

Kentucky Retirement Systems CERS Overview



Presented to:

*Louisville Metro Council
Intergovernmental Affairs Committee*

February 13, 2014

Kentucky Retirement Systems (KRS) Facts

- **KRS administers retirement benefits for over 340,000 state and local government employees**
 - These employees include state employees, state police officers, city and county employees, local agency employees, and nonteaching staff of local school boards and regional universities.
- **KRS administers three plans:**
 - Kentucky Employees Retirement System (KERS)
 - KRS 61.510 to 61.705 and KY Administrative Regulations, Title 105
 - County Employees Retirement System (CERS)
 - KRS 78.510 to 78.852 and KY Administrative Regulations, Title 105
 - State Police Retirement System (SPRS)
 - KRS 16.505 to 16.652 and KY Administrative Regulations, Title 105

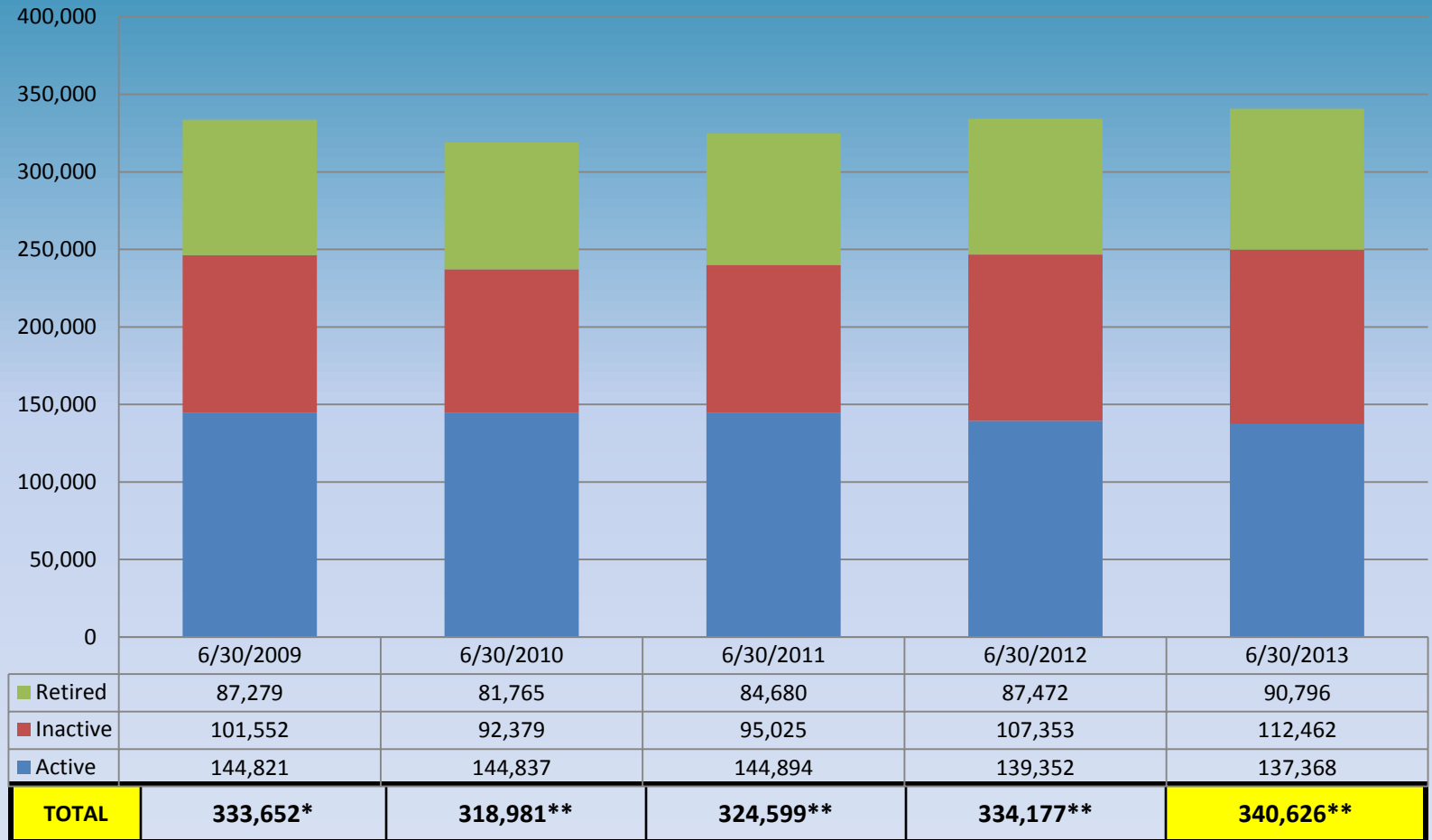
Plan Administration

- **A thirteen-member Board of Trustees administers the Systems:**
 - Two trustees elected by KERS members
 - Three trustees elected by CERS members
 - One trustee elected by SPRS members
 - Six trustees appointed by the Governor
 - *One must be knowledgeable about the pension requirements on local governments*
 - *Two must have at least 10 years of investment experience*
 - *One each from lists of nominees submitted by the KY League of Cities, the KY Association of Counties, and the KY School Boards Association*
 - The Secretary of the Kentucky Personnel Cabinet, *ex officio*
- **The Board appoints an Executive Director to act as the Chief Administrative Officer of the Board**
- **KRS reports for budget purposes to the Kentucky General Assembly**

Plan Administration

- **The following standing committees are created in the bylaws of the KRS Board of Trustees:**
 - Administrative Appeals Committee
 - Disability Appeals Committee
 - Audit Committee
 - Investment Committee
 - Legislative and Budget Committee
 - Human Resources Committee
 - Retiree Health Committee
 - Legal, Compliance and Governance Committee
- **The members and the chair of each standing committee are appointed by the chair of the KRS Board of Trustees**
- **The chair of the KRS Board of Trustees or the Board may also create *ad hoc* committees, as needed**

KRS Membership (2009 – 2013)



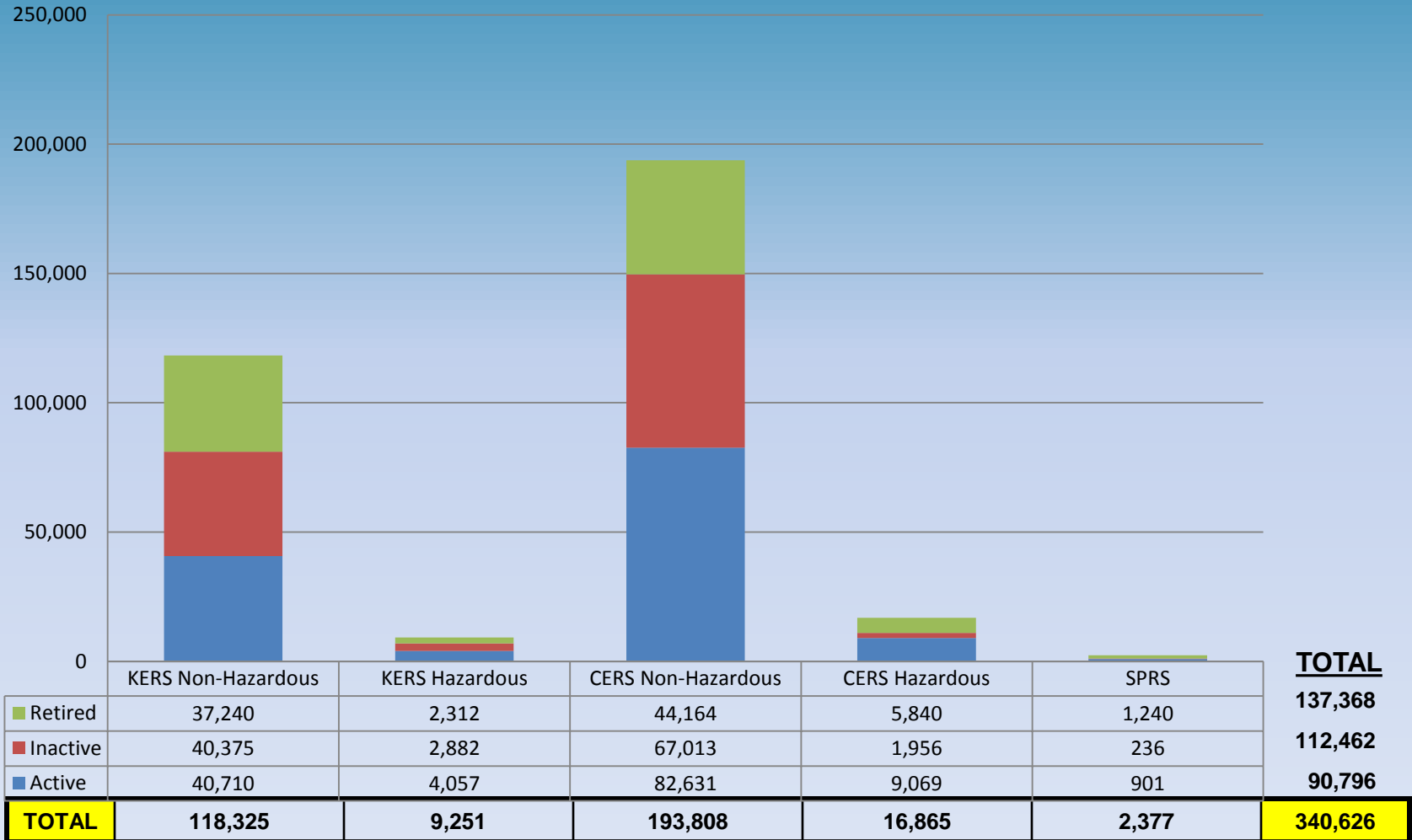
* The data for years 2006 – 2009 reflects the number of accounts in each system.

** Beginning in 2010 each person is counted only once in the Membership by System report.

Source: June 30, 2013 Comprehensive Annual Financial Report (CAFR)

KRS Membership by System and Status

As of June 30, 2013



Source: June 30, 2013 Comprehensive Annual Financial Report (CAFR)

KRS Current Assets and Benefit Payments

- As of June 30, 2013, the market value of KRS assets (pension and insurance) was **\$14.67 billion**
- KRS pays over **\$2 billion** in pension and insurance benefits each year
 - 95% of benefit payments are delivered to Kentucky residents and have a significant impact on the Kentucky economy

Source: June 30, 2013 Actuarial Valuation and June 30, 2013 Comprehensive Annual Financial Report

Allocation of KRS Administrative Costs

- KRS 61.580 provides the following: “The retirement allowance account shall be the account in which shall be accumulated all employer contributions From this account shall be paid the expenses of the system and the board incurred in administration of the system
- KRS administrative costs are paid from each plan’s Retirement Allowance Account and are allocated based on pro rata share of the System’s total membership. **For the 2014-2015 fiscal year, the membership totals and the Administrative Percentages have been calculated as follows:**

System	Member Count	System Percentage
KERS	117,177	35.10%
KHAZ	8,809	2.60%
CERS	188,884	56.60%
CHAZ	16,536	4.90%
SPRS	2,349	0.80%
TOTALS	333,755	100.00%

- All allotments and administrative expense transfers made directly from the retirement allowance accounts on July 1, 2014, and thereafter, are made based on the percentages shown above.

How is KRS Funded?

- **There are three (3) sources of funding for Kentucky Retirement Systems:**
 - **Employee Contributions:**
 - Set by statute
 - **Employer Contributions:**
 - Set annually by the KRS Board of Trustees based on an independent actuarial valuation and recommendation
 - Contribution paid by KERS and SPRS employers subject to the appropriation amount set forth by the General Assembly in the biennial budget legislation
 - **Return on Investments**
 - The KRS Investment Committee has the authority to make investment decisions and hire external investment managers and consultants
 - KRS utilizes internal investment staff, external investment managers, and independent investment consultants to conduct the investment program

How is KRS Funded?

The Majority of KRS Funding Comes from **Return on Investments**



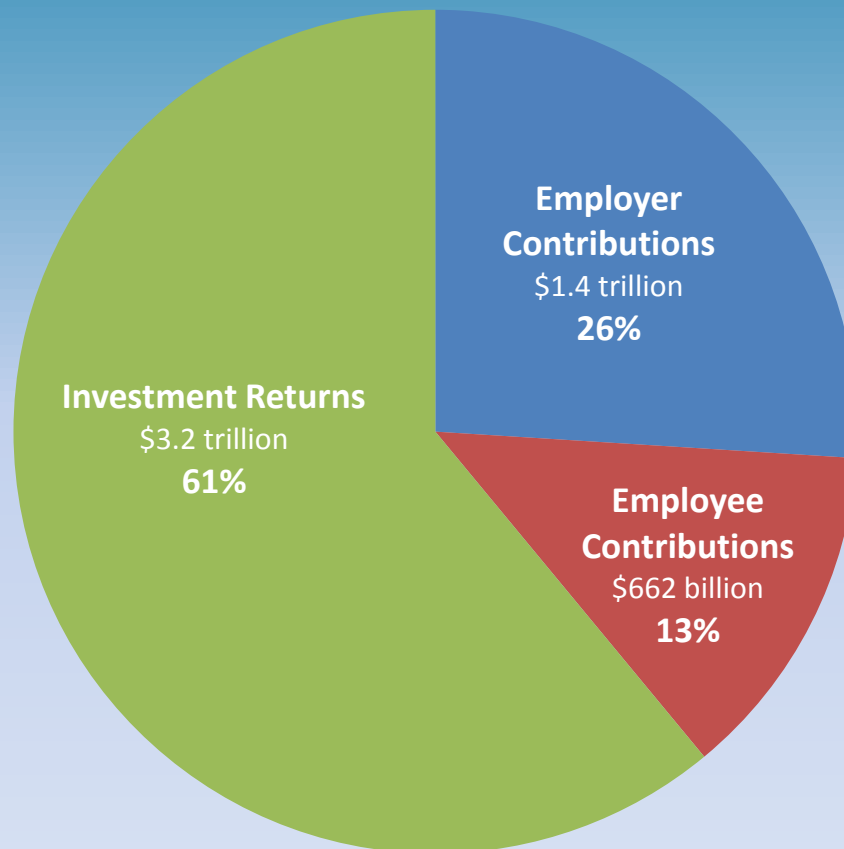
↑
Employee
12%

↑
Employer
20%

↑
Investment Income
68%

Public Pension Fund Revenue Sources

United States, 1982 to 2011



Sources: *US Census Bureau and the National Association of State Retirement Administrators (NASRA Issue Brief: Employee Contributions to Public Pension Plans, January 2014).*

The US Census Bureau first began reporting public pension fund revenue data in 1982.

Employer Contributions

- **Set by Board of Trustees based on actuarial analysis and recommendations**
- **Employer Contribution Rate Consists of:**
 - **Pension Contribution**
 - **Normal Cost** = The cost of projected benefits allocated to the current year (the year the valuation is conducted)
 - **UAL Payment** = The present value of benefits earned to date that are not covered by current plan assets
 - **Insurance Contribution**
 - Created by 1978 Legislature
 - Made a contractual obligation by 1988 Legislature; taken out of inviolable contract for employees hired on or after July 1, 2003
 - In 2006, GASB 43 and 45 changed the accounting and reporting requirements related to Other Post Employment Benefits (OPEB) for public retirement systems.
 - KRS must now recognize and report on an accrual basis the cost of retiree health insurance benefits over the working life of the employee

Actuarially Required *versus* Actual FY 2013 - 2014 Employer Contributions

- KERS and SPRS employer contribution rates are subject to approval by the Kentucky General Assembly in biennial budget legislation
- CERS employer rates are set by the Board of Trustees

System	Required Contribution	Actual Contribution
KERS Non-Hazardous	45.28%*	26.79%
KERS Hazardous	28.84%*	32.21%
CERS Non-Hazardous	18.89%	18.89%**
CERS Hazardous	35.70%	35.70%**
SPRS	96.52%*	71.15%

* Required contribution rates prior to applying the House Bill 1 (2008 Legislative Session) phase-in percentages set forth in KRS 61.565(5) .

** The CERS rates reflect the ten-year phase-in of the insurance portion of the rate required by KRS 61.565(6).

Actuarially Required 2014-2015 Employer Contributions

(as a percent of payroll)

System	Normal Pension Cost	Admin. Expense	Payment On Pension UAL	Insurance Fund	Actuarial Required Rates from 2013 Valuation	Phase-in Rates*
KERS (Non-Hazardous)	3.48%	0.65%	26.71%	7.93%	38.77%	-
KERS (Hazardous)	5.24%	0.55%	10.58%	9.97%	26.34%	-
SPRS	8.05%	0.41%	45.44%	53.90%	75.76%	-
CERS (Non-Hazardous)	3.56%	0.79%	8.40%	5.35%	18.10%	17.67%*
CERS (Hazardous)	6.09%	0.26%	14.38%	14.97%	35.70%	34.31%*

* The CERS rates reflect the ten-year phase-in of the insurance portion of the rate required by KRS 61.565(6).

**CERS Non-Hazardous Members
(SB 2 Provisions - 7.3% Crediting Rate)**

Fiscal Year Ending June 30	Contribution Rate			Projected Payroll	Total Contribution	Actuarial Accrued Liability		
	Pension	Insurance	Total			Pension	Insurance	Total
2013	12.62%	6.93%	19.55%	\$2,260,762,874	\$441,979,142	\$8,918,085,025	\$3,073,973,205	\$11,992,058,230
2014	13.74	5.15	18.89	2,312,061,847	436,712,370	9,139,567,695	2,370,771,288	11,510,338,983
2015	12.95	5.40	18.35	2,369,158,739	434,740,629	9,463,142,084	2,535,028,593	11,998,170,677
2016	12.70	5.64	18.34	2,430,848,763	445,817,663	9,787,686,266	2,695,846,394	12,483,532,660
2017	12.64	5.89	18.53	2,496,333,891	462,570,670	10,111,223,784	2,851,995,810	12,963,219,594
2018	12.82	6.13	18.95	2,565,765,341	486,212,532	10,433,025,223	3,002,813,255	13,435,838,478
2019	12.81	5.13	17.94	2,639,069,408	473,449,052	10,752,706,087	3,148,318,860	13,901,024,947
2020	12.79	4.95	17.74	2,716,918,951	481,981,422	11,069,317,453	3,288,227,365	14,357,544,818
2021	12.78	4.83	17.61	2,799,964,913	493,073,821	11,381,538,301	3,421,722,581	14,803,260,882
2022	12.76	4.71	17.47	2,887,247,671	504,402,168	11,689,406,972	3,549,178,583	15,238,585,555
2023	12.75	4.59	17.34	2,978,689,464	516,504,753	11,993,343,030	3,670,876,705	15,664,219,735
2024	12.73	4.48	17.21	3,075,425,140	529,280,667	12,291,052,834	3,786,531,911	16,077,584,745
2025	12.74	4.37	17.11	3,177,699,431	543,704,373	12,581,376,983	3,896,024,917	16,477,401,900
2026	12.73	4.27	17.00	3,285,506,927	558,536,178	12,863,047,607	3,998,741,254	16,861,788,861
2027	12.72	4.16	16.88	3,398,817,543	573,720,401	13,135,808,398	4,094,353,159	17,230,161,557
2028	12.72	4.08	16.80	3,518,128,886	591,045,653	13,398,831,150	4,182,179,110	17,581,010,260
2029	12.72	3.99	16.71	3,644,209,844	608,947,465	13,651,554,566	4,261,265,801	17,912,820,367
2030	12.73	3.92	16.65	3,778,066,173	629,048,018	13,892,265,110	4,331,155,241	18,223,420,351
2031	12.72	3.83	16.55	3,920,489,215	648,840,965	14,121,198,991	4,391,524,548	18,512,723,539
2032	12.72	3.77	16.49	4,071,878,654	671,452,790	14,339,819,658	4,443,039,964	18,782,859,622

Actuarial Basics

- **Funding Level**

- Ratio of Actuarial Assets to Actuarial Liabilities
- Measure of the plan's financial soundness
- Provides a “snapshot” of the plan's ability to meet liabilities (benefits) earned to date
- Actuarial funding level is based on a 5-year smoothing method, i.e. 20% of market gains/losses are recognized each year over a 5-year period

Actuarial Basics

Summary of Actuarial Funding Level (2008 – 2013)

CERS Non-Hazardous PENSION



Source: June 30, 2013 Comprehensive Annual Financial Report

Actuarial Basics

Summary of Actuarial Funding Level (2008 – 2013)

CERS Non-Hazardous INSURANCE

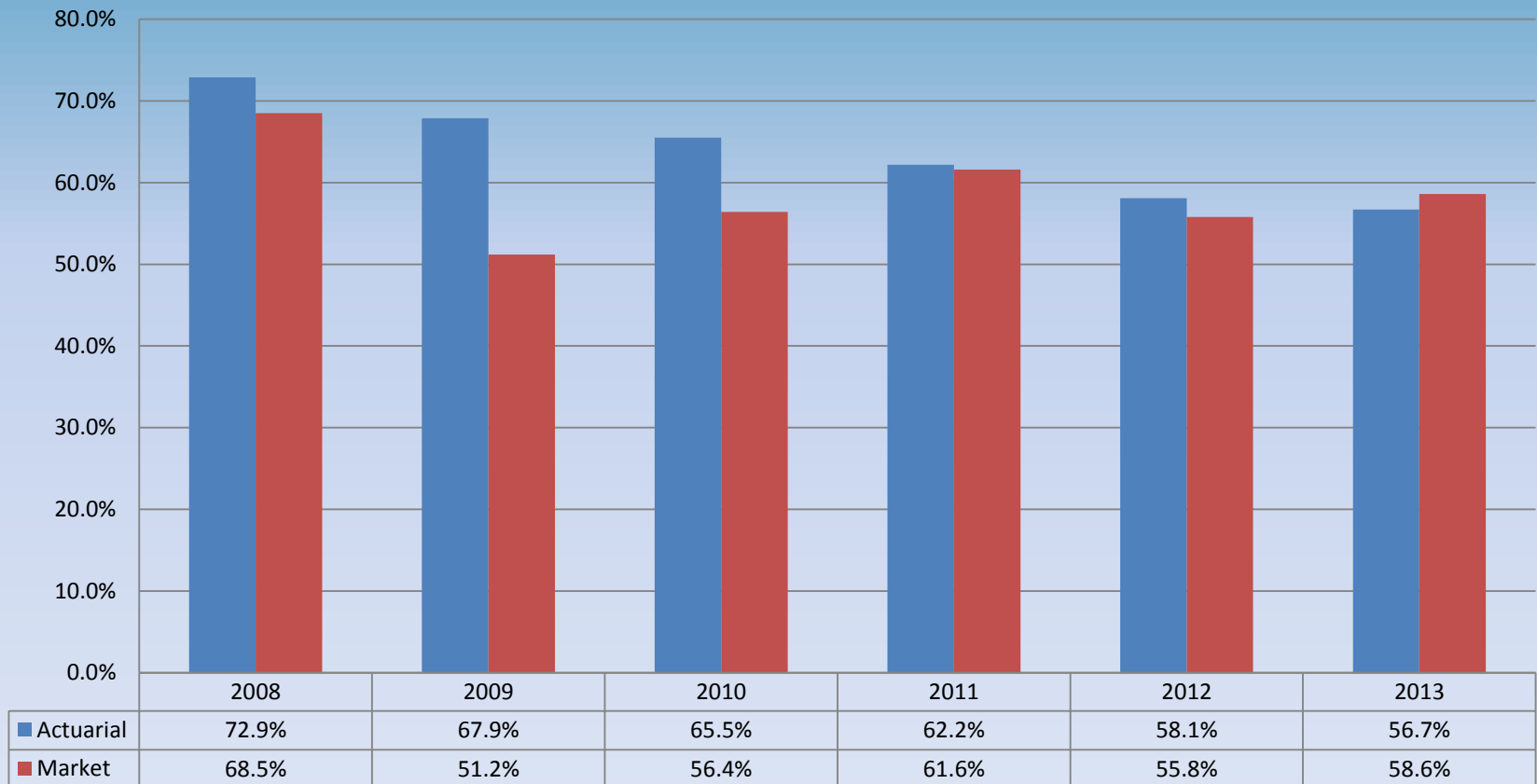


Source: June 30, 2013 Comprehensive Annual Financial Report

Actuarial Basics

Summary of Actuarial Funding Level (2008 – 2013)

CERS Hazardous PENSION

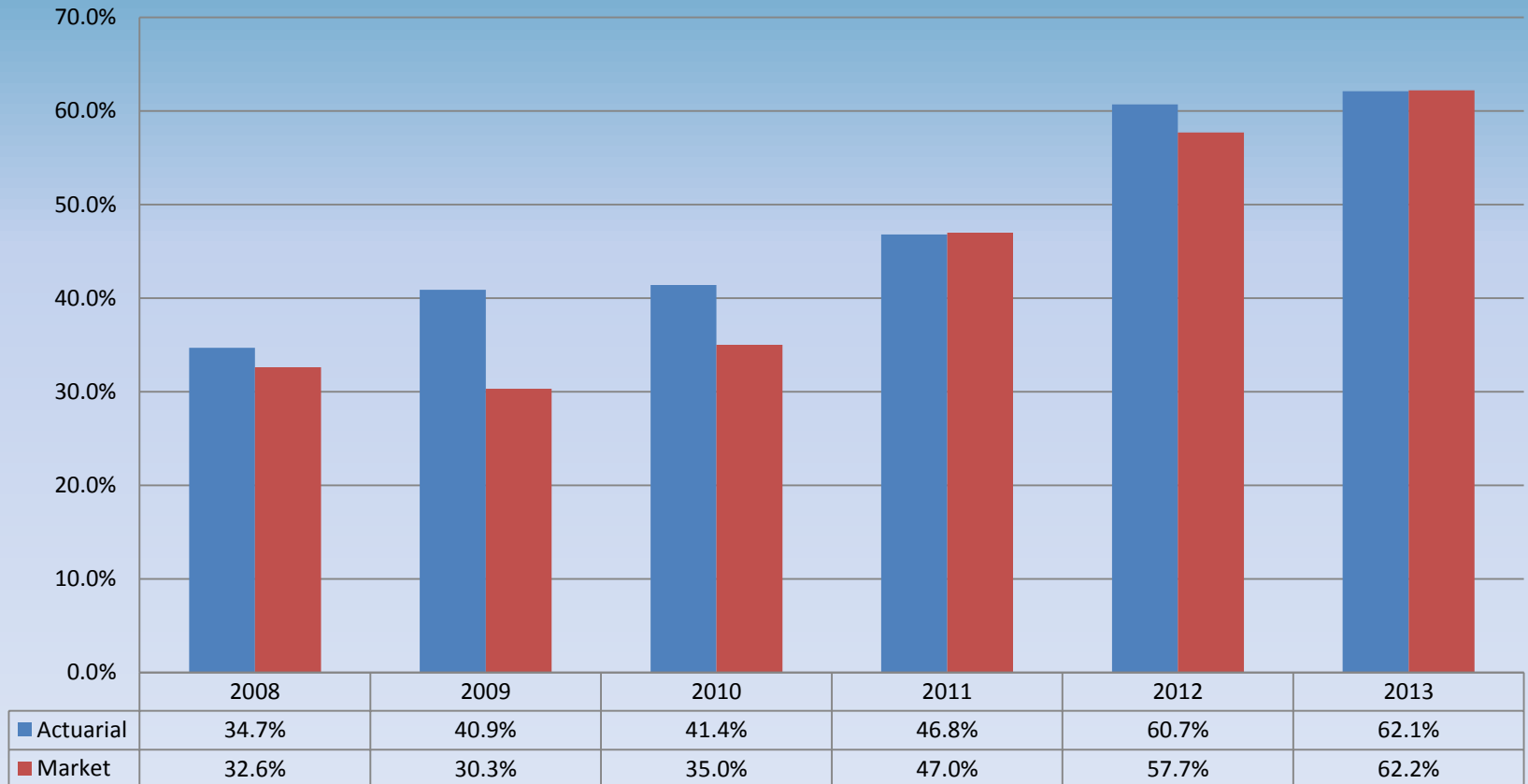


Source: June 30, 2013 Comprehensive Annual Financial Report

Actuarial Basics

Summary of Actuarial Funding Level (2008 – 2013)

CERS Hazardous INSURANCE



Source: June 30, 2013 Comprehensive Annual Financial Report

Actuarial Basics

- **Unfunded Actuarial Liability (UAL)**
 - Difference between current value of assets and liabilities
 - Represents the unfunded liability on benefits already earned by employees and retirees
 - UAL is amortized over a 30 year or shorter period, much like a home mortgage
 - The amortized payment is a part of the employer contribution rate

CERS 2013 Unfunded Liabilities

(in billions of dollars)

	2013			2012		
System	Pension	Insurance	Combined	Pension	Insurance	Combined
CERS Non-Hazardous	\$3.74	\$0.82	\$4.56	\$3.59	\$0.86	\$4.45
CERS Hazardous	\$1.32	\$0.54	\$1.86	\$1.26	\$0.54	\$1.80
TOTAL	\$5.06	\$1.36	\$6.42	\$4.85	\$1.40	\$6.25

Source: June 30, 2013 Actuarial Valuation

What Caused the Increase in Unfunded Liabilities?

- 1. Reductions to Employer Contribution Rates in KERS and SPRS**
- 2. Retiree COLA increases not pre-funded**
- 3. 2008-2009 Market Losses**
- 4. Cost Inflation for Retiree Insurance**
- 5. Compliance with GASB 43/45 (2006)**
- 6. Demographic losses**

CERS Unfunded Liability Attribution

Actuary Prepared Attribution of Unfunded Liability: CERS Non-Hazardous Pension Plan

Fiscal Year	Unfunded Actuarial Liability (Beg. Of Year)	Investment (G) / L	COLA	Benefits	Actuarial Assumptions	Demographic & Salary Experience	Other	Unfunded Actuarial Liability (End of Year)
2007	1,017	-53	118	0	0	60	51	1,192
2008	1,192	28	129	0	0	83	141	1,573
2009	1,573	344	101	0	44	36	165	2,262
2010	2,262	354	55	0	0	7	235	2,912
2011	2,912	230	62	0	0	35	49	3,288
2012	3,288	341	71	0	0	-71	-37	3,592
Total Increase		1,243	536	0	44	149	604	2,576
Attribution %		48.3%	20.8%	0.0%	1.7%	5.8%	23.4%	100.0%

What Action Has Already Been Taken to Address These Issues?

- Board completed a full review in 2003 and offered several considerations to the Legislature as it relates to benefits for future employees
- Many of these options for new hires were implemented into law by **HB 290** (2004 GA)
- Savings from these changes were estimated by KRS staff to amount to \$2.25 billion dollars realized over a 20 year period as current employees are replaced by new employees covered under the new benefits provisions

What Action Has Already Been Taken to Address These Issues?

2004 Changes:

- *Employees hired on or after July 1, 2003 earn health insurance benefits based upon dollar value*
 - *Non-Hazardous: \$10/month for each year of actual service*
 - *Hazardous: \$15/month for each year of actual service*
- *Purchases*
 - *Purchases after 8/1/2004 do not count towards vesting for health insurance benefits*
 - *Purchases made by new hires after 8/1/2004 will not count towards vesting for retirement eligibility*
 - *Purchase factor methodology reviewed and amended in 2005*

What Action Has Already Been Taken to Address These Issues?

2006 Actuarial Experience Study:

- Modified actuarial assumptions related to retiree health premium increases, retirement rates, and life expectancies will increase rates
- Eventually, GASB 43/45 and changes in actuarial assumptions (including the expected continuation of retiree health premium inflation) and COLAs will exceed changes made to stabilize rates

What Action Has Already Been Taken to Address These Issues?

2008 Changes:

- **House Bill 1** (2008 Special Session) made significant changes to retirement benefits for employees who begin participating with KRS on or after September 1, 2008
- **HB 1** also had provisions affecting current employees and retirees
 - COLA at 1.5% instead of based on CPI-U
 - Service Purchase costs now include COLA and are calculated on earliest retirement date member can retire with an unreduced benefit
 - Retired/reemployed changes for employees returning to work on or after September 1, 2008 regardless of the employee's retirement date
- **HB 1** amended KRS 61.565 to create a phase-in schedule for paying 100% of the Actuarially Required Contribution rates
 - If the General Assembly adheres to the schedule, all participating agencies will be required to pay the full employer contribution by 2025

What Action Has Already Been Taken to Address These Issues?

2013 Changes:

- **Senate Bill 2 (2013 Regular Session) created a hybrid cash balance plan for employees who begin participating with KRS on or after January 1, 2014**
 - Retirement benefits will be based upon the member's accumulated account balance, which includes:
 - Employee Contributions
 - Employer Pay Credit
 - Interest paid on the Employee Contribution and the Employer Pay Credit
 - Interest based on the fund's geometric investment returns

What Action Has Already Been Taken to Address These Issues?

2013 Changes:

- **For members participating on or after January 1, 2014, Service Credit purchases are limited to:**
 - Recontribution of Refund
 - Omitted
 - Omitted with Interest
 - Military Omitted
 - USERRA
 - Decompression
- **SB 2 removed the phase-in schedule for paying 100% of the Actuarially Required Contribution rates**
 - The General Assembly is required to pay the full actuarially required contribution rates in Fiscal Years occurring on or after July 1, 2014

What Action Has Already Been Taken to Address These Issues?

2013 Changes:

- **SB 2 also had provisions affecting current employees and retirees**
 - Recontributions of Refunds made on or after January 1, 2014 will **not** be used to determine a member's participation date in the system

 - COLA for retirees only permitted under two scenarios:
 1. If the particular system for which the COLA is provided...
 - Is Greater than 100% funded, *and*
 - The COLA will not reduce the funding level of the system below 100%, *and*
 - The COLA is authorized by the legislature to be paid using surplus funds
 2. OR if the legislature prefunds the COLA

What Action Has Already Been Taken to Address These Issues?

2013 Changes:

- **SB 2 also had provisions affecting current employees and retirees**
 - Authorizes the KRS Board to establish a
 - **Health Savings Account**
 - **Health Reimbursement Account, *or***
 - A program through which members may purchase coverage through a **Health Insurance Exchange**

KENTUCKY RETIREMENT SYSTEMS



Questions and Comments

CONTACT INFORMATION



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