



Kentucky Retirement Systems
PRESENTATION TO

Interim Joint Committee on Appropriations and Revenue

David Eager, Executive Director
Kathy Rupinen, General Counsel Advocacy

Oct 25, 2018

AGENDA

- 1. HB 62 Process**
- 2. HB 351 Revisions**
- 3. HB 362 What passed and what was removed**
- 4. Task force to deal with the Quasi conundrum**
- 5. Discussion on agencies reducing their participating workforces**

CEASING PARTICIPATION IN KERS AND CERS

HB 62 2015

- **Applies to certain agencies**
- **Well-defined process taking up to 18 months**
 1. Agency may request estimate actuarial cost
 2. Application and deposit
 3. Board initial approval
 4. Must set up alternative retirement plan
 5. Employees elect to stay with KRS or move to alternative plan.
 6. Final actuarial cost
 7. Agency Go/No-Go and Board final approval.
- **Lump sum or 20-year installment**

HB 351 2017

- **Changed the assumed interest rate to the higher of:**
 - **30-year treasury**
 - OR
 - **Actuarial assumed interest rate less 3.50%**
- **Allowed for lump sum only**
 - **No installment**

HB 362

- **Froze the KERS Quasi rate at 49.43% for FY 2019 (passed)**
 - 83.43% in FY 2020
- **Allowed for (up to) 12% phase-in for CERS employers (passed)**
 - Up to 28.08% over no more than 10 years
- **Permitted up to a 40-year interest-free loan (removed)**
 - Potential subsidy of up to \$2 Bil (\$1.7 Bil KERS Non-Haz alone)
 - Remaining agency contribution rates would increase by 6-8%

The Kentucky Pension Conundrum

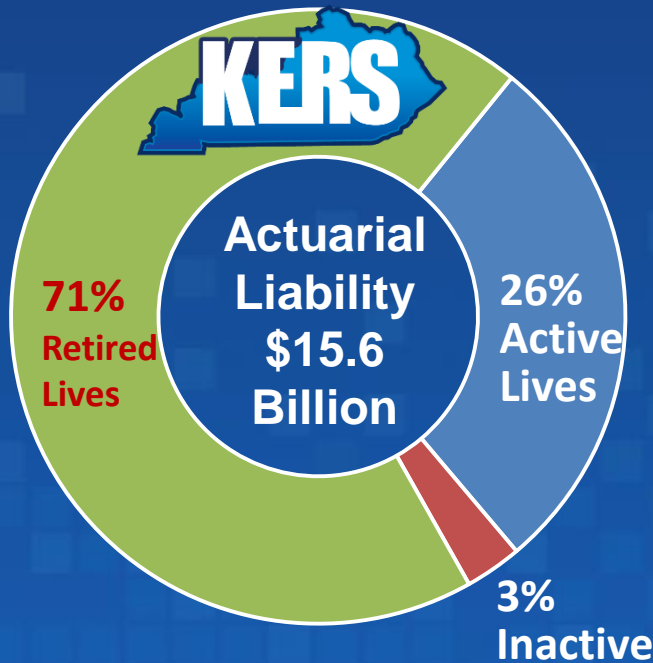
- **Economic assumptions revised in 2017, led to much higher contribution rates for FY 2019 and FY 2020 (up about 50%)**
 - **83.43% for KERS NH (Quasi agencies have a one year freeze at 49.47%)**
 - **28.05% for CERS NH (C plans are phased in)**
 - **Normal costs for new members have declined to under 3% (KERS NH) and 5.44% (SPRS) with Tier 3.**
 - **The pension conundrum is with Retiree payments and pending Tier 1 retirements, not future benefit obligations**

The Kentucky Pension Conundrum

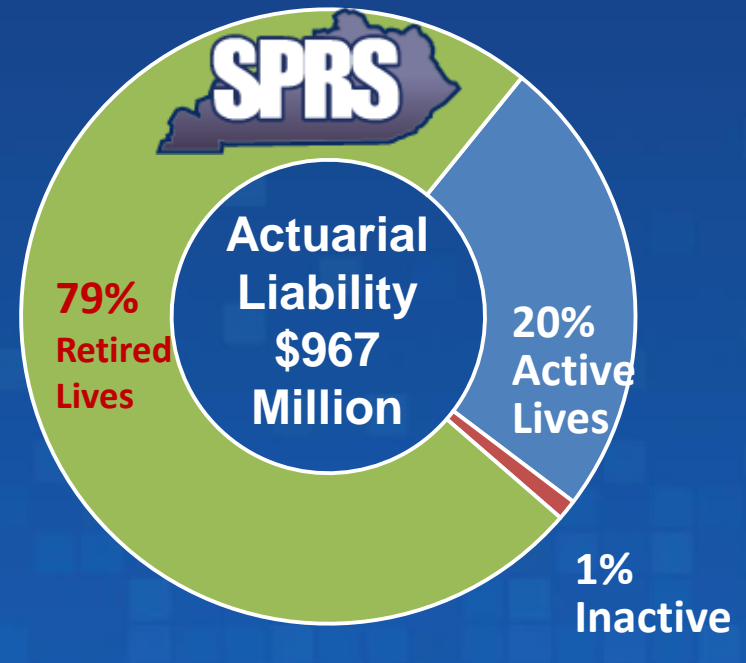
- **Many Quasi Agencies are “between a rock and a hard place”**
 - **Can’t afford the higher contributions in FY 2020**
 - **Can’t afford to withdraw from the system under HB 351**
 - **Continuing to outsource and/or lay-off**
 - **State wants the services they provide**

RETIRED ISSUE

Represents \$10B of Unfunded Liability



Unfunded Liability = \$13.5B



Unfunded Liability = \$706M

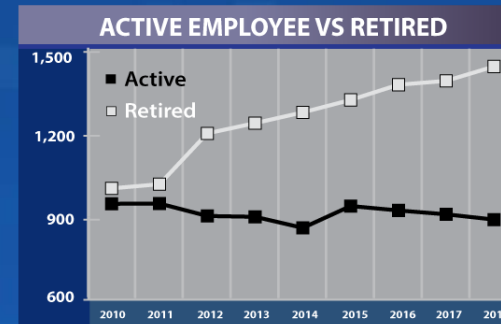
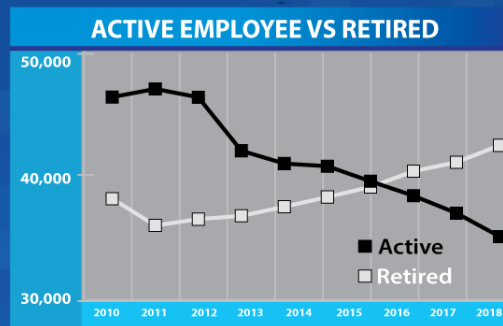
KERS Non-Haz Quasi Agencies = 118
\$2.9 Billion Actuarial Liability

19% of Plan Liability

June 30, 2017 Valuation

UNFAVORABLE TRENDS

- Prospective benefits changes (e.g. DC plan) - don't reduce retiree payments



- Actives who will retire over next 10+ years from Tier 1



Projected Retirements	0 - 5 years	6 - 10 years	11 - 15 years	16 - 20 years	21 - 25 years	26 - 30 years	30+ years	Total
KERS NHZ	6,530	5,762	4,808	1,962	286	24	-	19,372
SPRS	236	180	39	17	-	-	-	472
Total	6,766	5,942	4,847	1,979	286	24	-	19,844

OUR APPROACH

1. **KRS has a fiduciary responsibility to its systems and members.**
2. **KRS' recommended solution(s) due December 2018.**
3. **KRS Task force formed:**
 - David Eager, Executive Director KRS
 - Karen Roggenkamp, Deputy Executive Director
 - Mark Blackwell, Executive Director - Office of Legal Services
 - John Chilton, Trustee and Budget Director
4. **Discussions with many constituents.**
 - Help them understand the dynamics of the problems and the solutions
 - Understand agency dynamics
 - Seek input
 - Create proper expectations
5. **Assistance from GRS (actuary).**
 - Understand the liabilities
 - Collaborate on alternatives

OUR APPROACH

6. Consulting with or gained insights from other retirement systems regarding employer cessation and unfunded liability reduction efforts.

- Missouri
- Michigan
- South Carolina
- Illinois
- Kansas
- Utah
- Maine
- Indiana
- Ohio
- Tennessee

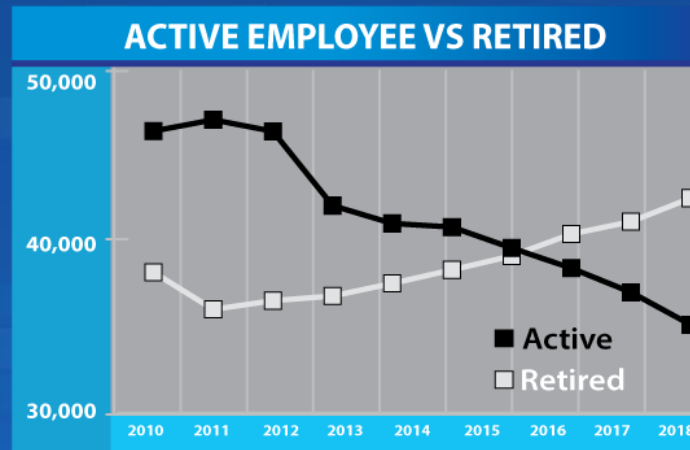
7. Propose solution(s) and assess impacts.

- Don't limit our options
- Legal and statutory requirements as well as federal funding must be considered for each proposal
- Solution(s) may need a funding source
- Solution(s) will require legislative action

MANNERS OF REDUCTION IN PARTICIPATION/WORKFORCE

- **Agency cessation**
- **Attrition without replacement**
- **Outsourcing**
- **Changes to positions in order to avoid participation**
- **Current litigation**

ATTRITION WITHOUT REPLACEMENT



OUTSOURCING EXAMPLES

Estimated Number of Employees:

- **EKU - 180**
- **WKU - 160**
- **KRCC - 500**
- **Others**

LEGAL ISSUES WITH OUTSOURCING AND APPROACHES TO AVOID PARTICIPATION

- **KRS has an obligation to determine who are employees of participating employers**
 - ❖ **KRS 61.510(5)**
 - ❖ **KRS 61.637(9)**
 - ❖ **Common Law and IRS 20 Factor Test**
- **Federal Law Concerns**
 - ❖ **Bona Fide separation from service**
 - ❖ **CODA requirements**

LEGAL ISSUES WITH OUTSOURCING AND APPROACHES TO AVOID PARTICIPATION, continued

- **Approaches to Avoid Participation**
 - ❖ **Employers failing to report employees**
 - * New and ongoing
 - ❖ **Employers changing positions to non-participating status**
 - ❖ **“Outsourcing”**
- **Litigation**
 - ❖ **Bankruptcy (Seven Counties Services)**
 - ❖ **Outsourcing (WKU and KRCC)**
 - ❖ **Other**

Regional Mental Health Boards & Seven Counties Services

Overview

- CHFS designates Regional Mental Health Boards
- 12 Regional Mental Health Boards (excluding Seven Counties) participate in KERS
 - (1) Adanta Behavioral Health Services
 - (2) Bluegrass.org
 - (3) Communicare, Inc.
 - (4) Comprehend, Inc. MHMR BD
 - (5) Cumberland River MHMR BD
 - (6) Green River MHMR BD
 - (7) KY River Community Care, Inc.
 - (8) Lifeskills, Inc.
 - (9) Mountain Comp Care Center
 - (10) Northern KY MHMR BD
 - (11) Pennyroyal MHMR BD
 - (12) Western KY MHMR BD

Regional Mental Health Boards & Seven Counties Services

Seven Counties Services, Inc.

- August 1, 1978 -- Seven Counties became the regional mental health board for Jefferson and the six surrounding counties.
- January 24, 1979 -- Executive Order 79-78 designates Seven Counties Services a participating “department” in KERS.
- April 2013 - Chapter 11 bankruptcy petition filed.
 - Approximately 1,300 employees who participated in KERS
 - Total payroll was approximately \$50 million per year
 - Estimated additional \$90 million in KERS unfunded liability would result from Seven Counties’ withdraw.
 - That shortfall is imposed upon the remaining employers in KERS

Regional Mental Health Boards & Seven Counties Services

Timeline of Events in Bankruptcy Case

- **April 2013** – Seven Counties files for Chapter 11 bankruptcy and stops making retirement contributions initially for approximately 1,000 employees.
- **May 2014** – Judgment by bankruptcy court in favor of Seven Counties.
 - KERS appeals to the Federal District Court.
 - Stops making retirement contributions for remaining 300 employees at Central State Hospital.
- **March 2016** – District Court affirms bankruptcy court decision.
 - KERS appeals to the Sixth Circuit Court of Appeals.
- **November 2017** – Oral arguments conducted before a three judge panel of the Sixth Circuit Court of Appeals.
- **August 2018** – Sixth Circuit affirms District Court’s decision that Seven Counties eligible to file under chapter 11.
 - Holds appeal in abeyance asking Kentucky Supreme Court to decide:
“*Whether Seven Counties Services, Inc.’s participation as a department in and its contributions to the Kentucky Employees Retirement System are based on a contractual or a statutory obligation.*”
 - 2-1 Decision
 - Includes a lengthy 20 page dissent by Judge David W. McKeague.
- **September 2018** – KERS requests a rehearing *en banc* of the majority opinion that Seven Counties is not a “governmental unit” and therefore eligible to file bankruptcy under chapter 11 of the Bankruptcy Code.
- **October 2018** – Sixth Circuit holds petition for *en banc* review in abeyance pending a response from Kentucky Supreme Court.