# MEMORANDUM

To: Board of Trustees

From: Jarod Waltner, Planning and Research Officer
Alan D. Conroy, Executive Director
Judy McNeal, Chief Fiscal Officer

Date: January 18, 2019

Subject: Governor's FY 2019, FY 2020 and FY 2021 Budget Recommendation

The Governor's Budget Report was released on January 17, 2019. The Budget Report includes the recommended administrative budgets for State agencies for FY 2019 and FY 2020, as well larger budget policies recommended by the Governor.

## KPERS Operating Budget

The Governor's recommendation for KPERS operating expenditures is unchanged from the request that Trustees approved during the September 2018 Board meeting. The Governor's recommended expenditures are summarized in the following table:

| | FY 2019 Governor's Recommendation | FY 2020 Governor's Recommendation |
|---|---|---|
| Administration | $12,914,199 | $13,110,769 |
| Deferred Compensation | 478,880 | 491,803 |
| Investments | 34,762,265 | 36,491,420 |
| Total Operating Budget | $48,155,344 | $50,093,992 |

The Governor is recommending a 2.5% increase for State employee pay, which would have an effect on KPERS administrative expenditures. At this time the additional expenditures have not been calculated at the agency level. If that policy initiative moves forward, the KPERS administrative budget will be adjusted to reflect the additional funding for salary adjustments.

## Re-Amortization of the Legacy Unfunded Actuarial Liability

Part of the Governor's budget policies includes recommending the Legislature extend the amortization of the State/School group legacy unfunded actuarial liability. The Governor's recommendation is for a closed, 30-year period starting on 12/31/2016 (first affecting employer contributions rates in FY 2020). There are 15 years remaining on the current, 40-year closed amortization period that was set by the Legislature in 1993.

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In addition to extending the amortization period, the Governor's recommendation would:

- Eliminate the layered payments on delayed contributions from FY 2017 and FY 2019 and add those missed contributions to the unfunded actuarial liability.
    - The FY 2017 delayed payments totaled $64 million and were to be repaid on a 20-year, level-dollar payment of $6.4 million. KPERS has received two of the payments, making the total missed contributions about $51.2 million.
    - The FY 2019 delayed payments total $194 million and were scheduled to be paid over 20 years on a level-dollar payment of $19.4 million. The payments are scheduled to begin in FY 2020, so the full amount of the missed contributions will be added to the unfunded actuarial liability.

- Eliminate the contingent $56 million transfer in FY 2019.
    - The 2018 Legislature approved a contingent $56 million transfer to KPERS in additional contributions for the School group. The payment is contingent on actual FY 2019 receipts being more than the April consensus revenue estimates.

| Summary of Governor's Recommended Contribution Adjustments | |
|---|---|
| **Recommended Adjustment** | **Adjustment Amount** |
| Eliminate remaining payments on FY 2017 delayed contributions (initially $64 million) | $51.2 million |
| Eliminate payments on FY 2019 delayed contributions | $194 million |
| Eliminate contingent $56 million payment in FY 2019 | $56 million |
| Total recommended adjustments | $301.2 million |

For actuarial projection purposes, the $301.2 million has already been calculated as received by the Trust Fund.

***Actuarial Impact***

Staff provided the details of the Governor's proposal, as we understand it, to the actuary for a cost impact projection. According to the actuarial cost projection, the extension of the amortization period would:

- Reduce the actuarial required contribution rate in FY 2020 from 14.74% to 11.45%.
    - The State/School employer contribution rate in FY 2020 would be equal to the new actuarial required contribution rate.

- Projected employer contributions would be about $770 million lower over the first five years (FY 2019 - FY 2023) after extending the amortization period.

- Total State/School employer contributions over the 30-year projection period are estimated to be $20.9 billion, compared to $13.5 billion under the baseline projection ($7.4 billion increase in total employer contributions).

- The State/School unfunded actuarial would initially increase under an extended amortization, peaking at $6.8 billion in the 12/31/2019 actuarial valuation. The unfunded actuarial liability would remain above $6 billion until 2036. Under the baseline projection, the State/School unfunded actuarial liability decreases each year and is extinguished in 2035.

- The State/School funded ratio under the extended amortization remains below 70% until 2023 (an additional 3 years compared to the baseline) and below 80% until 2038 (an additional 12 years compared to the baseline). Under the baseline projection, the State/School group is projected to be fully funded in 2035.

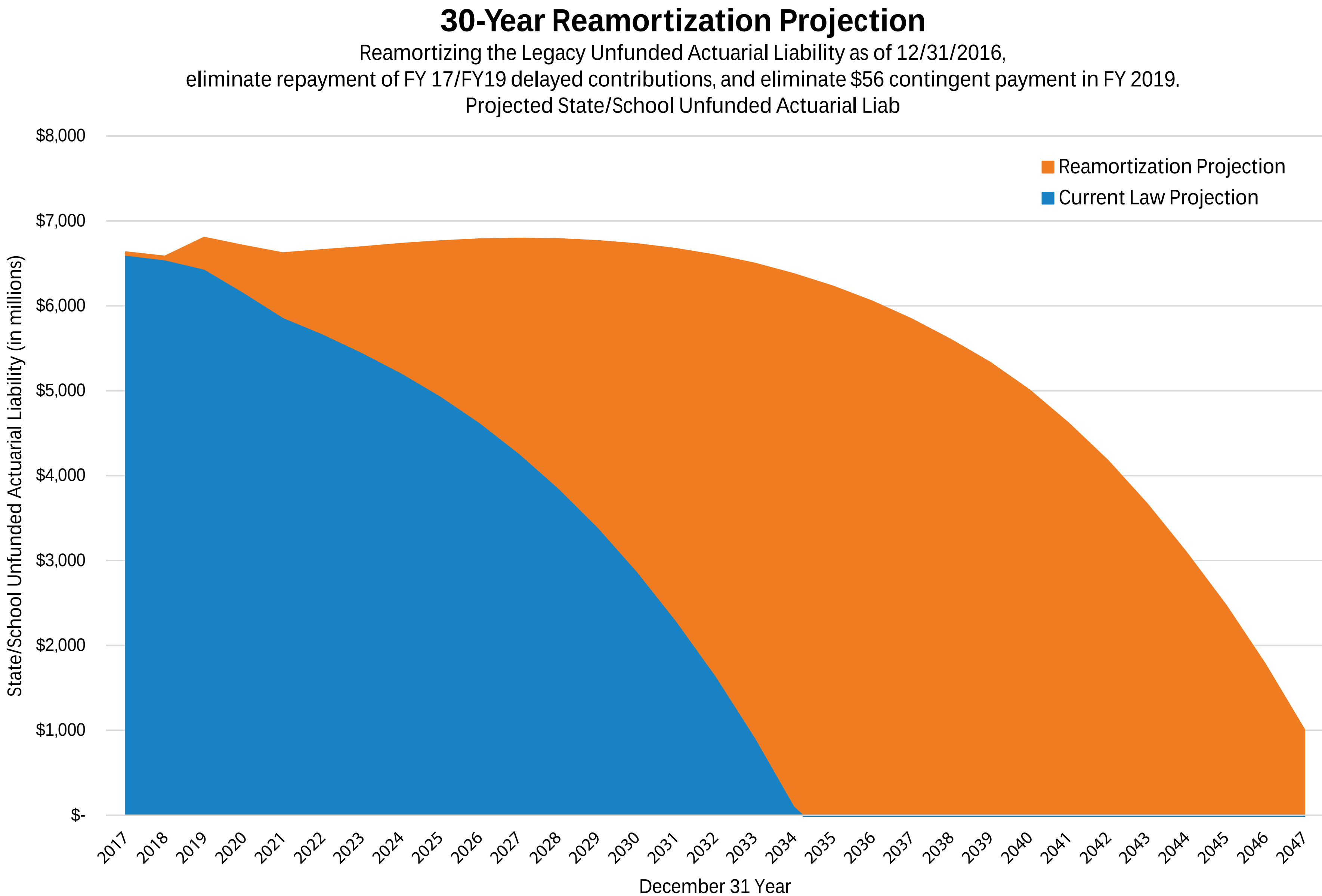
Attached to this memorandum are a series of charts that summarize the actuarial cost impact described above.

One important distinction in the Governor's Budget Report is that this recommendation only applies to the State/School group. The current amortization schedules for KPERS-Local, KP&F and Judges are recommended to remain in place. Having different amortization schedules for different groups does not cause any issues from an actuarial funding standpoint.

We would be happy to respond to any questions the Trustees have regarding the Governor's budget recommendations.

Attachments

Attachment A




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.

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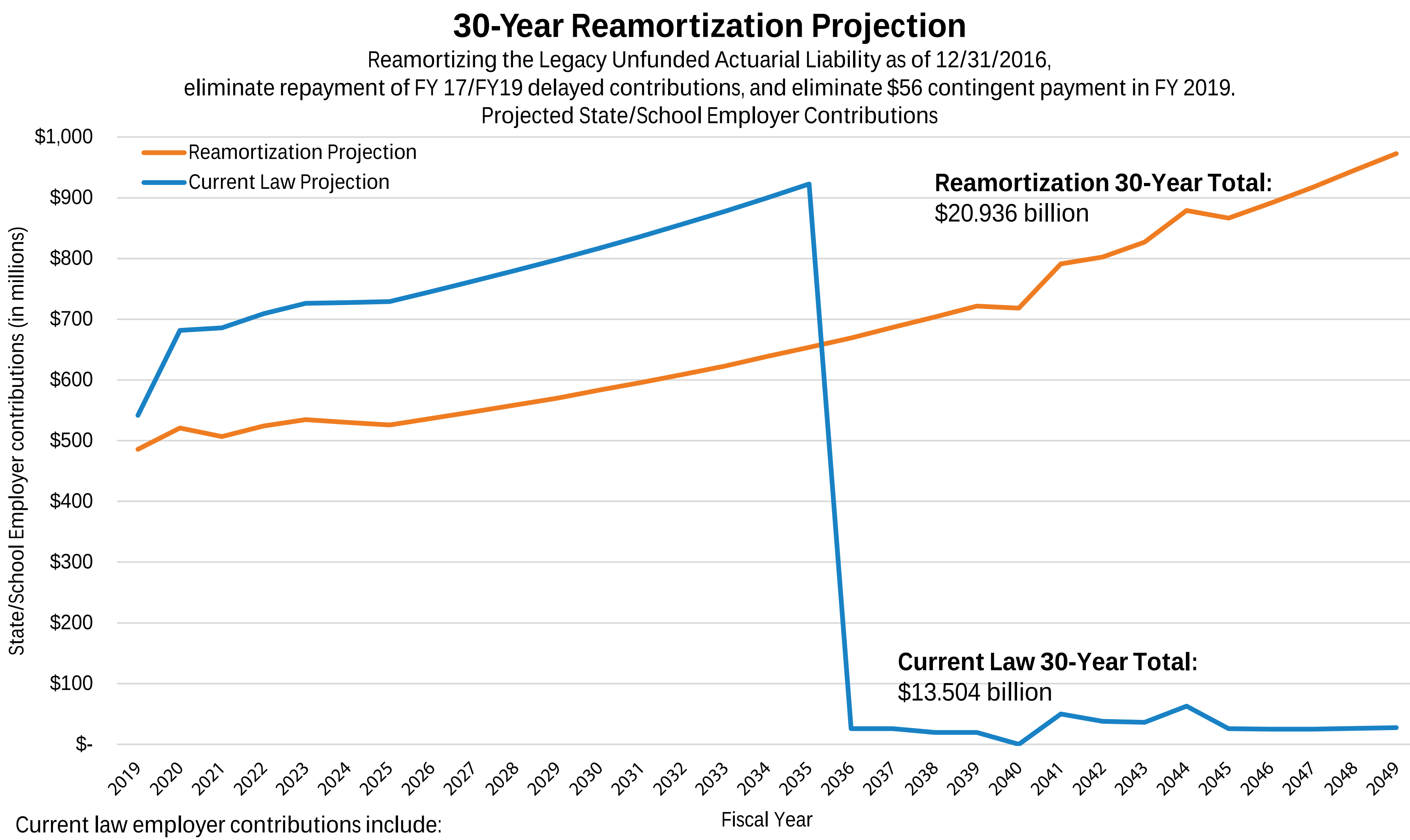
Attachment B




Current law employer contributions include:
1. The payment of delayed contributions in FY 2017 ($6.4 million anually 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.

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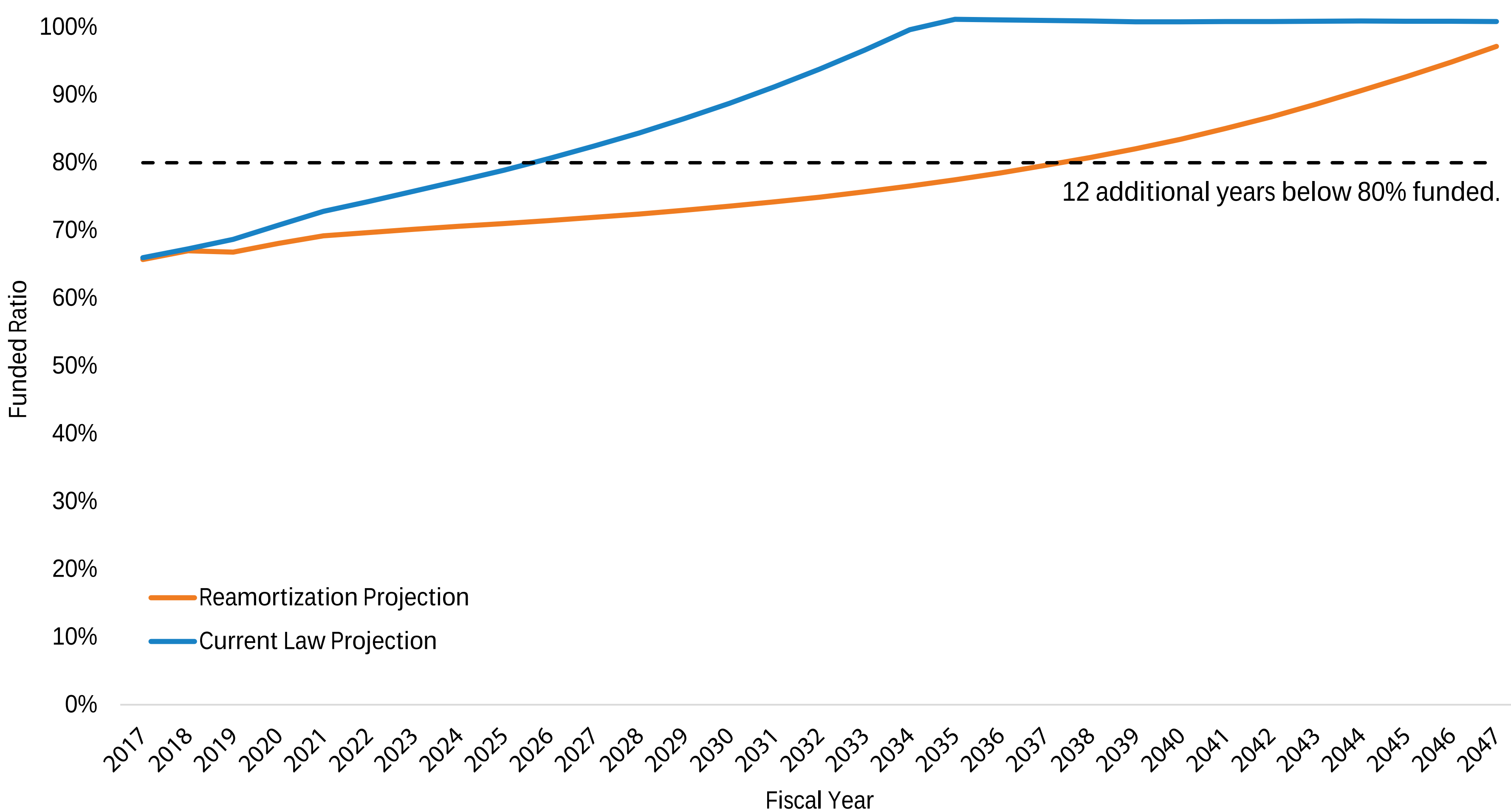
Attachment C

# 30-Year Reamortization Projection

Reamortizing the Legacy Unfunded Actuarial Liability as of 12/31/2016,
eliminate repayment of FY 17/FY19 delayed contributions, and eliminate $56 contingent payment in FY 2019.
Projected State/School Funded Ratio

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