

Kentucky County Employees Retirement System

GASB No. 74 Accounting Valuation Report
As of June 30, 2020





December 3, 2020

Board of Trustees
Kentucky Retirement Systems
Perimeter Park West
1260 Louisville Road
Frankfort, KY 40601

Re: GASB No. 74 Reporting – Actuarial Information – County Employees’ Retirement System

Dear Members of the Board:

This report provided herein contains certain information for the Kentucky County Employees’ Retirement System (CERS) in connection with the Governmental Accounting Standards Board (GASB) Statement No. 74, “Financial Reporting for Postemployment Benefit Plans Other than Pension Plans” for the fiscal year ending June 30, 2020. A separate report will be provided at a later date with additional accounting information determined in accordance with GASB Statement No. 75, “Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions”.

The liability calculations presented in this report were performed for the purpose of satisfying the requirements of GASB No. 74 and are not applicable for other purposes, such as determining the plans’ funding requirements. The plan’s liability for other purposes may produce significantly different results. This report may be provided to parties other than the Board of Trustees of the Kentucky Retirement Systems only in its entirety and only with the permission of the Board. GRS is not responsible for unauthorized use of this report.

The total OPEB liability, net OPEB liability, and sensitivity information shown in this report are based on an actuarial valuation date of June 30, 2019. The total OPEB liability was rolled-forward from the valuation date to the plan’s fiscal year ending June 30, 2020, using generally accepted actuarial principles. GASB No. 74 requires Kentucky Retirement Systems to disclose a 10-year history of certain information in the Required Supplementary Information within their comprehensive annual financial report. The exhibits provided in this report include the applicable information for historical years that were calculated in accordance with this accounting standard. Information disclosed for years prior to June 30, 2017 were prepared by KRS’s prior actuary.

The discount rate used to calculate the total OPEB liability decreased from 5.68% to 5.34% for the Non-Hazardous Fund and from 5.69% to 5.30% for the Hazardous Fund (see further discussion on the calculation of the single discount rate later in this letter). The assumed increase in future health care costs, or trend assumption, was reviewed during the June 30, 2019 valuation process and was updated to better reflect more current expectations relating to anticipated future increases in the medical costs. Also, the June 30, 2020 GASB No. 74 actuarial information reflects the anticipated savings from the repeal of the “Cadillac Tax” and “Health Insurer Fee”, which occurred in December of 2019. The assumed load on pre-Medicare premiums to reflect the cost of the Cadillac Tax was removed and the Medicare premiums were reduced by 11% to reflect the repeal of the Health Insurer Fee. There were no other material assumption changes and it is our opinion that these procedures are reasonable and appropriate, and comply with applicable requirements under GASB No. 74.

Senate Bill 249 changed the funding period for the amortization of the unfunded liability to 30 years as of June 30, 2019. Gains and losses incurring in future years will be amortized over separate 20-year amortization bases. This change does not impact the calculation of the Total OPEB Liability and only impacts the calculation of the contribution rates that would be payable starting July 1, 2020. There were no other material plan provision changes and it is our opinion that these procedures are reasonable and appropriate, and comply with applicable requirements under GASB No. 74.

The fully-insured premiums KRS pays for the Kentucky Employees' Health Plan are blended rates based on the combined experience of active and retired members. Because the average cost of providing health care benefits to retirees under age 65 is higher than the average cost of providing health care benefits to active employees, there is an implicit employer subsidy for the non-Medicare eligible retirees. GASB No. 74 requires that the liability associated with this implicit subsidy be included in the calculation of the Total OPEB Liability.

This report is based upon information, furnished to us by the Retirement System, which includes benefit provisions, membership information, and financial data. We did not audit this data and information, but we did apply a number of tests and concluded that it was reasonable and consistent. GRS is not responsible for the accuracy or completeness of the information provided by the Retirement System. Please see the "Actuarial Valuation Report as of June 30, 2019" for additional discussion of the nature of the actuarial calculations and more information related to participant data, economic and demographic assumptions, and benefit provisions. These reports should be considered together as a complete report for KRS's fiscal year ending June 30, 2020.

Single discount rates of 5.34% for the non-hazardous system and 5.30% for hazardous system were used to measure the total OPEB liability as of June 30, 2020. The single discount rates are based on the expected rate of return on OPEB plan investments of 6.25% and a municipal bond rate of 2.45%, as reported in Fidelity Index's "20-Year Municipal GO AA Index" as of June 30, 2020. Based on the stated assumptions and the projection of cash flows as of each fiscal year ending, the plan's fiduciary net position and future contributions were projected to be sufficient to finance the future benefit payments of the current plan members. Therefore, the long-term expected rate of return on insurance plan investments was applied to all periods of the projected benefit payments paid from the retirement system. However, the cost associated with the implicit employer subsidy is not currently being included in the calculation of the System's actuarial determined contributions, and it is our understanding that any cost associated with the implicit subsidy will not be paid out of the System's trust. Therefore, the municipal bond rate was applied to future expected benefit payments associated with the implicit subsidy.

The projection of cash flows used to determine the single discount rate must include an assumption regarding actual employer contributions made each future year. Except where noted below, the future contributions are projected assuming that each participating employer in the System contribute the actuarially determined employer contribution rate each future year calculated in accordance with the current funding policy, as most recently revised by Senate Bill 249, passed during the 2020 Legislative Session. This includes the phase-in provisions from House Bill 362 (passed in 2018) that applies to the CERS Funds as well as the provisions from Senate Bill 249 (passed in 2020) which kept CERS contributions level for fiscal year ending 2021.

If there is future legislation that has a resulting effect of employers making contributions less than the actuarially determined rate, we may be required to project contributions that are reflective of recent actual contribution efforts regardless of the stated funding policy (as required by paragraph 50 of GASB Statement No. 74).



Based on guidance issued by GASB in connection with GASB Statement No. 74, the 1% of pay member contributions for Tier 2 and Tier 3 members to a 401(h) subaccount is considered as an OPEB asset. As a result, the reported fiduciary net position includes these 401(h) assets. Additionally, these member contributions and associated investment income are included in the reconciliation of the fiduciary net position.

Future actuarial measurements may differ significantly from the current measurements presented in this report due to such factors as the following: plan experience differing from that anticipated by the economic or demographic assumptions; changes in economic or demographic assumptions; increases or decreases expected as part of the natural operation of the methodology used for these measurements; and changes in plan provisions or applicable law.

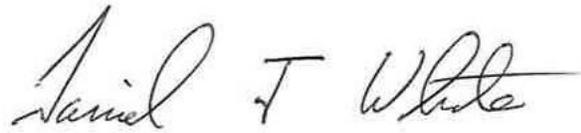
To the best of our knowledge, this report is complete and accurate and is in accordance with generally recognized actuarial practices and methods. Mr. Newton, Mr. White, and Mr. Riazi are Enrolled Actuaries. All of the undersigned are independent actuaries and consultants and members of the American Academy of Actuaries and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion herein. They are also experienced in performing valuations for large public retirement systems. This communication shall not be construed to provide tax advice, legal advice or investment advice.

Sincerely,

Gabriel Roeder Smith & Co.



Joseph P. Newton, FSA, EA, MAAA
Pension Market Leader and Actuary



Daniel J. White, FSA, EA, MAAA
Senior Consultant and Actuary



Jamie Shaw, ASA, MAAA
Consultant and Actuary



Mehdi Riazi, FSA, EA, MAAA
Consultant and Actuary



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SECTION 1

EXHIBIT 1a

Schedule of the Employers' Net OPEB Liability – CERS Non-Hazardous Plan (\$ in thousands)

Year	Total OPEB Liability (1)	Plan Fiduciary Net Position (2)	Net OPEB Liability/(Asset) (3) = (1) - (2)	Plan Fiduciary Net Position as a Percentage of the Total OPEB Liability (4) = (2) / (1)	Covered Employee Payroll ¹ (5)	Net OPEB Liability as a Percentage of Covered Employee Payroll (6) = (3) / (5)
2020	\$ 4,996,309	\$ 2,581,613	\$ 2,414,696	51.67%	\$ 2,620,585	92.14%
2019	4,251,466	2,569,511	1,681,955	60.44%	2,577,378	65.26%
2018	4,189,606	2,414,126	1,775,480	57.62%	2,570,156	69.08%
2017	4,222,878	2,212,536	2,010,342	52.39%	2,480,130	81.06%

Note:

¹ Based on derived compensation using the provided employer contribution information.



EXHIBIT 1b

Schedule of the Employers' Net OPEB Liability – CERS Hazardous Plan (\$ in thousands)

Year	Total OPEB Liability (1)	Plan Fiduciary Net Position (2)	Net OPEB Liability/(Asset) (3) = (1) - (2)	Plan Fiduciary Net Position as a Percentage of the Total OPEB Liability (4) = (2) / (1)	Covered Employee Payroll ¹ (5)	Net OPEB Liability as a Percentage of Covered Employee Payroll (6) = (3) / (5)
2020	\$ 2,245,222	\$ 1,321,117	\$ 924,105	58.84%	\$ 596,001	155.05%
2019	2,080,574	1,340,714	739,860	64.44%	583,632	126.77%
2018	1,993,941	1,280,982	712,959	64.24%	588,526	121.14%
2017	2,015,673	1,189,001	826,672	58.99%	542,710	152.32%

Note:

¹ Based on derived compensation using the provided employer contribution information.



EXHIBIT 2

Development of Single Discount Rate

	<u>CERS Non-Hazardous</u>	<u>CERS Hazardous</u>
Single Discount Rate	5.34%	5.30%
Long-Term Expected Rate of Return	6.25%	6.25%
Long-Term Municipal Bond Rate ¹	2.45%	2.45%

Notes:

¹ Fixed-income municipal bonds with 20 years to maturity that include only federally tax-exempt municipal bonds as reported in Fidelity Index's "20-Year Municipal GO AA Index" as of June 30, 2020.

EXHIBIT 3a

Schedule of the Employers' Net OPEB Liability – CERS Non-Hazardous Plan (\$ in thousands)

Change in the Net OPEB Liability	2020	2019	2018	2017
Total OPEB liability				
Service Cost	\$ 131,289	\$ 119,011	\$ 122,244	\$ 85,468
Interest on the total OPEB liability	236,126	240,352	242,048	240,854
Benefit Changes	0	0	4,306	0
Difference between actual and expected experience	505,843	(404,301)	(240,568)	(6,641)
Assumption Changes	60,225	268,842	(4,876)	520,286
Benefit Payments ¹	<u>(188,640)</u>	<u>(162,044)</u>	<u>(156,426)</u>	<u>(140,120)</u>
Net Change in Total OPEB Liability	744,843	61,860	(33,272)	699,847
Total OPEB Liability - Beginning	\$ 4,251,466	\$ 4,189,606	\$ 4,222,878	\$ 3,523,031
Total OPEB Liability - Ending (a)	\$ 4,996,309	\$ 4,251,466	\$ 4,189,606	\$ 4,222,878
Plan Fiduciary Net Position				
Contributions - Employer ²	\$ 179,521	\$ 168,905	\$ 145,809	\$ 133,326
Contributions - Member	12,964	11,801	10,825	9,158
Benefit Payments ¹	(188,640)	(162,044)	(156,426)	(140,120)
OPEB Plan Net Investment Income	9,160	137,591	202,068	264,782
OPEB Plan Administrative Expense	(903)	(877)	(761)	(789)
Other	<u>0</u>	<u>9</u> ⁴	<u>75</u> ⁴	<u>0</u>
Net Change in Plan Fiduciary Net Position	12,102	155,385	201,590	266,357
Plan Fiduciary Net Position - Beginning	\$ 2,569,511	\$ 2,414,126	\$ 2,212,536	\$ 1,946,179
Plan Fiduciary Net Position - Ending (b)	\$ 2,581,613	\$ 2,569,511	\$ 2,414,126	\$ 2,212,536
Net OPEB Liability - Ending (a) - (b)	2,414,696	1,681,955	1,775,480	2,010,342
Plan Fiduciary Net Position as a Percentage of the Total OPEB Liability	51.67%	60.44%	57.62%	52.39%
Covered Employee Payroll³	\$ 2,620,585	\$ 2,577,378	\$ 2,570,156	\$ 2,480,130
Net OPEB Liability as a Percentage of Covered Employee Payroll	92.14%	65.26%	69.08%	81.06%

Notes:

¹ Benefit payments include expected benefits due to the implicit subsidy for members under age 65. They are also offset by insurance premiums received from retirees, Medicare Drug Reimbursements, and Humana Gain Share Payments (in applicable years).

² Employer contributions include expected benefits due to the implicit subsidy for members under age 65.

³ Based on derived compensation using the provided employer contribution information.

⁴ Northern Trust Settlement



EXHIBIT 3b

Schedule of the Employers' Net OPEB Liability – CERS Hazardous Plan (\$ in thousands)

Change in the Net OPEB Liability	2020	2019	2018	2017
Total OPEB liability				
Service Cost	\$ 47,443	\$ 32,623	\$ 33,948	\$ 20,493
Interest on the total OPEB liability	115,998	116,768	118,009	113,166
Benefit Changes	0	0	484	0
Difference between actual and expected experience	38,156	(103,317)	(100,348)	(2,470)
Assumption Changes	46,925	116,618	(2,500)	391,061
Benefit Payments ¹	<u>(83,874)</u>	<u>(76,059)</u>	<u>(71,325)</u>	<u>(63,656)</u>
Net Change in Total OPEB Liability	164,648	86,633	(21,732)	458,594
Total OPEB Liability - Beginning	\$ 2,080,574	\$ 1,993,941	\$ 2,015,673	\$ 1,557,079
Total OPEB Liability - Ending (a)	\$ 2,245,222	\$ 2,080,574	\$ 1,993,941	\$ 2,015,673
Plan Fiduciary Net Position				
Contributions - Employer ²	\$ 59,662	\$ 60,445	\$ 51,615	\$ 44,325
Contributions - Member	2,762	2,458	2,173	1,708
Benefit Payments ¹	(83,874)	(76,059)	(71,325)	(63,656)
OPEB Plan Net Investment Income	2,315	73,317	109,854	143,892
OPEB Plan Administrative Expense	(462)	(434)	(376)	(381)
Other	<u>0</u>	<u>5</u> ⁴	<u>40</u> ⁴	<u>0</u>
Net Change in Plan Fiduciary Net Position	(19,597)	59,732	91,981	125,888
Plan Fiduciary Net Position - Beginning	\$ 1,340,714	\$ 1,280,982	\$ 1,189,001	\$ 1,063,113
Plan Fiduciary Net Position - Ending (b)	\$ 1,321,117	\$ 1,340,714	\$ 1,280,982	\$ 1,189,001
Net OPEB Liability - Ending (a) - (b)	924,105	739,860	712,959	826,672
Plan Fiduciary Net Position as a Percentage of the Total OPEB Liability	58.84%	64.44%	64.24%	58.99%
Covered Employee Payroll³	\$ 596,001	\$ 583,632	\$ 588,526	\$ 542,710
Net OPEB Liability as a Percentage of Covered Employee Payroll	155.05%	126.77%	121.14%	152.32%

Notes:

¹ Benefit payments include expected benefits due to the implicit subsidy for members under age 65. They are also offset by insurance premiums received from retirees, Medicare Drug Reimbursements, and Humana Gain Share Payments (in applicable years).

² Employer contributions include expected benefits due to the implicit subsidy for members under age 65.

³ Based on derived compensation using the provided employer contribution information.

⁴ Northern Trust Settlement



EXHIBIT 4a

Schedule of Employers' Contributions – CERS Non-Hazardous Plan (\$ in thousands)

Fiscal Year Ending ¹	Actuarially Determined Contribution ²	Total Employer Contributions ³	Contribution Deficiency (Excess)	Covered Employee Payroll ⁴	Actual Contributions as a Percentage of Covered Payroll
2020	\$ 124,740	\$ 129,268	\$ (4,528)	\$ 2,620,585	4.93%
2019	160,055	139,655	20,400	2,577,378	5.42%
2018	120,797	124,619	(3,822)	2,570,156	4.85%
2017	122,270	120,712	1,558	2,480,130	4.87%
2016	110,987	111,836	(849)	2,352,762	4.75%
2015	119,511	119,444	67	2,296,716	5.20%
2014	130,652	123,278	7,374	2,272,270	5.43%
2013	195,561	159,993	35,568	2,236,277	7.15%
2012	214,421	171,925	42,496	2,236,546	7.69%
2011	213,429	186,886	26,543	2,276,596	8.21%

Notes:

¹ Data for years prior to 2018 is based on contribution data provided in the 2017 CAFR, based on calculations provided by the prior actuary.

² Actuarially determined contribution for fiscal year ending 2020 is based on the contribution rate calculated with the June 30, 2018 actuarial valuation.

³ Employer contributions do not include the expected implicit subsidy included in exhibit 3.

⁴ Based on derived compensation using the provided employer contribution information.



EXHIBIT 4b

Schedule of Employers' Contributions – CERS Hazardous Plan (\$ in thousands)

Fiscal Year Ending ¹	Actuarially Determined Contribution ²	Total Employer Contributions ³	Contribution Deficiency (Excess)	Covered Employee Payroll ⁴	Actual Contributions as a Percentage of Covered Payroll
2020	\$ 56,739	\$ 57,897	\$ (1,158)	\$ 596,001	9.71%
2019	71,028	62,272	8,756	583,632	10.67%
2018	55,027	56,002	(975)	588,526	9.52%
2017	53,131	51,537	1,594	542,710	9.50%
2016	64,253	67,619	(3,366)	492,851	13.72%
2015	69,103	71,778	(2,675)	483,641	14.84%
2014	74,360	74,792	(432)	479,164	15.61%
2013	102,011	85,319	16,692	461,673	18.48%
2012	110,763	92,564	18,199	464,229	19.94%
2011	109,227	98,592	10,635	466,964	21.11%

Notes:

¹ Data for years prior to 2018 is based on contribution data provided in the 2017 CAFR, based on calculations provided by the prior actuary.

² Actuarially determined contribution for fiscal year ending 2020 is based on the contribution rate calculated with the June 30, 2018 actuarial valuation.

³ Employer contributions do not include the expected implicit subsidy included in exhibit 3.

⁴ Based on derived compensation using the provided employer contribution information.



Notes to Schedule of Employers' Contributions for FYE 2020

The actuarially determined contribution rates effective for fiscal year ending 2020 that are documented in the schedule on the previous pages were calculated as of June 30, 2018. Based on the June 30, 2018 actuarial valuation report, the actuarial methods and assumptions used to calculate these contribution rates are below:

Item	CERS Non-Hazardous	CERS Hazardous
Determine by the Actuarial Valuation as of:	June 30, 2018	June 30, 2018
Actuarial Cost Method:	Entry Age Normal	Entry Age Normal
Asset Valuation Method:	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized
Amortization Method:	Level Percent of Pay	Level Percent of Pay
Amortization Period:	25 Years, Closed	25 Years, Closed
Payroll Growth Rate:	2.00%	2.00%
Investment Return:	6.25%	6.25%
Inflation:	2.30%	2.30%
Salary Increases:	3.30% to 11.55%, varies by service	3.05% to 18.55%, varies by service
Mortality:	RP-2000 Combined Mortality Table, projected to 2013 with Scale BB (set back 1 year for females)	RP-2000 Combined Mortality Table, projected to 2013 with Scale BB (set back 1 year for females)
Healthcare Trend Rates: Pre-65	Initial trend starting at 7.00% at January 1, 2020 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 12 years. The 2019 premiums were known at the time of the valuation and were incorporated into the liability measurement.	Initial trend starting at 7.00% at January 1, 2020 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 12 years. The 2019 premiums were known at the time of the valuation and were incorporated into the liability measurement.
Post-65	Initial trend starting at 5.00% at January 1, 2020 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 10 years. The 2019 premiums were known at the time of the valuation and were incorporated into the liability measurement.	Initial trend starting at 5.00% at January 1, 2020 and gradually decreasing to an ultimate trend rate of 4.05% over a period of 10 years. The 2019 premiums were known at the time of the valuation and were incorporated into the liability measurement.
Phase-In provision	Board certified rate is phased into the actuarially determined rate in accordance with HB 362 enacted in 2018.	Board certified rate is phased into the actuarially determined rate in accordance with HB 362 enacted in 2018.



EXHIBIT 5a

Sensitivity of the Net OPEB Liability to Changes in the Discount Rate and Healthcare Trend Rate CERS Non-Hazardous Plan (\$ in thousands)

Table 1. Sensitivity of the Net OPEB Liability to Changes in the Discount Rate

1.00% Decrease, 4.34%	Current Discount Rate, 5.34%	1.00% Increase, 6.34%
\$ 3,102,175	\$ 2,414,696	\$ 1,850,046

Table 2. Sensitivity of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rate

1.00% Decrease	Current Healthcare Cost Trend Rate	1.00% Increase
\$ 1,869,578	\$ 2,414,696	\$ 3,076,209

EXHIBIT 5b

Sensitivity of the Net OPEB Liability to Changes in the Discount Rate and Healthcare Trend Rate CERS Hazardous Plan (\$ in thousands)

Table 1. Sensitivity of the Net OPEB Liability to Changes in the Discount Rate

1.00% Decrease, 4.30%	Current Discount Rate, 5.30%	1.00% Increase, 6.30%
\$ 1,254,449	\$ 924,105	\$ 657,916

Table 2. Sensitivity of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rate

1.00% Decrease	Current Healthcare Cost Trend Rate	1.00% Increase
\$ 660,393	\$ 924,105	\$ 1,248,318

APPENDIX 1

Appendix 1

Development of Baseline Claims Cost

For non-Medicare retirees, the initial per capita costs were developed using retiree claims experience for calendar year 2019. The claims were projected on an incurred claim basis, adjusted for prescription drug rebates, and loaded for administrative expense. The per capita costs shown in the table below also include HRA contributions for retirees on the CDHP plans. An inherent assumption in this methodology is that the projected future retirees will have a similar distribution by plan type as the current retirees. The fully-insured premiums KRS pays the Kentucky Employees' Health Plan are blended rates based on the combined experience of active and retired members. Because the average cost of providing health care benefits to retirees under age 65 is higher than the average cost of providing health care benefits to active employees, there is an implicit employer subsidy for the non-Medicare eligible retirees.

For Medicare retirees, the initial per capita costs were estimated based on the plan premiums effective January 1, 2020, and are used for both current and future retirees. An inherent assumption in this methodology is that the projected future retirees will have a similar distribution by plan type as the current retirees.

Age graded and sex distinct premiums are utilized by this valuation. These costs are appropriate for the unique age and sex distribution currently existing. Over the future years covered by this valuation, the age and sex distribution will most likely change. Therefore, our process "distributes" the average premium over all age/sex combinations and assigns a unique premium for each combination. The age/sex specific costs more accurately reflect the health care utilization and cost at that age.

FOR THOSE NOT ELIGIBLE FOR MEDICARE		
AGE	MALE	FEMALE
40	\$337.39	\$548.24
50	546.91	673.74
60	929.50	915.24
64	1,130.30	1,066.69

FOR THOSE ELIGIBLE FOR MEDICARE		
AGE	MALE	FEMALE
65	\$186.68	\$176.08
75	218.42	213.13
85	230.96	233.68

Mehdi Riazi is a Member of the American Academy of Actuaries (MAAA) and meets the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.



Mehdi Riazi, FSA, EA, MAAA