KENTUCKY

TEACHERS' RETIREMENT SYSTEM

April 30,2010

Historic Legislation Passes

Kentucky's Education Community, General Assembly and Governor Establish a Solution of Shared Responsibility for Long-Term Funding of Retiree Health Care

Retiree health care legislation, developed and supported by the education community, passed through the Kentucky House of Representatives and Senate, without a single negative vote, and was signed into law on Tuesday, April 13, 2010, by the Governor. This legislation helps insure that not only Kentucky's current retired teachers, but active teachers when they retire as well, will continue to receive health benefits. It also helps the pension fund.

The medical benefit, first provided in 1964, was established on a pay-as-you-go basis similar to Medicare. In other words, all dollars coming in were used to pay for retiree medical benefits as they became due, leaving no spare funds to invest to cover future costs. The source of funding consisted of contributions from active members with the state paying an equal amount. Currently these contributions are .75% of salary (1.75% for those members hired after June 30, 2008). For years now, the costs of providing retiree health care have overwhelmed the contributions generated by these two sources of funding. For the most recent year, these contributions generated only $48 million of the $182 million cost, a shortfall of $134 million.

As previously reported, to make up this growing shortfall, the state has been redirecting contributions away from the teachers' pension fund to the medical insurance fund. Since 2004, over $560 million has been redirected with the agreement it will be repaid by the state with interest over staggered 10 year terms. At this rate, even with repayment, the assets of the pension plan would be depleted by 2029. Though all involved knew this practice wasn't sustainable long-term, we are extremely grateful to the General Assembly and Governor for providing this short-term strategy without which retiree health care would have been drastically cut years ago. This short-term strategy provided needed time to develop a long-term solution.

The Shared Responsibility Solution

The KTRS Board of Trustees and Executive Secretary, Gary Harbin, have been calling attention to this growing problem for years. With the immediate urgency of the issue, the Board of Trustees and the staff of KTRS began working with constituent groups representing Kentucky's education community. This included retired teachers, active teachers, school boards, school superintendents and the state to search for a solution to this problem. Numerous meetings among these constituent groups involved reviewing many options presented by experts. From these meetings, a consensus was formed to support a solution of Shared Responsibility. This proposed solution, developed only after serious deliberations by these groups of its effect on retirees, members and employers, was introduced in the General Assembly on February 26, 2010, as House Bill 540.

House Bill 540 is a Shared Responsibility solution that provides permanent funding for retiree health care and ends the long history of underfunding this important benefit. Shared Responsibility calls upon each party (active teachers, retired teachers, school districts, and the state) to share in a piece of the solution by investing a little more now to receive substantial returns later.

The Shared Responsibility Solution for Active Teachers

Active teachers are an essential piece of the Shared Responsibility solution and were key in passing this legislation. Views of active teachers were sought throughout and though teachers will be contributing more, the long-term benefit they receive will be far greater. In short, this legislation was about helping teachers and improving their security in retirement.

Under Shared Responsibility, active members will now have medical benefits when they retire. Without Shared Responsibility, teachers would have to pay the full cost of health care, currently $7,068 per year. As is clearly evident, without medical benefits, retirement security is uncertain. The likely outcome would be that teachers would need to work much longer to make up for the loss of this benefit. Shared Responsibility means teachers will be able to retire at a time of their choice, with greater retirement security.

Effective July 1, 2010, most active members will begin contributing an additional ¼ of 1% of salary on a pre-tax basis into the medical insurance fund. For the average teacher earning $45,000 per year, the net amount will be approximately $8 per month in the first year. Over six years, this will gradually increase to three percent. Historically, salary increases over that time span have been more than sufficient to offset this amount.

Shared Responsibility Solution
Supported by:

Jefferson County Teachers Association
Kentucky Association of School Administrators
Kentucky Association of School Superintendents
Kentucky Education Association
Kentucky Education Association-Retired
Kentucky Retired Teachers Association
Kentucky School Boards Association
KTRS Board of Trustees-*fiduciary*
Universities & Community Colleges
and others

~listed in alphabetical order

The Shared Responsibility Solution for Retired Teachers

The second piece of the Shared Responsibility solution is provided by retirees who receive medical benefits. Retired teachers also are an essential piece of the Shared Responsibility solution and were very instrumental in passing this legislation. Their views and insights were sought to determine the impact of this legislation on both current and future retirees. They certainly were cognizant that Shared Responsibility would save this most important benefit for retirees and strongly supported it.

Retirees participate by paying either the Medicare Part B premium if they are age 65 and over, or by paying into the medical insurance fund the equivalent of the Medicare Part B premium if under age 65. Since retirees age 65 and over are already paying the Medicare Part B premium (standard rate of $110.50 per month) they will experience no change. Retirees under age 65, regardless of retirement date, who receive medical benefits through the Kentucky Employees' Health Plan, will begin contributing an additional amount to the medical insurance fund effective July 1, 2010. This amount is based on the Standard Medicare Part B premium that is currently paid by retirees age 65 and over. The amount will be 1/3 of the cost of the Standard Medicare Part B premium, or $37 per month (1/3 x $110.50) for the last six months of 2010. The Standard Medicare Part B premium is subject to adjustment by the Centers for Medicare and Medicaid Services each January 1st. Should that occur, the amount paid by retirees would adjust accordingly at that time.

Effective July 1, 2011, the amount will be 2/3 of the cost of the Standard Medicare Part B premium, and effective July 1, 2012, the amount will then be equal to the full Standard Medicare Part B premium paid by retirees age 65 and over. Amounts contributed will be automatically deducted from the monthly pension.

The Shared Responsibility Solution for School Districts & Other Employers

School districts and other employers provide the third piece of the Shared Responsibility solution by paying the same additional amount that active members will contribute. Shared Responsibility will save the school districts future salary costs estimated to be over $300 million per year by maintaining normal retirement patterns. To further explain, a series of negative events would occur for employers if the medical benefit for retirees is lost. As the bubble of baby boomers in America approaches retirement age, approximately one in four of Kentucky's teachers today is eligible to retire. Replacement of those teachers lowers salary costs for districts because retiring teachers on average earn $57,000 per year compared to starting teacher average salaries of $34,000. Without the medical benefit, the average retirement age would move closer to age 65, the time retirees would be eligible for lower cost coverage through Medicare. Therefore, by employers participating in Shared Responsibility, they are able to maintain normal retirement patterns and reduce the overall cost of education.

The KTRS Board of Trustees sincerely appreciates all the many active and retired members that participated in the enactment of this historic legislation. With your efforts in bringing attention to the need for funding retiree health care, this important benefit has been saved.

The Shared Responsibility Solution for the Commonwealth

Beginning July 1, 2010, the state will begin paying the net cost of medical insurance for all new retirees who are not Medicare eligible, thus providing the final piece of the Shared Responsibility solution. In addition to saving future salary costs, Shared Responsibility has other far reaching positive impacts for the Commonwealth. By pre-funding this benefit, taxpayers will be relieved of over $2.8 billion of future costs in funding retiree health care (as based on last year's actuarial report, the unfunded liability will be reduced from $6.2 billion to $3.4 billion). In addition, by relieving Kentucky taxpayers of these future liabilities, bond rating agencies will look upon future borrowings of the Commonwealth more positively, giving the state a better rating, thus a better interest rate on debt and reducing the amount of interest the Commonwealth will pay on that debt.

As originally drafted and supported by the various groups in the education community, House Bill 540 also required increased matching contributions by the state into the pension fund to begin addressing its unfunded liability. Though the final version of the bill omitted these contributions, the KTRS Board of Trustees is most appreciative that a number of members of the General Assembly stated that they will work with the education community on a solution addressing this need. Kentucky Teachers' Retirement System benefits are not only valuable to the retirement security of more than 123,000 educators; they also provide a $1.5 billion, and growing, economic stimulus that is injected annually into local economies across the Commonwealth.

Legislative leaders have applauded Kentucky's education community for their strong leadership and hard work in developing the Shared Responsibility approach that will provide the needed funding for the health care of current and future retired teachers. The pension and medical benefits are *extraordinary tools* for recruitment and retention of teachers. Protecting the integrity of these tools continues the Commonwealth's commitment to education and Kentucky's future.

(For answers to frequently asked questions, please visit www.ktrs.ky.gov "Historic Legislation Passes".)