# MEMORANDUM

To: Senate Committee on Financial Institutions and Insurance

From: Alan D. Conroy, Executive Director

Date: March 14, 2017

Subject: HB 2268; working after retirement

During the 2016 Legislative Session, 2016 SB 168 made a number of changes to working after retirement legislation passed in 2015. As a part of SB 168, a number of the new provisions were made subject to a July 1, 2020 sunset, including application of the $25,000 earnings limit whether returning to the same or a different employer, the grandfathering provision for members who retired before May 1, 2015, and are subsequently hired in a licensed school professional position, and new hardship, hard-to-fill, and special education exemptions. HB 2268, as amended, makes changes to these new working after retirement policies.

**House Committee Recommendation**

The House Committee on Financial Institutions and Pensions made several amendments to HB 2268:

1. Working after retirement sunset date. Retains the existing sunset date of July 1, 2020. HB 2268, as introduced, delayed the working after retirement sunset date by one year, to 2021.
2. Third party and independent contractors. Provides clarification about the way working after retirement restrictions apply to retirees returning to work for KPERS employers as independent contractors or through a third party contractor. The language now requires a three-part test to determine whether a person is subject to the working after retirement rules: the member does not hold a position similar to the one filled prior to retirement; the activities performed are not normally performed exclusively by an employee; and the activities performed are on a limited-term basis.
3. Regents provision. Includes the provisions of HB 2005, clarifying that KPERS retirees who work for Regents institutions in positions covered by the Regents retirement plan are exempt from the working after retirement earnings limit.
4. Consolidate exemptions. Creates a single "emergency" exemption that could be used for up to three years with a possibility of a one-year extension (after submitting an assurance protocol) and eliminates the hardship, hard-to-fill and special education exemptions. Like the existing exemptions, employers filling a position under the emergency exemption would make contributions at a rate of 30% of the retiree's compensation.
5. Legislative earnings cap. Clarified that certain legislative expenses would not be considered in applying the working after retirement earnings cap for KPERS retirees serving as legislators.
6. Technical amendment. Changed a specific statutory reference to 8.0 percent as the assumed investment rate of return to the "rate as specified by the Board of Trustees" (now 7.75%).
7. Age 62 exemption. Added a new exemption from the working after retirement rules for any licensed school professional member who retires at the age of 62 or later on and after July 1, 2017. Employers must pay a 30% contribution on these rehired retirees.

KPERS

**Actuarial Costs**

Most of the amendments in HB 2268 are not expected to have a material fiscal impact on KPERS. However, three of the amendments to HB 2268 may in some way affect the ability of retirees to return to work without an earnings limit: the clarifications relating to third party and independent contractors; the Regents provision, and addition of an age 62 exemption. Exemptions from the earnings limitation for retirees returning to work can impact the cost of retirement benefits, with the degree of the impact dependent on the number of retirees affected and the demographic characteristics of the employees (e.g., age, earnings, gender, and years of service).

The potential for such an impact results primarily from two factors:

1. Changes in retirement patterns and behavior stemming from incentives for members to retire later or earlier than they would have absent the exemption.
2. Actuarial assumptions regarding retirement rates, set by age and used to project actuarial liabilities.

Members can be expected to act in their own financial interest. Retirees who can continue receiving pension benefits while earning all or a significant portion of their pre-retirement salary through employment with a KPERS-affiliated employer can realize a significant increase in their income. This potential financial benefit can be a significant incentive for members to modify the timing of their retirement. Therefore, changes to the existing rules and exemptions that make it easier for a member to receive both a pension and salary could be expected to become a material factor in members' decisions about when to retire.

Projections of actuarial liabilities and calculations of the actuarial contribution rates needed to fund those liabilities are built on the assumption that members will retire at certain rates. Actuarial costs to the System occur when retirement behavior differs from the actuarial assumptions. To the extent the proportion of members retiring is higher than the assumptions for their age, actuarial liabilities and the actuarial contribution rate may increase. However, there is no precise way to quantify with any certainty the cost impact of permitting KPERS members to return to work without an earnings limit.

Of the changes proposed in HB 2268, the age 62 exemption is more likely to have a significant impact on retirement behavior. There may be some licensed school professional members who choose to delay retirement until age 62 in order to be able to return to work without an earnings limit (assuming that other working after retirement rules make it significantly more difficult to do so prior to age 62). In those instances, the delay in their retirement would have a positive actuarial impact on the system. However, a significant proportion of retirees reach normal retirement eligibility for the first time at age 62 or after (KPERS 1 members can take normal retirement at age 62 with 10 years of service). In addition, not all members are expected to retire when first eligible for normal retirement. The proposed exemption would create a clear incentive for members who were not planning to retire when they first become eligible for normal retirement, thereby increasing the actuarial liability for their benefits. Therefore, it is not possible to ascertain whether the exemption would result in a net positive or adverse actuarial impact to KPERS.

Because it is not possible to project the extent or impact of changes in retirement patterns, it is not possible to calculate a precise employer contribution rate needed to fully fund any net actuarial costs caused by the "age 62" or other exemptions. However, there may well be a long-term actuarial cost associated with resulting changes in retirement patterns and behaviors.