

Pension Obligation Bonds



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Pension Obligation Bonds

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- History of approved pension obligation bonds
- Current pension obligation bond issues outstanding
- Investment performance

Pension Obligation Bonds

Purpose

- Pension obligation bond proceeds immediately improve funded status of the Retirement System.
- Bond debt is considered “hard debt” and is one of the highest budgeting priorities.
- The expectation is that, over time, KPERS’ investment returns will exceed interest rate paid on the pension obligation bonds, which in turn will reduce required future employer contributions.

Pension Obligation Bonds

History of approved pension obligation bonds

- The State of Kansas has issued pension obligation bonds to improve the funded status of the System on two occasions.
 - The first pension obligation bond issue was in 2004 (2004C) for a total of \$500 million, gross of fees.
 - The second pension obligation bond issue was approved by the Legislature and issued in 2015 (2015H). The approved amount of the pension obligation bonds was \$1.0 billion, net of fees.

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2004C bond issue

- In 2004, the Legislature approved a \$500 million bond issue to be deposited in the KPERS Trust Fund.
- The bonds are 30-year maturity bonds with a total interest cost of 5.39%.
- The structure of the bonds included capitalized interest totaling about \$60 million.
- KPERS ultimately received \$440,165,000 in net proceeds.
- Approximate annual debt service is \$33 million. Funding source is the Expanded Lottery Act Revenues Fund.

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2015H bond issue

- In 2015, the Legislature approved a \$1.0 billion bond issue, net of fees, with proceeds to be deposited in the KPER Trust Fund.
- The bonds are 30-year maturity bonds with a total interest cost of 4.68%.
- The 2015H bonds sold in August 2015 and KPER received the full \$1.0 billion in proceeds.
- Approximate annual debt service is \$65 million. Funding source is the State General Fund.

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Investment performance as of September 30, 2017

- As of September 30, 2017, investment returns on the System's investment portfolio have exceeded the interest cost of both bond issues.
- The System's average annualized total return for the time period since the 2004C bond issue is 7.38%, compared to the bond interest cost of 5.39%. The value added since issuance, after payment of the debt service, over **\$259 million**.
- The System's average annualized total return for the time period since the 2015H bond issue is 7.95%, compared to the bond interest cost of 4.68%. The value added since issuance, after payment of the debt service, is over **\$73.9 million**.

Pension Obligation Bonds

Considerations

- Both pension obligation bond issues are 30-year maturity bonds.
- The value to the State of issuing the bonds will not be fully known for many years, particularly on the 2015H bond, which is barely two years into the 30-year period.
- The expectation is that KPERs will be able to invest the proceeds and realize an investment return that exceeds the bond rate.
- As of today, both pension obligation bond issues have been a net positive to the State. This position is expected to vary over time, depending on market conditions.