

MEMORANDUM

To: House Financial Institutions and Pensions
From: Alan D. Conroy, Executive Director
Date: February 15, 2023
Subject: HB 2195; Working After Retirement

When a member retires from KPERS, there are statutory rules regarding that retiree returning to work for a KPERS employer in a covered position. The statutory rules include:

1. **Waiting Period.** Members who retire before age 62 have a 180-day waiting period before being rehired by a KPERS employer. Members who retire at age 62 or later have a 60-day waiting period.
2. **No Prearrangements.** Before retirement and during the waiting period, retirees and employers cannot communicate in any way about returning to work.
3. **Employer Contributions.** If a retiree returns to work in a covered position, the employer makes contributions to KPERS to help fund the System. Employers pay the statutory contribution rate (currently 12.57% for the State/School Group) for the first \$25,000 of the retiree's salary, and a 30% contribution rate on earnings over \$25,000.

Some employers may adjust the salary paid to a retiree to shift the cost of the contributions to the retiree, but statutorily the contribution is an employer contribution.

KPERS retirees who return to work do not have an earnings limitation.

If a KPERS member retires and goes to work for a private company or other non-KPERS employer, there are no restrictions.

KP&F and Judges retirees can return to work for a KPERS employer without considering working after retirement rules. Because they are separate plans, the KP&F or Judges retiree is enrolled as an active member of KPERS.

A summary of the current working after retirement rules are included in Attachment A.

Statutory Changes in HB 2195

HB 2195 makes two changes to the current statutory working after retirement rules:

1. Raising the threshold for the 30% employer contribution from \$25,000 per calendar year to \$35,000 per calendar year.
2. Create an 18-month window from July 1, 2023, to December 31, 2024, when employers would only make the statutory employer contribution on all retiree compensation (the 30% rate is waived).



The existing rules prohibiting prearrangements to return to work and the waiting period would remain the same.

HB 2195 also strikes several expired sections of K.S.A. 74-4914.

Working After Retirement Experience

In the 12/31/2021 KPERS actuarial valuation there were over 4,700 retirees with reported compensation during the calendar year. Since the current working after retirement rules went into effect on January 1, 2018, the number of retirees returning to work has trended slightly downward but has averaged about 5,000 retirees reported as working each year.

KPERS does not collect position information for retirees who return to work, so we do not know how many retirees are working as teachers, in management positions, or any other position. However, if a retiree is working in a position that is less than 1,000 hours for State and Local employers or less than 630 hours for School employers, they are considered non-covered positions and not subject to working after retirement contributions.

Internal Revenue Service Regulations

Working after retirement rules are necessary to remain compliant with the Internal Revenue Code. The IRS requires a “bona fide” retirement before members begin receiving retirement benefits. This requires termination from covered employment and no agreement to return to work.

As part of the plan design, the Legislature includes a statutory waiting period as a proxy test to establish that termination from covered employment has occurred and therefore establishes bona fide retirement. In general terms, the longer the waiting period in place the stronger the test of a bone fide retirement. The IRS has not specified the required length of the waiting period to be considered a valid test, but a 60-day waiting period was in place during the last plan review by the IRS and the plan passed the review without comment on the waiting period.

However, employer contributions are not considered under the internal revenue code and left up to the plan sponsor. HB 2195, as introduced, would not create any compliance issues with the internal revenue code.

Actuarial Cost Implications

The actuarial cost implications of HB 2195 are based on two factors:

1. The loss of expected employer contributions due to the change and
2. Potentially changing the pattern of retirement behavior by changing the working after retirement rules.

Based on the data for the calendar year 2021, the estimated employer contributions for working after retirement would have there were about 4,700 working after retirement members. Total contributions for 2021, based on the existing \$25,000 threshold, were approximately \$15.6 million. If the compensation limit for the 30% contribution rate had been increased to \$35,000, the total contributions would be reduced by \$1.4 million to \$14.2 million, about 10% lower. The difference of about \$1.4 million would directly reduce the assets and therefore increase the unfunded actuarial liability. Given the total KPERS (State, School and Local) unfunded actuarial liability of \$8.7

billion, the loss of \$1.4 million annually does not greatly impact the long-term funding of KPERS and would not be actuarially significant.

In addition, HB 2195 also provides that only the statutory employer contribution rate will be assessed on all compensation paid to retirees who return to work in covered employment from July 1, 2023, through December 31, 2024. Based on the available data, the estimated loss of contributions for this 18-month period is \$5.5 million (approximately \$3.7 million during FY 2024). Since this is a time-limited window, the long-term impact on the funding of the plan is negligible.

As the threshold for the 30% contribution rate increases, it becomes more attractive for employers to rehire retirees rather than seeking to fill the job with a new employee. This has the potential to encourage active members to retire earlier than they would otherwise and then return to work because of the financial incentives. If retirement behavior changes and members retire earlier, it can create a negative actuarial impact that was not expected or intended. However, this cost cannot be easily quantified.

Administrative Costs

The changes in HB 2195 would require some technical work to the pension administration system and updating of publications and education efforts. These costs can be accomplished within the existing appropriation request.

I would be pleased to respond to any questions the Committee has regarding HB 2195.

Attachment