

# **Firefighters' & Rescue Squad Workers' Pension Fund State Contribution Rate Stabilization Policy (SCRSP)**

## ***Policy Purpose***

This policy is being developed as required by the N.C. General Assembly under Session Law 2016-108. Section five of that legislation states, "The Board of Trustees of the Local Governmental Employees' Retirement System shall develop a 'State Contribution Rate Stabilization Policy' for the North Carolina Firefighters' and Rescue Squad Workers' Pension Fund and report it to the Office of State Budget and Management and the Fiscal Research Division on or before March 1, 2017." The proposal below was presented to the Board of Trustees of the Retirement System on October 27, 2016 in anticipation of a vote by the Board in January 2017.

## ***Policy Objectives***

This policy establishes how the Board of Trustees (The Board) of the Local Governmental Employees Retirement System will develop an annual appropriation amount to recommend to the General Assembly to fund the Firefighters' and Rescue Squad Workers' Pension Fund (FRSWPF) for the next five years or until the next experience review. It further describes when benefit increases and member contribution increases will be considered and recommended.

## ***State Contribution Rate Stabilization: Development of The Board's Annual Appropriation Recommendation***

- The SCRSP is being developed because low interest rates and volatile investment markets are likely to increase the volatility of employer contribution rates, resulting in roller coaster appropriations which are difficult to plan for and which create incentives within the appropriations process for programs that compete with the FRSWPF over a limited pool of revenue to increase their recurring funding requirements even though a reduction to the FRSWPF appropriation would effectively be nonrecurring. The recommended minimum increase to the annual appropriation in the policy is also designed to mirror the estimated growth rate tax on gross property insurance as provided for in N.C. Gen. Stat. § 105.228.5(d)(3), for the reasons described below.
- An "underlying Actuarially Determined Employer Contribution (ADEC)" is developed based on the Board's adopted assumptions for the FRSWPF. This number is compared to the current General Fund appropriation for the FRSWPF. The Board will then recommend to the General Assembly the higher of the underlying ADEC or \$350,000 greater than the current year's appropriation. This recommended appropriation, if subsequently enacted by the General Assembly, will result in full funding of the annual actuarially determined contribution (underlying ADEC) for the FRSWPF each year.
- The annual state appropriations recommendation developed under this policy will be deemed by the Board to be the annual actuarially determined employer contribution for funding purposes (funding ADEC) for the FRSWPF.

### ***Benefit Enhancements: Development of Recommended Benefit Changes and Member Contribution Rates***

- In addition to the rate stabilization feature, this policy will provide a mechanism for the Board to make recommendations to the General Assembly to improve the benefit structure or protect the value of the benefit from the impact of inflation, but will limit the scope of those recommendations by requiring consideration of:
  1. the year-over-year change in the Consumer Price Index for All Urban Consumers (CPI-U), U.S. City Average, all items, not seasonally adjusted, standard reference base, as published by the Bureau of Labor Statistics of the U.S. Department of Labor;
  2. the growth rate of revenue to the state provided by the tax on gross property insurance as provided for in N.C. Gen. Stat. § 105.228.5(d)(3). Currently the tax on premiums is 0.74% of 10% of the gross premiums for automobile physical damage coverage and 0.74% of 100% of the gross premiums for all other property coverage. Three other programs benefitting firefighters and rescue squad workers are paid for directly out of the proceeds of this tax, with the remainder being transferred to the General Fund to partially offset the cost of the FRSWPF;
  3. an evaluation of whether sufficient funding is available to improve the benefit without adding unfunded liability for pension debt to the state's balance sheet where there are no funds reserved to pay for it; and
  4. an evaluation of how the proposed change affects progress towards the Board's funding goals.
- This policy additionally sets a funding goal of a 50/50 split between member and state contributions toward the normal cost portion of the annual contribution, with the state additionally paying 100% of the unfunded accrued liability portion of the annual contribution. The policy will keep the unfunded liability associated with the plan as close to zero over time as is practicable and aggressively reduce the unfunded balance in virtually all years.
- This policy will further require immediate realization of the cost to the pension fund of benefit increases or enhancements. This means that the cost of benefit improvements will be paid for by undistributed investment gains, which will be reserved and amortized over a 12-year period to match the current amortization of the associated liabilities. As a result, these improvements will no longer result in new unfunded liability stemming from benefit enhancements without reserving sufficient investment gains to pay for the increases. This change requires an amendment to the assumptions adopted by the Board in January, 2016. Optionally, the General Assembly could also immediately realize the cost of benefit enhancements paid for by appropriations in the same manner.
- This policy will be in effect until the next experience review and will then be reset based on the results of that review.