Testimony to House Pensions and Benefits Committee

Conversion to Defined Contribution Plan

March 20, 2013

Dave Trabert, President

Chairman Johnson and members of the Committee:

We are pleased to submit this written testimony in support of legislation that would begin the transition from a defined benefit plan to a defined contribution plan. A great deal of legislative discussion has been devoted to this topic over the last few years as a means of providing employees with a substantial retirement benefit in a fiscally responsible manner.

Recent changes notwithstanding, Kansas still has one of the worst-funded pension plans in the nation. The most recent valuation shows a funded ratio of only 55% based on the market value of plan assets.[1] This is especially significant because funding ratios that fall below 80% are considered cautionary; a ratio below 60% is considered dangerous.

Table 1 Unfunded Accrued Actuarial Liability

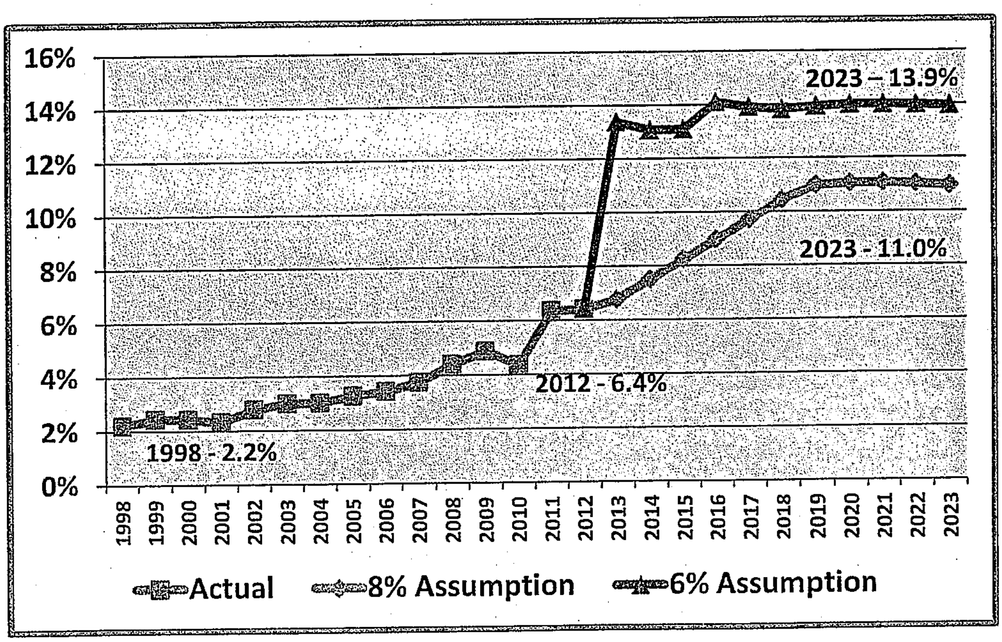
Asset Basis	12/31/07	12/31/08	12/31/09	12/31/10	12/31/11
Actuarial Value					
Funded Ratio	71%	59%	64%	62%	59%
UAAL	$5,552	$8,279	$7,677	$8,264	$9,228
Market Value					
Funded Ratio	75%	49%	56%	59%	55%
UAAL	$4,817	$10,250	$9,384	$8,936	$10,130

[1] KPERS Comprehensive Annual Financial Report, June 30, 2012. KPERS uses an asset smoothing reporting method which recognizes losses over a five year period. As of June 30, 2012 there was about $900 million of actual losses that were not included in the Actuarial Value of assets.

KPERS was fully funded until the early 1990s, but then benefits were increased by about 25% and legislation was enacted that set employer contribution levels below what was actuarially required. This deliberate under-funding has understandably prompted some people to say the Legislature should just contribute more money to make up the difference, but the consequences of doing so at this point would be far-reaching (if in fact even practical).

As shown in Figure 1, KPERS funding consumed 6.4% of General Fund revenue in 2012 but that is expected to rise to 11% by 2023 if the plan continues to be funded based on an assumed investment return of 8% for plan assets.[2] A more realistic long term investment assumption of 6% would put the unfunded liability at about $15 billion and push the necessary funding level to 13.9% of SGF revenue by 2023.[3]

Figure 1 KPERS Employer Contributions as a Percentage of General Fund Revenue



The crowding-out effect on other state service funding is going to get considerably worse unless substantive action is taken, such as converting from a defined benefit to a defined contribution plan.

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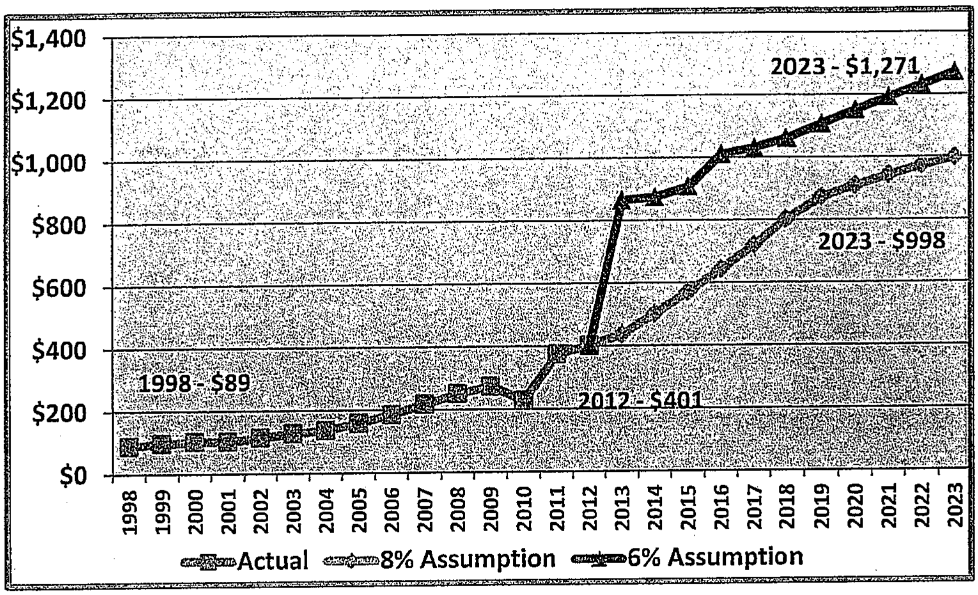
[2] "Major Structural Deficits Looming in Kansas," Dr. Art Hall, December 2011; assumes 3.5% General Fund revenue growth based on historical average

[3] Ibid; A KPERS actuarial estimate in 2011 said reducing the investment return assumption by a half-point would add $1.3 billion to the unfunded liability.

Figure 2 show KPERS spending in dollars (calculated as of December, 2011; minor variations may exist today). Depending upon the investment return assumption, the incremental cost of funding KPERS over the next ten years could approach $3 billion.

Figure 2 KPERS Spending (millions)



Finally, conversion to a defined contribution plan may also be necessary to ensure the safety of retirement benefits for current employees and retirees. Another recession in the next ten years of even half the magnitude of the last one could cripple a plan that is only 55% funded. And with the federal government running trillion dollar deficits and the national debt expected to hit $20 trillion in the near future, the prospect of another recession only worsens.