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Kentucky Teacher Retirement System Funding Work Group

Introductory Issues

July 31, 2015

Goal: *Make recommendations to strengthen the solvency of the KTRS*

Brief Introduction from PTA

- Three consulting actuaries partnering for Kentucky
  - William Fornia: 35 years
  - Paul Schrader: Over 40+ years
  - Linda Bournival: Nearly 30 years
- Lots of similar experience
  - Ohio Retirement Study Council
  - Colorado reform and review
  - Prior actuarial work on non-SS teacher plans

Experience with pension reform

- Ohio
  - Also covers health care
  - 2012 reform, still fixed rate but 30-year funding target
- Colorado
  - Shared sacrifice approach
  - Sued for COLA cut (3.5% to 2.0%) but successful
- Alaska
  - Went DC in 2005, hasn't solved UAAL
  - Labor groups trying to return to DB
- Rhode Island
  - Cut accruals, froze COLA, hybrid

Experience with pension reform (continued)

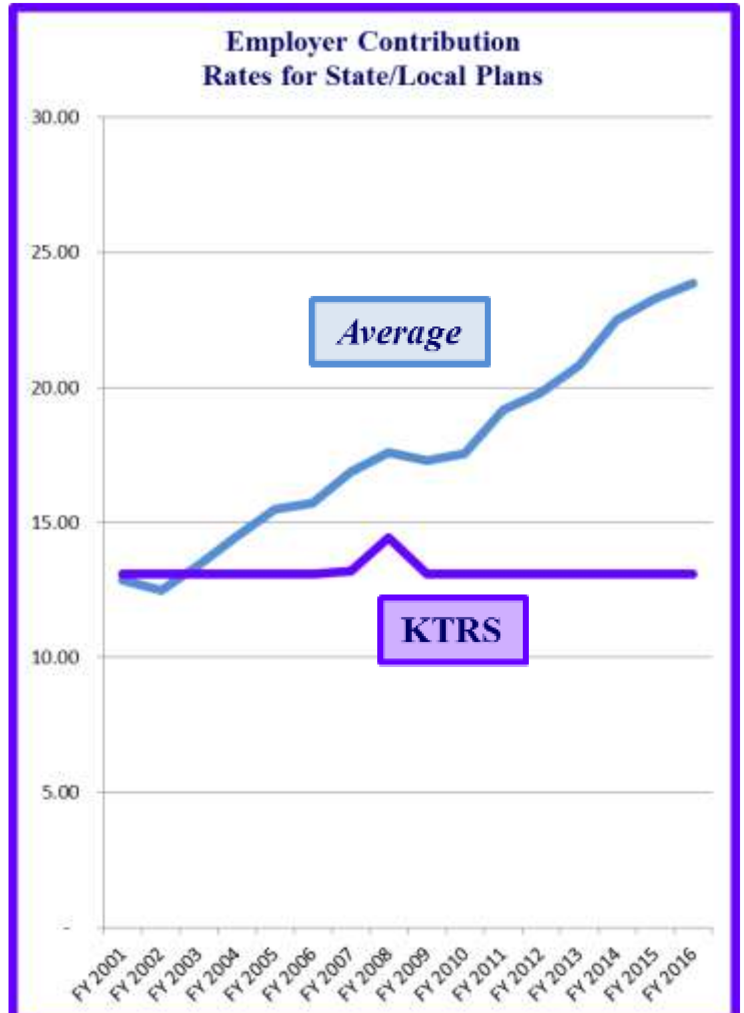
- Stockton, CA
  - No pension cut, severe retiree health cut, creditors impaired significantly in bankruptcy
- Puerto Rico
  - Added DC in 2000, POBs, still nearly insolvent
- Baltimore
  - Modified COLA, sued but won key provisions
- Detroit
  - Bankruptcy resulted in reduced accruals, plus COLA cut and other (mostly modest) benefit reductions
- South Dakota
  - Well funded plan but initiated reform to remain so
  - Sued for COLA cut (indexed to funded status), but successful

Key Points from July 17 – KTRS Presentation

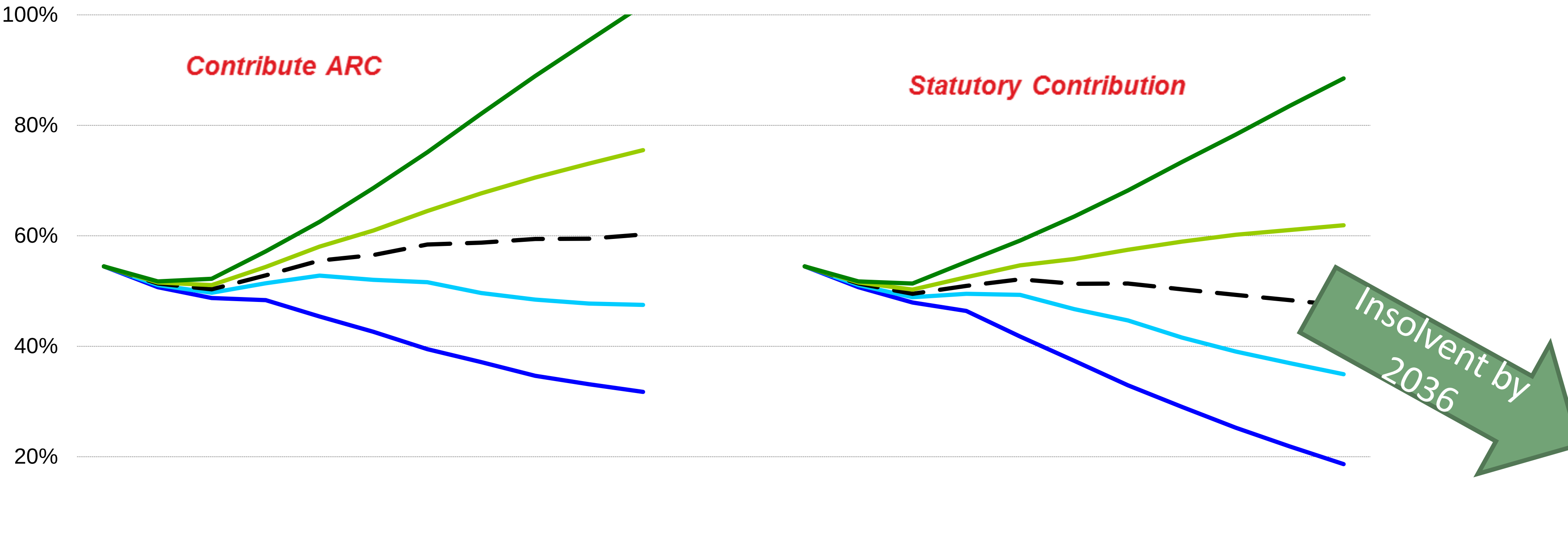
- KTRS benefits are important to Kentucky
- Future benefit normal cost is 16.75% of pay
  - Members pay 9.11%
  - Leaving 7.64% for State, only 1.44% above 6.20% Social Security would require
- KTRS investment returns are not the problem
- KTRS administrative costs are not the problem
- Many problems have been essentially "solved"
  - Air time
  - Return to work
- Have begun to prefund retiree health
  - And adopted cost control measures

Key Points from July 17 (continued)

- KTRS Statutory Contribution is significantly below the Actuarially Required Contribution
- Other States are too, but KTRS is trailing, according to Boston College study
- Currently about $500 million below ARC
  - $551 million contribution projected FY 2016
  - $487 million short of ARC
- Pension Obligation Bond helps, but primarily because it softens phase-in to ARC funding



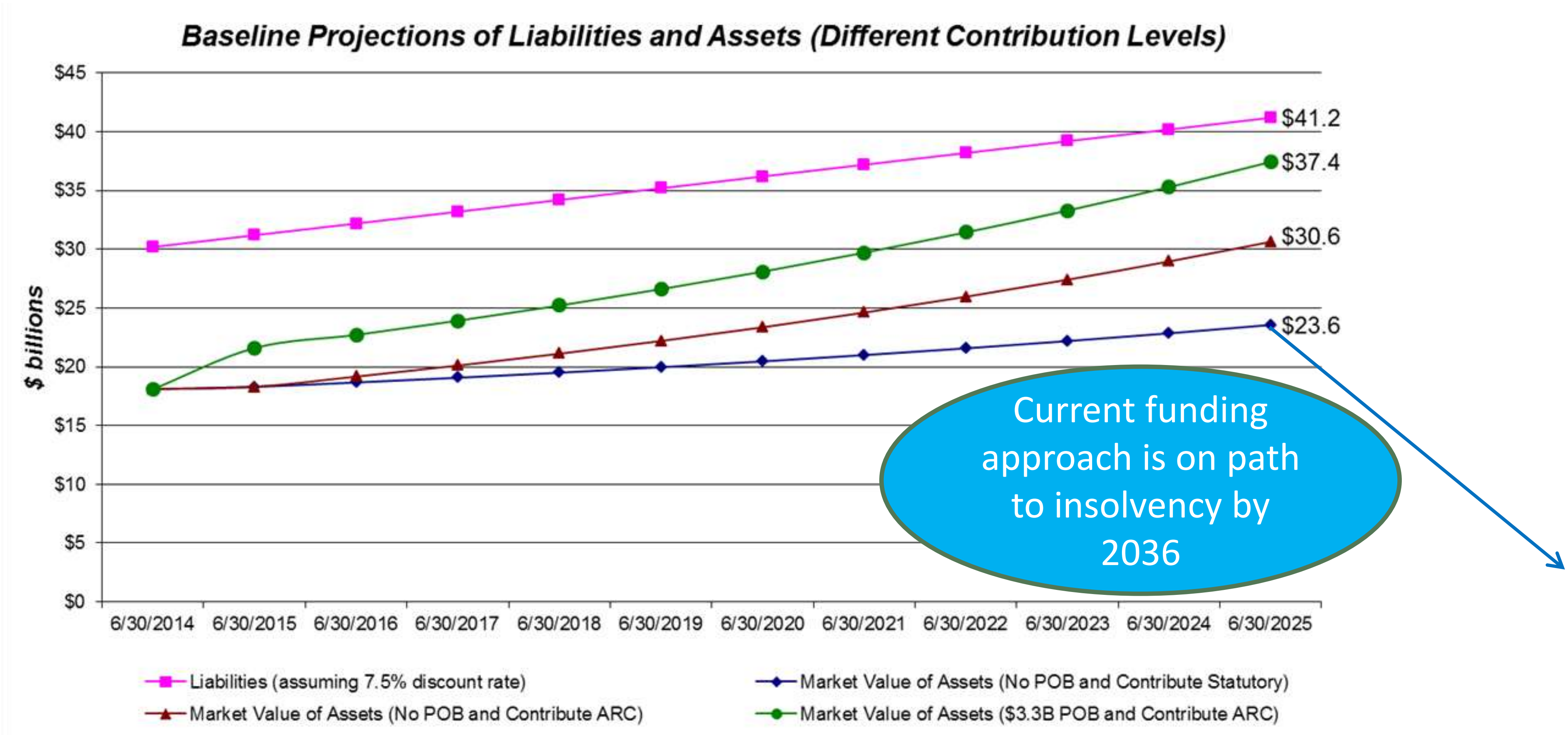
Unless contributions are increased, current plan is on road to insolvency



	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
5th %	54%	51%	49%	48%	45%	43%	39%	37%	35%	33%	32%
25th %	54%	51%	50%	51%	53%	52%	52%	50%	48%	48%	47%
50th %	54%	51%	50%	53%	56%	57%	58%	59%	59%	59%	60%
75th %	54%	52%	51%	54%	58%	61%	64%	68%	71%	73%	76%
95th %	54%	52%	52%	57%	63%	69%	75%	82%	89%	95%	102%

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	54%	51%	48%	46%	42%	37%	33%	29%	25%	22%	19%
	54%	51%	49%	50%	49%	47%	45%	42%	39%	37%	35%
	54%	51%	50%	51%	52%	51%	51%	50%	49%	48%	47%
	54%	52%	50%	52%	55%	56%	57%	59%	60%	61%	62%
	54%	52%	51%	55%	59%	64%	68%	73%	78%	84%	88%

Unless contributions are increased, current plan is on road to insolvency – another look



Key Points from July 17 (continued)

- Pension assets as of 6/30/14 were $18 billion
- But Actuarial Liability was $30 billion
- Unfunded Actuarial Liability is a problem:
  - $14 billion (on actuarial basis)
  - $22 billion (on GASB reporting basis)
- Pension multiplier has decreased from 2.5%
  - To 2.0% in first ten years, 2.5% beyond ten
  - To a further reduced rate as low as 1.7%
- Negative cash flow exacerbates funding shortfall
- COLA is 1.5% of pay, additional only provided on funded ad hoc basis

What makes pension reform successful?

- Focus on big picture
  - Current contribution approach will not sustain current benefit level
- Realize that the low hanging fruit have probably already been picked or are not enough
  - Maximizing investment return
  - Benefit tweaks (Air time, Return-to-work, COLA funding)
- Keep open mind
- Consider shared sacrifice precedent
- Realize that postponing decision will make solution more difficult

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Where We Go From Here

July 31, 2015

Goal: *Make recommendations to strengthen the solvency of the KTRS*

What are our broad alternatives

- If we don't increase contributions, we won't be able to pay current level of benefits
  - If not now, likely within 20 years
- So broad options are:
  - Increase Contributions
  - Reduce Benefits
  - Some combination of both
- Key points
  - Pension Obligation Bonds can help, but at risk, and alone is not complete solution – phase into ARC is key driver
  - What benefit changes meet our commitments, pass legal muster and minimize impact on educational professionals

What to expect August 28

- Comparisons of benefits
  - Other non-Social Security States
  - Neighbor States
- Recap of changes already made to KTRS
- Case studies of reform
  - Not a legal analysis of what's possible, but a survey of what's been done (and employee/legal/financial ramifications)
- PTA analysis of actuarial components

Future Agendas

- August 28 – Benefit analysis (PTA)
  - Comparison of KTRS benefits to other states
    - Border states
    - More importantly, states also not in Social Security
  - Overview of other pension reforms
  - Review of KTRS actuarial assumptions and methods
- September 11 – Constituency Concerns
- September 25 – PTA general presentation of broad alternatives
- October 16 – Work group feedback on alternatives
- November 6 – Begin to sketch out and draft proposal
- November 20 – Complete proposal