

# PUBLIC PENSION OVERSIGHT BOARD

## Minutes

April 24, 2023

### Call to Order and Roll Call

The 3rd meeting of the Public Pension Oversight Board was held on April 24, 2023, at 1:00 PM in Room 154 of the Capitol Annex. Senator Jimmy Higdon, Chair, called the meeting to order, and the secretary called the roll.

### Present were:

Members: Senator Jimmy Higdon, Co-Chair; Representative DJ Johnson, Co-Chair; Senator Christian McDaniel, Senator Robby Mills, Senator Gerald A. Neal, Senator Michael J. Nemes, Senator Mike Wilson, Representative Ken Fleming, Representative Derrick Graham, Representative Jason Petrie, Representative Phillip Pratt, Representative James Tipton, Representative Russell Webber, Mike Harmon, and Victor Maddox.

Guests: Bo Cracraft, Executive Director, Judicial Form Retirement System; David Eager, Executive Director, and Erin Surratt, Executive Director, Office of Benefits, Kentucky Public Pensions Authority; and Beau Barnes, Deputy Executive Secretary and General Counsel, Teachers' Retirement System.

LRC Staff: Brad Gross, Michael Clancy, Jennifer Hans, and Angela Rhodes.

### Approval of Minutes

Senator Wilson moved that the minutes of the February 27, 2023, meeting be approved. Senator Mills seconded the motion, and the minutes were approved without objection.

### Judicial Form Retirement System

Bo Cracraft, Executive Director, Judicial Form Retirement System (JFRS), presented a review of the investment performance for the Judicial Retirement Plan (JRP) and the Legislators Retirement Plan (LRP). He discussed the gross and net performance for the defined-benefit and hybrid cash balance plans for the quarter ending March 31, 2023, and for the 1-, 3-, 5-, 10-, 20-, 30-year, and inception-to-date trailing time periods.

Mr. Cracraft discussed cash flow for both plans for FYTD 2023 compared to FYTD 2022. He reviewed the cash inflows, outflows, investment gains or losses, and the total net plan assets across both time periods.

In response to a question from Senator McDaniel, Mr. Cracraft stated that realized gains are the gains received from selling an asset, and unrealized gains are the value above purchase price of assets that have not yet been sold. In response to a follow-up regarding the value of bonds with a lower sale price due to rising interest rates, Mr. Cracraft stated that JFRS fixed income assets are largely corporate and are priced based on a fair value, and as long as the bonds are held until maturity, they will get the yield and the full par amount. He also confirmed that unrealized gains and losses are booked monthly.

Mr. Cracraft gave a legislative update on House Bill 236 from the 2023 Regular Session, which had a direct impact on JFRS that required action. He stated that the JFRS board of trustees has always taken their fiduciary responsibility very seriously and has always managed assets in the sole interest of JRP and LRP members. Mr. Cracraft noted that JFRS partners with Baird Trust Company (Baird), who serves as the board's sole investment provider. Baird acknowledges its fiduciary duty in its contract, is a registered investment manager, and has a long history of providing above benchmark returns for over 30 years. Also, Baird currently handles all proxy voting and votes in accordance with its approved policy. Under House Bill 236, the JFRS board will either formally adopt the Baird proxy policy or designate separate guidelines at a future quarterly meeting.

Lastly, Mr. Cracraft provided an actuarial assumption review. He stated that the JFRS board plans to review economic assumptions during their July 2023 meeting where they also plan to discuss actuarial audit recommendations made by Milliman. Full funding valuations will be conducted as of July 1, 2023, with results expected no later than November 15, 2023.

In response to a question from Representative Johnson, Mr. Cracraft stated that under House Bill 236, JFRS will not have to change anything other than written guidelines. Representative Johnson asked JFRS to inform the Public Pension Oversight Board if any issues arise in complying with House Bill 236.

In response to a question from Senator Higdon, Mr. Cracraft stated that JFRS' inflation assumption was higher as a result of the audit, and that he would not be surprised if the JFRS board chooses to drop the rate of return assumption a little.

In response to a question from Representative Tipton, Mr. Cracraft stated that the last cost of living adjustment for the JFRS plans was applied effective July 1, 2011 (FY 2012). In response to an additional question, Mr. Cracraft stated new legislators and judges who have prior service with Kentucky Employees Retirement System (KERS) or the County Employee Retirement System (CERS) almost exclusively choose the KERS cash balance plan rather than opting to participate in LRP or JRP. The most recent data shows that out of 55 new judges as a result of elections and terms, 36 joined KERS with all but 2 having prior KERS or CERS service, and the remaining 23 joined JRP. With the 32 new legislators, 18 joined LRP and 14 joined or remained with KERS.

### **Kentucky Public Pensions Authority**

David Eager, Executive Director, Kentucky Public Pensions Authority (KPPA), began his presentation with an appreciation of appropriations received thus far.

In response to a comment from Senator Higdon, Mr. Eager stated that House Bill 551 relating to sports gaming will provide additional revenue for KPPA.

Mr. Eager continued with the investment and cash flow update. He provided a chart of the third quarter fiscal year 2023 market asset class returns.

Next, Mr. Eager discussed the pension and insurance investment returns for the quarter ending March 31, 2023. He provided the preliminary one month, FYTD, 1-, 3-, 5-, 10-, 20, and 30-year net of fees rates of return.

Mr. Eager discussed the pension cash flow for all plans for FYTD 2023 compared to FYTD 2022. He reviewed the cash inflows, outflows, investment gains or losses, and the total net plan assets across both time periods.

Senator Higdon commented that KPPA has received \$180 million in general fund appropriations so far, this fiscal year.

In response to a question from Representative Tipton, Mr. Eager stated that KPPA will follow-up with more clarification on why employer contributions to health insurance are down in KERS non-hazardous plan.

Mr. Eager discussed the health insurance cash flow for all plans for FYTD 2023 compared to FYTD 2022. He reviewed the cash inflows, outflows, investment gains or losses, and the total net plan assets across both time periods.

Mr. Eager gave a legislative update. He discussed the Senate's confirmations of reappointments and appointments of trustees to the Kentucky Retirement Systems' (KRS) board. The implementation process is complete for Senate Bill 20, which prohibits the use of TikTok on any state government network. Regarding the implementation of House Bill 236, which requires that fiduciaries of the systems consider only pecuniary factors and that proxy votes are consistent with board policy, the boards already have existing investment policy statements and proxy voting policy statements in place; and KPPA is working toward having all investment managers in compliance, with only one manager requiring additional negotiations. Further implementation will focus on mitigating the expected increase in administrative costs for each plan to cover the cost of compiling and reporting proxy votes on a quarterly basis.

In response to a question from Representative Johnson, Mr. Eager stated that KPPA is hoping to have their first proxy voting quarterly report by June 30, 2023. In response to a follow-up, Mr. Eager stated that the investment policy statements should comply by June 30, 2023.

In response to a question from Auditor Harmon, Mr. Eager confirmed that the proxy voting services utilized will vote according to the boards' proxy voting policy, which allows the consideration of pecuniary factors only.

Erin Surratt, KPPA, discussed House Bill 506, which reinstates the partial lump sum option as a retirement payment option and changes the required break in service for retired reemployed members to one calendar month. She stated that the implementation is in process and is expected to be completed in the Fall of 2023 in advance of the bill's effective date of January 1, 2024.

Mr. Eager discussed House Bill 587, which reorganizes the position of the KPPA Internal Auditor position, and stated that the implementation is in process and is expected to be completed by June 2023.

Mr. Eager discussed the actuarial assumption update. He stated that GRS is finalizing an experience study for both economic and demographic assumptions for CERS and KRS. The KPPA board will have the opportunity to review the material and may decide to make assumption changes.

Ms. Surratt provided an update on line of duty, disability, and death benefits. She reviewed the recent legislative changes impacting the line of duty benefits and line of duty benefit statistics for all plans.

In response to a question from Senator Higdon, Ms. Surratt stated that, in 2021, there were a total of 660 active members who died compared to 725 in 2022. Four of those in 2022 received the enhanced line of duty benefits.

In response to a question from Representative Johnson, Mr. Eager confirmed that KPPA live-streams their board meetings and committee meetings. In response to a follow-up question, Mr. Eager stated that KPPA is ready for its five-year financial audit as required by statute.

In response to a question from Senator Higdon, Mr. Eager stated that KPPA has reviewed the recommendations from the actuarial audit performed by Milliman.

### **Teachers' Retirement System**

Beau Barnes, Teachers' Retirement System (TRS), began his presentation with the investment performance. He discussed the preliminary gross and net performance for the retirement and insurance plans for the quarter ending March 31, 2023, for the 1-, 3-, 5-, 10-, and 20-year time periods.

Mr. Barnes discussed cash flow for both plans for FYTD 2023 compared to FYTD 2022. He reviewed the cash inflows, outflows, investment gains or losses, and the total net plan assets across both time periods.

Mr. Barnes gave a legislative update on House Bill 236. He stated that, as a fiduciary, TRS invests solely in the interest of its members and annuitants and votes its shares using only pecuniary factors and not to further any nonpecuniary interest. In addition, TRS is in the process of implementing changes to comply with the new proxy vote reporting requirements of House Bill 236 and has issued a request for proposals (RFP) to solicit competitive bids from proxy voting advisors and companies providing proxy voting services. Mr. Barnes also discussed House Bill 76 from the 2022 session, which requires an experience study for economic assumptions to be completed every two years. The study will be ready by November 15, 2023.

In response to a question from Representative Johnson, Mr. Barnes stated that TRS is in full compliance with House Bill 236 and can provide a report after June 30, 2023. In response to a follow-up, Mr. Barnes stated that all TRS board meetings are in-person meetings at this time. Representative Johnson stated he thinks it would be better if the meetings could be live-streamed.

In response to a question from Senator Mills, Mr. Barnes stated that the RFP issued to proxy voting services included House Bill 236 requirements.

In response to a question from Representative Tipton, Mr. Barnes stated that the current funding level is 63.7 percent for the health insurance fund as of June 30, 2022. In response to a follow-up, Mr. Barnes stated that he would have to follow-up later in regards to the much higher employer contributions toward the health insurance trust. In response to an additional follow-up, Mr. Barnes confirmed that by 2032 the actuarially required contribution will be \$2 billion and, while the funded status will accelerate, TRS' annuity trust will not be 100 percent funded until

2045-2046.

In response to a question from Senator Higdon, Mr. Barnes stated that schools report sick leave at the time of retirement and that their actuary does project a liability. Senator Higdon commented that he would like to have the actual liability reported yearly.

## **Adjournment**