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Contact: John E. Chilton
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To: All CERS Employers

Attn: Chief Executive Officer

From: John Chilton, State Budget Director

Subject: CERS pension plans

Delivered via email by KRS

I am writing to provide an update on the status of pension reform as it relates to the County Employees' Retirement System (CERS) of which your organization is a participant.

The current situation

Required pension contributions will continue as a percent of your organization's actual payroll, assuming no legislative changes occur. The rates that will apply for FY 2018-2019 are substantially higher than the previous year. The increase arises primarily from revised actuarial assumptions that the KRS Board believes are realistic and which will result in immediate decreases in the unfunded liability. The most significant revised assumptions include the long-term average investment rate of return (6.25%, previously 7.5%) and the payroll growth rate (2%, previously 4.0%). The preliminary rates for FY 2018-2019 are shown below. For reference, I have included rates that apply to KERS and State Police plans.

	CERS plans		Other KRS plans		
Percent of payroll	CERS – NH	CERS – H	KERS – NH	KERS – H	SPRS
Old assumptions	19.18%	31.55%	50.39%	21.82%	80.67%
Revised Assumptions	28.86%	50.67%	84.06%	41.12%	154.10%
FY 2019 increase	50.47%	60.62%	66.68%	88.45%	71.85%

You can determine the projected increase in the impact on your budget by referring to the schedule that accompanies this memorandum. Note that Non-hazardous and Hazardous amounts are on separate lines.

Reform efforts

As you know, discussions about changes to the pension system have become more intense since PFM Group Consulting LCC presented their "Report #3 – Recommended Options." That report presented options that Governor Bevin and legislative leadership are evaluating and considering. The recommendations provide a framework for legislation to be proposed in an upcoming special session of the General Assembly.



Addressing the crisis

It is well known that the Commonwealth's pension plans are in a crisis. While the CERS plans are in better shape than other Kentucky plans, the funding level is below 60%. This is in spite of the fact that the assessment of funding levels is based on the old actuarial assumptions that were used in the FY 2016 calculations. Applying realistic assumptions, CERS plans' funding levels are actually much lower. In addition, using the same investment rates of return that corporate plans are required to use – the Corporate Bond Index rate – the CERS unfunded liability goes from \$5 billion to \$9 billion. Across all Commonwealth plans, using the Corporate Bond Index rate, the aggregate underfunding for all of Kentucky's eight plans goes from \$33 billion to \$64 billion.

Furthermore, if Kentucky plans were subject to federal standards for single-employer private plans, the CERS plans would be designated as having severe funding shortfalls because their funded status is less than 60%. As such, federal law would require that all benefits be frozen and the plans terminated. This is true even using the old 2016 actuarial assumptions, not the more realistic discount rates and other assumptions required of private plans.

The need for significant reform is evident to anyone looking at the health of the CERS plans within that larger context, not simply benchmarking it against the health of the KERS plans.

Budget impact

While changes can be made to moderate the cost of pensions, each of the plans will need more money in order to avoid future insolvency and to safeguard future pension benefits. Implementing the appropriate changes will require a long-term commitment by employers to reforms that are necessary to rebuild the financial foundations and that allow a path to fully sustainable fiscal health.

The obvious problem is most employers cannot afford the additional pension contributions associated with the higher rates indicated above. The pension plans are in a crisis but so are employer budgets.

In order to address this predicament, the Governor and legislators believe it is appropriate to do two things:

1. Assess the status of all of the plans, not just the CERS plans, using conservative and realistic actuarial assumptions. No more pretending that everything is just fine. Everyone needs to understand the severity of the situation. To do otherwise will lead to solutions that fall short of solving the problem.
2. Examine the benefit structures with a view to lowering future costs without jeopardizing employee and retiree retirement security.

To address budgetary implications to the Commonwealth and to all employers, priorities must be set and choices must be made. Unfortunately, the choices are not happy choices – make structural changes to the pension plans and/or reduce other spending. Governor Bevin and the members of the General Assembly are considering, but have not decided upon, changes to KERS, CERS and the other state plans.

The PFM report identified changes to CERS benefit structures that would reduce the cost of each of the eight plans. These need to be considered and some of the suggested options should be implemented. I urge you to work with the Kentucky League of Cities, Kentucky Association of Counties, Kentucky School Boards Association, and other organizations to address the pension crisis and to consider ways to put the financial condition of the plans and the employer organizations on a sustainable path forward.

We look forward to working with these groups to find a solution that strengthens the Commonwealth's fiscal foundation and fulfills Kentucky's commitments to its public servants and teachers.

RETIREMENT SYSTEM CODE	RETIREMENT PLAN CODE	AGENCY CLASSIFICATION DESCRIPTION	AGENCY CODE	AGENCY NAME	FY17 REPORTED SALARY (Actuals)	FY17 Employer Contributions (Actuals)	FY18 Estimated Employer Contributions	FY19 Estimated Employer Contributions	FY18 to FY19 Payment Increase	FY18 to FY19 Percent Increase
CERS	CERSNHZ	Fiscal Courts	V028	CRITTENDEN CO FIS CT	1,816,568	339,335	348,418	524,261	175,844	50.47%
CERS	CERSNHZ	Utility Boards	L028	CRITTENDEN/LIV CO WAT DIS	465,804	87,012	89,341	134,431	45,090	50.47%
CERS	CERSNHZ	County Attorneys	W029	CUMBERLAND CO ATTORNEY	71,943	13,439	13,799	20,763	6,964	50.47%
CERS	CERSNHZ	Boards of Education	J029	CUMBERLAND CO BD OF ED	1,081,407	202,007	207,414	312,094	104,680	50.47%
CERS	CERSNHZ	Fiscal Courts	M029	CUMBERLAND CO FISCAL CT	1,022,799	191,059	196,173	295,180	99,007	50.47%
CERS	CERSNHZ	Libraries	N029	CUMBERLAND CO PUBLIC LIB	76,450	14,281	14,663	22,064	7,400	50.47%
CERS	CERSNHZ	Conservation Districts	L029	CUMBERLAND CO SOIL & WAT	26,940	5,032	5,167	7,775	2,608	50.47%
CERS	CERSNHZ	Area Development Districts	N063	CUMBERLAND VAL AREA DEV	1,097,945	205,096	210,586	316,867	106,281	50.47%
CERS	CERSNHZ	Planning Commissions	N049	CYNTHIANA HARRISON CO JPC	93,202	17,410	17,876	26,898	9,022	50.47%
CERS	CERSNHZ	Libraries	L049	CYNTHIANA/HARRISON LIBRAR	239,869	44,808	46,007	69,226	23,219	50.47%
CERS	CERSNHZ	Community Action Agencies	L026	DANIEL BOONE COMM AGENCY	2,874,660	536,987	551,360	829,627	278,267	50.47%
CERS	CERSNHZ	Parks and Recreation	L011	DANVILLE BOYLE CO REC	141,885	26,504	27,214	40,948	13,734	50.47%
CERS	CERSNHZ	Planning Commissions	R011	DANVILLE BOYLE PLANNING	124,737	23,113	23,925	35,999	12,075	50.47%
CERS	CERSNHZ	Boards of Education	J011	DANVILLE CITY BD OF ED	2,787,300	520,667	534,604	804,415	269,811	50.47%
CERS	CERSNHZ	Airport Boards	R030	DAVISS CO AIRPORT BD	280,911	52,416	53,879	81,071	27,192	50.47%
CERS	CERSNHZ	Boards of Education	M030	DAVISS CO BD OF EDUC	15,594,592	2,913,065	2,991,043	4,500,599	1,509,556	50.47%
CERS	CERSNHZ	County Clerks	39939	DAVISS CO CLERK	1,042,428	194,726	199,938	300,845	100,907	50.47%
CERS	CERSNHZ	Fiscal Courts	V030	DAVISS CO FISCAL COURT	3,539,820	1,099,468	1,116,813	1,793,627	676,814	60.60%
CERS	CERSNHZ	Fiscal Courts	V030	DAVISS CO FISCAL COURT	6,058,253	1,131,682	1,161,973	1,748,412	586,439	50.47%
CERS	CERSNHZ	Libraries	J030	DAVISS CO LIBRARY DIST	1,490,122	278,355	285,805	430,049	144,244	50.47%
CERS	CERSNHZ	Sheriff Departments	39940	DAVISS CO SHERIFF	1,927,581	598,707	608,152	976,705	368,553	60.60%
CERS	CERSNHZ	Sheriff Departments	39940	DAVISS CO SHERIFF	160,831	30,043	30,847	46,416	15,568	50.47%
CERS	CERSNHZ	Boards of Education	L054	DAWSON SPRINGS PUBLIC SCH	860,427	160,728	165,030	248,319	83,289	50.47%
CERS	CERSNHZ	Boards of Education	V419	DAYTON CITY SCHOOLS	1,185,582	221,467	227,395	342,159	114,764	50.47%
CERS	CERSNHZ	Utility Boards	M023	E CASEY CO WATER DISTRICT	246,372	46,022	47,254	71,103	23,849	50.47%
CERS	CERSNHZ	Special Districts & Boards	M097	E KY CONCEN EMPLOY PRO	1,972,087	368,386	378,246	569,144	190,898	50.47%
CERS	CERSNHZ	Boards of Education	V163	EAST BERNSTADT BD OF ED	352,270	65,804	67,565	101,665	34,100	50.47%
CERS	CERSNHZ	Utility Boards	N025	EAST CLARK CO WATER DIST	244,641	45,699	46,922	70,603	23,681	50.47%
CERS	CERSNHZ	Utility Boards	M012	EAST PENDLETON WATER DIST	270,478	50,525	51,878	78,060	26,182	50.47%
CERS	CERSNHZ	Fire Departments	L356	EASTWOOD FIRE PROT DIST	961,505	298,643	303,355	487,194	183,840	60.60%
CERS	CERSNHZ	Fire Departments	L356	EASTWOOD FIRE PROT DIST	36,068	6,737	6,918	10,409	3,491	50.47%
CERS	CERSNHZ	Ambulance Services	L031	EDMONSON CO AMBULANCE DIS	272,201	84,546	85,880	137,924	52,045	60.60%
CERS	CERSNHZ	Ambulance Services	L031	EDMONSON CO AMBULANCE DIS	209,223	39,083	40,129	60,382	20,253	50.47%
CERS	CERSNHZ	Boards of Education	J031	EDMONSON CO BD OF EDUC	2,653,420	495,659	508,926	765,777	256,851	50.47%
CERS	CERSNHZ	Conservation Districts	M031	EDMONSON CO CONSERV DIST	15,063	2,814	2,889	4,347	1,458	50.47%
CERS	CERSNHZ	Fiscal Courts	V031	EDMONSON CO FISCAL CRT	1,395,655	260,701	267,687	402,786	135,099	50.47%
CERS	CERSNHZ	County Attorneys	W031	EDMONSON COUNTY ATTORNEY	26,352	4,923	5,054	7,605	2,551	50.47%
CERS	CERSNHZ	Utility Boards	J068	ELEC PLT BD OF VANCEBURG	858,736	160,412	164,706	247,831	83,126	50.47%
CERS	CERSNHZ	Boards of Education	N047	ELIZABETHTOWN BD OF EDUC	2,939,322	549,110	563,762	848,288	284,526	50.47%
CERS	CERSNHZ	Tourist Commissions	V547	ELIZABETHTOWN TOUR/CON BU	261,219	48,310	50,102	75,388	25,286	50.47%
CERS	CERSNHZ	Boards of Education	J032	ELLIOTT CO BD OF ED	1,220,975	228,078	234,183	352,373	118,190	50.47%
CERS	CERSNHZ	Fiscal Courts	V032	ELLIOTT CO FISCAL CT	81,695	25,374	25,775	41,395	15,620	60.60%
CERS	CERSNHZ	Fiscal Courts	V032	ELLIOTT CO FISCAL CT	876,828	163,558	168,176	253,053	84,877	50.47%