January 25, 2019

Members of the Public Pensions Working Group:

Greater Louisville Inc., The Metro Chamber of Commerce, represents more than 1,600 businesses in the Greater Louisville region. Our mission is to accelerate economic growth in our community by growing jobs, developing our regional workforce, and advocating for a strong, pro-business environment. On all three of these fronts, Kentucky's pension crisis has served as a seemingly immovable roadblock, slowing progress and holding our region back from reaching its full potential.

- **The uncertainty of the Commonwealth's fiscal future** discourages businesses from locating, expanding, or investing in Kentucky
- **The rising costs of annual public pension payments** prevent much-needed investments in education, workforce development programs, and infrastructure
- **The threat of future credit rating downgrades** calls into question the ability of the state, state entities, and local governments to secure funding for projects

The Public Pensions Working Group presents a unique opportunity to find a meaningful solution to these problems and to turn the page on one of the worst fiscal and economic crises in the Commonwealth's history.

Kentucky needs a bold, all-of-the-above strategy

No doubt, as members of the Working Group, you are hearing from numerous stakeholders offering recommendations on the best path forward. Some suggest an array of different structural reforms with varying degrees of impact. Others propose new sources of revenue and argue that all that is needed is consistent funding and patience while we await the full impact of the reforms from 2013. The reality is that Kentucky needs a bold, all-of-the-above strategy. For a crisis of this magnitude, every option should be on the table.

Structural reforms

In terms of structural modifications to our current systems, a difficult balance must be struck. Our public pension systems need to be competitive and appealing to attract high-quality candidates to our public sector workforce—which businesses and individuals alike depend on for vital services. This is especially true for teachers, who are responsible for molding our future generation and developing our homegrown workforce. But pensions must also come at a cost to taxpayers that is sustainable. An astounding 14 percent of the 2018-2020 general fund budget was dedicated to pensions. While the legislature should be commended for fully funding pensions, the sheer amount of taxpayer dollars allocated to pensions should be cause for serious reflection. It is a reminder of past failures and the dire need to rein in costs.

Structural reforms should focus not only on savings but stability and durability as well. Kentucky needs a pension system that minimizes future risks and maximizes long-run solvency. Simply put, the public pension systems of the twentieth century were not designed for the volatile and often economically unpredictable world we live in today. Structural changes should focus on building a durable public pension system capable of weathering the next recession and the economic downturns that accompany a rapidly changing global economy.

Just as in 2013, legislators will need to work together and approach structural reforms with an open mind. This should begin with a reconsideration of ideas from 2017 and 2018—including concepts widely (and successfully) used in the private sector and ideas put forward by PFM Group and Senate Bills 1 and 151 from last year. Several of the concepts that our members feel would be most impactful are listed below.

- Require or offer as an option defined contribution plans for employees in systems where such plans make sense
- Transition future TRS employees into hybrid cash-balance plans
- Disallow the use of sick days in determining retirement benefits
- Use the highest five years salaries for calculating teachers' retirement benefits
- Eliminate inviolable contract provisions for future teachers
- Raise the minimum retirement age for future public employees to receive full retirement benefits
- Mandate in statute level-dollar amortization for all public pension systems

Many of these ideas, such as transitioning future public employees into defined contribution plans, were dismissed too quickly, while ideas like caps on factoring sick days into retirement benefits should continue to be key parts of the conversation. The bottom line is that everything needs to be on the table when it comes to structural reform. The Working Group is a suitable venue to gather factual information on the pros and cons of these concepts.

Funding and revenue

On the issue of funding, it is critical that the General Assembly commits to fully funding pensions in all future budgetary sessions of the legislature. Given the decades it will take to pay off the Commonwealth's current liabilities, this will have to be a long-term commitment, ingrained in the culture of Frankfort to the point where not allocating the full ADC would be unthinkable. Today's strong national and state economies minimize some of the stresses of fully funding pensions, but this will not always be the case. A recent report by Moody's Analytics shows that even a moderate recession would place severe pressures on Kentucky's state budget and would dramatically accentuate the pain of public pension obligations. It will be during such times that the Commonwealth will depend on legislative fortitude to ensure fiscal responsibility. Our hope is that the 2020 budget session will follow the examples of 2016 and 2018 and allocate the full ADC, thereby helping to cement a tradition of fully funding pensions into the culture of the General Assembly.

New revenues should also be part of the solution, though—as opposed to what some have argued—not the solution itself. Rather, new revenues from sources such as expanded gaming, sports betting, and business-friendly tax reform could work alongside meaningful benefit changes and full funding of pensions to help alleviate some of the fiscal strains caused by the pension crisis. This is especially true for local governments. While House Bill 362 from the 2018 session offered much-needed temporary relief to local governments, the full bill is still due. In Jefferson County, for example, annual pension payments are projected to be $50 million more in five years than they are today. To confront this looming crisis, local governments across Kentucky should be given more options for generating revenues.

Process and litigation

Finally, a word on process and litigation: GLI expressed significant disappointment in the Kentucky Supreme Court's unfortunate ruling on Senate Bill 151 in December 2018. But regardless of one's opinion of the ruling, the General Assembly should work diligently to pass pension legislation that can not only withstand legal challenges but avoid them altogether.

Build consensus and move forward

The Greater Louisville business community is encouraged by the formation of the Public Pensions Working Group and we applaud the progress already being made to finally address the pension crisis. Undoubtedly, however, the most difficult work lies ahead. The General Assembly must work together to reach as much consensus as possible and embrace a comprehensive, sustainable solution to get Kentucky's fiscal house in order. The Working Group is well-positioned to shape and inform that process by laying the groundwork for a bold legislative package in the 2019 session.

Sincerely,

Kent Oyler
President & CEO