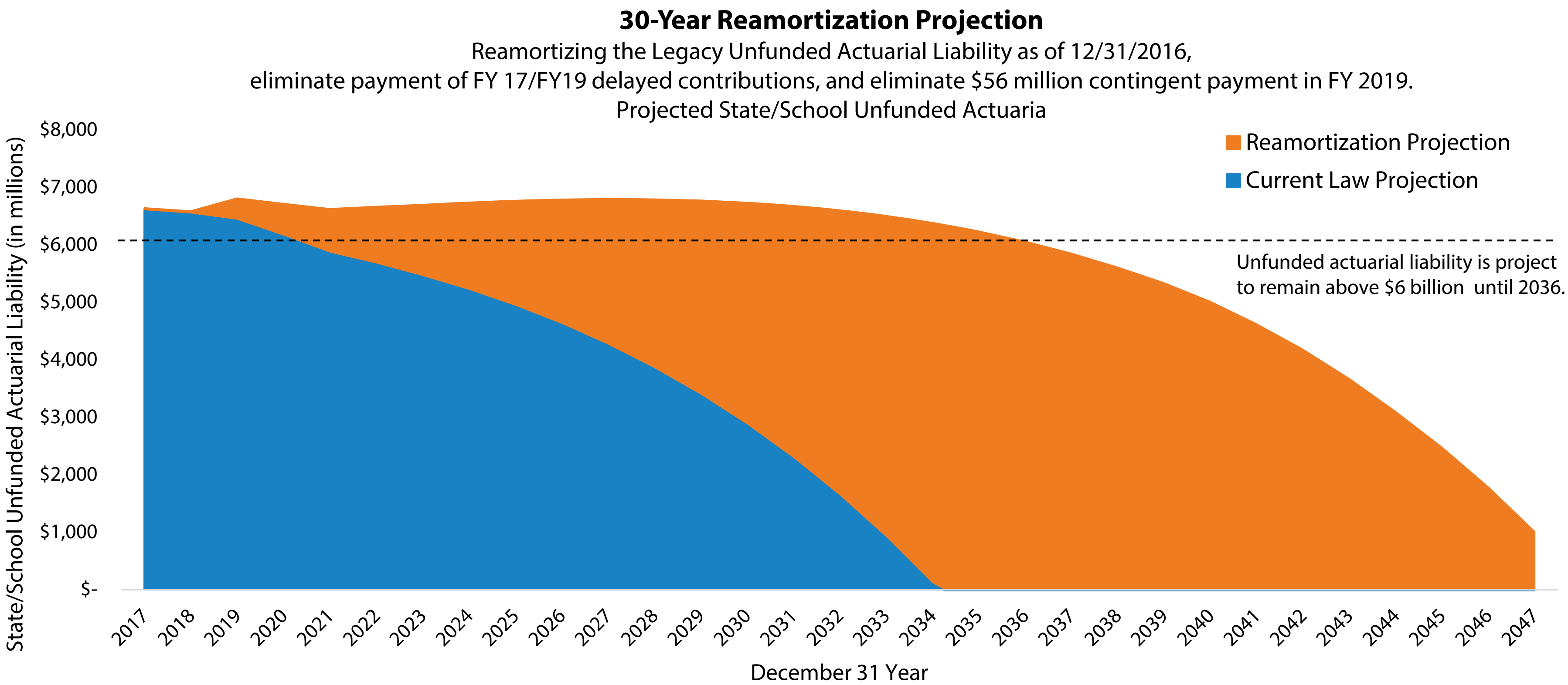
# Governor's Budget

## Actuarial cost projections

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# Governor’s Budget

## Amortization policy

- By statute, amortization policy is a delegated duty of the Board of Trustees.
- The current amortization schedule has reached the point where the Board would begin reviewing amortization options as part of their next triennial experience study process, which is scheduled to occur in 2019.
- The Board, with the help of the KPERS’ consulting actuary, will review many amortization options.
- The focus of the amortization discussions, from the Board’s perspective as fiduciaries to KPERS members, will be on creating a funding policy that:
  - Maintains consistent funding improvement;
  - Minimizes volatility in employer contributions as much as possible; and
  - Ensures reasonable allocation of costs to current and future generations.

# Conclusions

- KPERS funding has been improving over the last decade.

- KPERS has a funding policy in place to extinguish the remaining unfunded actuarial liability.

- Consistent full payment of the actuarial required contribution will have the most impact on continued improvement.

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# Conclusions

- Extending the current amortization schedule lowers contributions in the short term, but increases long-term contributions and keep KPERS vulnerable to volatile market conditions for many years.

- The Board of Trustees will be reviewing amortization policy in 2019 and in future years to ensure continued funding progress while minimizing contribution volatility.

# Questions?

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