



COMMONWEALTH OF KENTUCKY
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Kentucky Legislators
702 Capitol Ave
Capitol Annex
Frankfort, KY 40601

Sent via Email

Re: Proposed Senate Substitute for Senate Bill 1

Dear Legislators:

Last week, I provided you a letter stating Senate Bill 1 (“SB 1”), if passed, would violate the inviolable contract that you, the General Assembly, made with Kentucky’s public employees. My office’s initial review of SB 1 identified at least twenty-one (21) such violations of the inviolable contract. Since that time, a Proposed Senate Substitute (“PSS”) has been published.¹ As with the initial bill, the Office of the Attorney General was not provided with any advanced copy of the 293-page PSS for review.

Having now reviewed the PSS, we find that it fails to cure *any* of the twenty-one (21) violations identified in SB 1, including unlawful reductions in cost of living adjustments for teachers, caps on the use of sick time, and alterations to retirement allowance calculations.

As you know, the General Assembly promised Kentucky’s public employees that, in exchange for their public service, they would be guaranteed certain retirement benefits. This promise was made in the form of a contract, which was passed into law. *See* KRS 21.480; KRS 61.692; KRS 78.852; KRS 161.714. The statutes passed by the General Assembly declared this contract to be “inviolable,” meaning the General Assembly could not later break it.

If passed into law the PSS would breach the inviolable contract, resulting in numerous lawsuits against the Commonwealth – lawsuits the Commonwealth will lose. Like my previous letter, I have provided a description of some of the PSS’s violations below:²

¹ As of this date and time of this letter, the Senate Standing Committee for State and Local Government has not adopted the Proposed Senate Substitute, but it is available at <http://www.lrc.ky.gov/SB1PSS.PDF>.

² For a comparison of my review of SB 1 and the Proposed Senate Substitute, please see my letter of February 28, 2018, available at https://ag.ky.gov/pdf_news/20180228_KY-Legislators.pdf.

1. Kentucky Teachers

The General Assembly created an inviolable contract with public educators under KRS Chapter 161. The contract protects benefits provided between KRS 161.220 and KRS 161.710. *See* KRS 161.714. The PSS amends or repeals these statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to KTRS members. Violations include:

- **Reduction of Cost of Living Adjustments:** The inviolable contract guarantees teacher retirees a 1.5% annual COLA. *See* KRS 161.620(2). Section 73 of the PSS indefinitely reduces the annual member COLA from 1.5% to 1.00%. This reduction significantly reduces guaranteed retirement benefits. As such, the PSS materially impairs the rights and benefits due to retirees, and therefore violates the inviolable contract. *See e.g.*, OAG 17-031.
- **Mandatory Annual Contribution Increases:** Under the inviolable contract, teachers are required to contribute a defined amount of their annual compensation to the retirement system's health fund. *See* KRS 161.540. Section 57 of the PSS mandates that the KTRS governing board increase member contributions by up to one percent (1%) annually under certain conditions. This increase materially impairs the rights guaranteed to KTRS members and therefore violates the inviolable contract.
- **Cap of Sick Time Used to Increase Service Credit:** The inviolable contract does not cap the amount of accrued sick leave that teachers who started before July 1, 2008, may convert to additional service credit for purposes of their retirement. *See* KRS 161.623. Section 74 of the PSS caps the amount of accrued sick leave that members may convert to the amount accrued as of December 31, 2018. This limitation materially alters and impairs the rights and benefits due to employees who started before July 1, 2008, and therefore violates the inviolable contract.
- **Increase of Years of Service Requirement for 3% Benefit Factor:** The KTRS pension plan guarantees a 3% benefit factor for calculating retirees' retirement allowances, if the member has 30 years of service. *See* KRS 161.620. Section 73 of the PSS increases the service years required for this 3% benefit factor, limiting it to employees retiring with thirty (30) years of service, who have at least twenty (20) years of that service as of July 1, 2018. While members without twenty (20) years of service may still receive the 3% benefit factor, they are forced to work thirty-five (35) years and be at least age sixty (60) upon retirement to receive the factor. Because this increase materially alters the contractual service requirements and guaranteed benefits related thereto, it violates the inviolable contract.

2. Kentucky Employees

The Kentucky Employees Retirement System ("KERS") pension rights and benefits are located at KRS Chapter 61, with the inviolable contract found in KRS 61.510-61.705. *See* KRS 61.692. The PSS amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to KERS members. Violations include:

- **Excludes Compensatory Time Payments from Creditable Compensation:** The inviolable contract allows lump-sum payments for compensatory time to be included in the creditable

compensation of Tier I nonhazardous employees.³ *See* KRS 61.510. Section 14 of the PSS expressly excludes lump-sum payments from creditable compensation for non-hazardous, Tier I employees, retiring after July 1, 2023. This exclusion materially alters and impairs the ultimate calculation of KERS members' retirement allowances, and therefore violates the inviolable contract.

- **Eliminates Uniform and Equipment Allowances from Creditable Compensation:** Under the inviolable contract, uniform and equipment allowances may be included in KERS members' creditable compensation. *See* KRS 61.510. Section 14 of the PSS expressly excludes such allowances as well as undefined "other expense allowances," paid on or after January 1, 2019, from creditable compensation. This exclusion materially alters and impairs the ultimate calculation of KERS members' retirement allowances, and therefore violates the inviolable contract.
- **Caps Service Credit for Accumulated Sick Leave:** Under the inviolable contract, KERS Tier I employees are not limited in the amount of service credit they may receive for their accrued, unused sick leave. *See* KRS 61.546. Section 16 of the PSS caps service credit for sick leave for Tier I members who retire on or after January 1, 2019. Effective January 1, 2019, for any KERS member retiring on or after January 1, 2019, the maximum amount of service credited for sick leave would be set by – and could not exceed – the amount credited for balance on December 31, 2018. Because this cap materially impairs the sick leave conversion rights and benefits guaranteed to members, it violates the inviolable contract.
- **Prohibits Use of Sick Leave for Determination of Retirement Eligibility:** The inviolable contract guarantees KERS Tier I members may use accumulated, unused sick leave to determine retirement eligibility. *See* KRS 61.546. Section 16 of the PSS prohibits KERS Tier I employees from using sick leave service credit for retirement eligibility, if they retire on or after January 1, 2019. Because this prohibition materially impairs the rights and benefits due to members, it violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions in any amount from KERS Tier I members' creditable compensation for hospital and medical insurance. *See* KRS 61.702(2)(b). Section 30 of the PSS requires an employer of a KERS Tier I member employed after July 1, 2003 to deduct up to 1% of the member's creditable compensation for purposes of hospital and medical insurance under the plan. Because this provision alters and impairs the ultimate calculation of KERS members' retirement allowances, it violates the inviolable contract.
- **Alters Final Compensation Calculation:** The inviolable contract requires Tier I hazardous employees' final compensation be calculated using the creditable compensation from the three (3) fiscal years the employee was paid the highest average monthly rate. It requires the highest five (5) years for Tier I nonhazardous employees. *See* KRS 61.510. Section 14 of the PSS requires, after January 1, 2019, that Tier I hazardous employees' final compensation be calculated using the creditable compensation from their highest three (3) *complete* fiscal years, and that the highest five (5) *complete* fiscal years be used to calculate for Tier I nonhazardous employees' final compensation. Because the PSS alters and impairs the final compensation calculation guaranteed to hazardous and nonhazardous Tier I employees, it violates the inviolable contract.

³ Tier I employees began their employment prior to September 1, 2008. Tier II employees began their employment on or after September 1, 2008 but prior to January 1, 2014.

- **Eliminates Guaranteed Annual Interest for Hybrid Cash Balance Plan Participants:** KERS Tier I and Tier II employees who opted into the current hybrid cash balance plan are guaranteed an annual interest credit of at least 4%. *See* KRS 61.597. Section 19 of the PSS removes this guarantee. Because this change materially impairs the rights of these employees, it violates the inviolable contract.

3. Kentucky State Police

The State Police Retirement System (“SPRS”) pension rights and benefits are located at KRS Chapter 16, with the inviolable contract found in KRS 16.510-16.645. *See* KRS 16.652. The PSS amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to SPRS members. Violations include:

- **Caps Service Credit for Accumulated Sick Leave:** The inviolable contract guarantees Tier I employees are not limited in the amount of service credit they may receive for their accrued, unused sick leave. *See* KRS 16.645; KRS 61.546. Section 16 of the PSS caps service credit for sick leave for Tier I members who retire on or after January 1, 2019, requiring that the maximum amount of service credited for sick leave be set by – and could not exceed – the amount credited for balance on December 31, 2018. This cap materially impairs rights and benefits due to members, and therefore violates the inviolable contract.
- **Prohibits Use of Sick Leave for Determination of Retirement Eligibility:** The inviolable contract guarantees SPRS Tier I members may use accumulated, unused sick leave to determine retirement eligibility. *See* KRS 16.645; KRS 61.546. Section 16 of the PSS prohibits SPRS Tier I employees from using sick leave service credit for retirement eligibility, if they retire on or after January 1, 2019. This prohibition materially impairs rights and benefits due to members, and therefore violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions in any amount from SPRS Tier I members’ creditable compensation for hospital and medical insurance. *See* KRS 16.645; KRS 61.702(2)(b). Section 30 of the PSS requires an employer of a SPRS Tier I member, employed after July 1, 2003, to deduct up to 1% of the member’s creditable compensation for purposes of hospital and medical insurance under the plan. Because this provision alters and impairs the ultimate calculation of SPRS members’ retirement allowances, it violates the inviolable contract.

4. County Employees

The County Employees Retirement System (“CERS”) pension rights and benefits are located at KRS Chapter 78, with the inviolable contract found in KRS 78.510-78.852. *See* KRS 78.852. The PSS amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to CERS members. Violations include:

- **Excludes Compensatory Time Payments from Creditable Compensation:** The inviolable contract allows lump-sum payments for compensatory time to be included in the creditable compensation of Tier I nonhazardous employees. *See* KRS 78.510. Section 15 of the PSS expressly excludes lump-sum payments from creditable compensation for non-hazardous, Tier I employees, retiring after July 1, 2023. This exclusion materially alters and impairs the ultimate calculation of CERS members’ retirement allowances and therefore violates the inviolable contract.

- **Eliminates Uniform and Equipment Allowances from Creditable Compensation:** Currently, uniform and equipment allowances may be included in CERS members' creditable compensation. *See* KRS 78.510. Section 15 of the PSS expressly excludes uniform and equipment allowances as well as undefined "other expense allowances," paid on or after January 1, 2019, from creditable compensation. This exclusion materially alters and impairs the ultimate calculation of CERS members' retirement allowances, and therefore violates the inviolable contract.
- **Caps Service Credit for Accumulated Sick Leave:** The inviolable contract guarantees that CERS Tier I employees are not limited to the amount of service credit they may receive for their accrued, unused sick leave. Tier II employees can receive up to twelve (12) months of service credit. *See* KRS 78.616. Section 17 of the PSS caps service credit for sick leave for CERS members who retire on or after January 1, 2019, requiring the maximum amount of service credited for sick leave be set by – and not exceed – the amount credited for balance on December 31, 2018. Because the cap materially impairs the sick leave rights and benefits due to CERS members, it violates the inviolable contract.
- **Prohibits Use of Sick Leave for Determination of Retirement Eligibility:** The inviolable contract guarantees CERS members may use accumulated, unused sick leave to determine retirement eligibility. *See* KRS 78.616. Section 17 of the PSS prohibits CERS employees from using sick leave service credit for retirement eligibility, if they retire on or after January 1, 2019. This prohibition materially impairs rights and benefits guaranteed to CERS members, and therefore violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions, in any amount, from CERS Tier I members' creditable compensation for hospital and medical insurance. *See* KRS 78.545; KRS 61.702(2)(b). Section 30 of the PSS requires an employer of a CERS Tier I member, employed after July 1, 2003, to deduct up to 1% of the member's creditable compensation for purposes of hospital and medical insurance under the plan. As this provision alters and impairs the ultimate calculation of CERS members' retirement allowances, it violates the inviolable contract.
- **Alters Final Compensation Calculation:** The inviolable contract requires CERS Tier I hazardous employees' final compensation to be calculated using the creditable compensation from the three (3) fiscal years the employee was paid the highest average monthly rate. It requires the highest five (5) years for CERS Tier I nonhazardous employees. *See* KRS 78.510. Section 15 of the PSS requires, after January 1, 2019, that CERS Tier I hazardous employees' final compensation be calculated using the creditable compensation from their highest three (3) *complete* fiscal years, and that the highest five (5) *complete* fiscal years be used to calculate CERS Tier I nonhazardous employees' final compensation. Because this provision alters and impairs the ultimate calculation of CERS members' retirement allowances, it violates the inviolable contract.
- **Eliminates Guaranteed Annual Interest for Hybrid Cash Balance Plan Participants:** CERS Tier I and Tier II employees who opted into the current hybrid cash balance plan are guaranteed an annual interest credit of at least 4%. *See* KRS 61.597; KRS 78.545. Section 19 of the PSS removes this guarantee. Because this change materially impairs the rights of these employees, it violates the inviolable contract.

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The provisions of the PSS would undeniably breach the guarantees of the inviolable contract by significantly reducing the benefits and rights of retirees. The Kentucky Supreme Court has held that even a "...threat to those promised benefits might well run afoul of" Kentucky's Constitution. *Jones v. Bd. of Trustees of Kentucky Ret. Sys.*, 910 S.W.2d 710, 713 (Ky. 1995). For these reasons, it is our conclusion that a court will not uphold these violations.

As the chief law officer of the Commonwealth and the people's lawyer, I urge that you not break the inviolable contract you made with Kentucky state employees, teachers, firefighters, social workers, police officers, and other hardworking members of these systems.

Sincerely,

A handwritten signature in blue ink that reads "Andy Beshear". The signature is written in a cursive, flowing style.

Andy Beshear
Attorney General