North Carolina
Total Retirement Plans

STATE TREASURER OF NORTH CAROLINA
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January 25, 2024

Summary of Funding/Benefits Alternatives for Recommendations and Decisions for Fiscal Year Ending in 2025

Local Governmental Employees' Retirement System (LGERS) Board of Trustees

Executive Summary

This document summarizes alternatives for the Board's funding and benefits recommendations and decisions for the fiscal year ending in 2025.

For LGERS itself, the Board sets employer contribution rates and has limited authority to provide increases to ongoing retirement benefits or one-time supplement payments to beneficiaries. For the other benefit programs described in this memo, the Board does not establish funding or benefit requirements itself. For those programs, the Board may make recommendations to the legislature informed by the most recent annual valuation reports from the consulting actuaries (Buck), published in October 2023.

Staff believes the following are substantive issues for the Board to consider:

(1) Establishment of employer contribution rates for LGERS.

(2) Whether to recommend a benefit improvement under the Firefighters' and Rescue Squad Workers' Pension Fund (FRWSPF). Under the Board's policy, such a recommendation would require a simultaneous recommendation to increase the monthly member contribution rate from $10 to $15.

The remainder of this memo provides details regarding each Retirement System.

LGERS

Issue. G.S. 128-30(d)(5) requires that employer contributions to LGERS in each year "shall not be less than the sum of the rate per centum known as the actuarially determined employer contribution [ADEC] rate… as adjusted under a contribution rate policy adopted by the Board of Trustees and known as the 'required employer contribution' rate." G.S. 128-30(d)(2a) requires that the ADEC rate "shall be calculated annually by the actuary using assumptions and a cost method approved by the Actuarial Standards Board of the American Academy of Actuaries and selected by the Board of Trustees."

1. ADEC Prior to Contribution Rate Policy

The most recent LGERS actuarial valuation report documents the ADEC rates for the fiscal year ending in 2025. The "ADEC Prior to Contribution Policy" is the mathematical contribution rate that would fund the system using the Board's assumptions and methods adopted on January 28, 2021, and plan population and asset information as of December 31, 2022. For employees other than law enforcement officers (non-LEOs), the "ADEC Prior to Contribution Policy" is 12.66% of pay. For law enforcement officers (LEOs), it is 14.69% of pay.

2. Adjustment for Employer Contribution Rate Stabilization Policy (ECRSP)

The Board adopted the current ECRSP on April 29, 2021. This policy serves to provide predictable incremental increases in the employer contribution rate to protect against potential adverse experience for the five fiscal years ending 2023 through 2027. **The recommended contribution rates for the fiscal year ending in 2025 under the ECRSP are 13.60% of covered pay for non-LEOs and 15.10% of covered pay for LEOs.**

For non-LEOs, the rate is determined as the prior year's policy contribution (12.85%) plus 0.75%.[1] For LEOs, the rate is determined as the non-LEO rate (13.60%) plus 1.50%.[2] These ECRSP rates have the effect of increasing the ADEC from the rates in part (1), by a total of $72 million for the third year of the five-year ECRSP.[3] They represent an increase of $67 million from the amounts employers are expected to pay for the fiscal year ending 2024.

Cost of Living Adjustment to Retirement Allowances (COLA) or One-Time Supplements. Under G.S. 128-27(k) and (k1), the Board may authorize a COLA no greater than 4%, or a one-time supplement that is no greater than 4% of the annual retirement allowance, under the following limitations:

- Any COLA or one-time supplement must be no greater than inflationary increases defined by statute.
- If the Board authorizes a one-time supplement, the Board must also determine that it will not provide a COLA taking effect in the same year as the one-time supplement.

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[1] Additional adjustments would have been required if there had been any enacted change in benefits, assumptions, or methods, not yet incorporated in the policy contribution, with an effect measured by the consulting actuary. However, there have been no such changes. Another adjustment would have been required if the non-LEO rate described in part (1) above (12.66%) differed from the policy rate of 13.60% by more than 1.00% of compensation, but it does not.

[2] Additional adjustments would have been required if there were enacted LEO-specific changes in benefits not yet incorporated in the policy contribution, with an effect measured by the consulting actuary, but there have been none.

[3] As illustrated in the footnotes to the "Summary" page of this document, the approximate dollar amounts for appropriations effective July 1, 2024, are estimated using the "Estimated State Payrolls for Retirement Appropriations Purposes for the 2023 Session of the North Carolina General Assembly," set forth in a letter from the Executive Director of the Retirement Systems to the State Budget Director and the Director of the Fiscal Research Division of the General Assembly, dated March 14, 2023. For example, the approximate increase in ADEC ($72 million) is estimated as $1,449,339,000 (the LGERS LEO payroll from the aforementioned memo) multiplied by 0.41% (the difference between 15.10% in part 2 and 14.69% in part 1), plus $6,981,011,000 (the LGERS non-LEO payroll) multiplied by 0.94% (the difference between 13.60% in part 2 and 12.66% in part 1). Once a similar payroll letter is finalized for the 2024 Session of the General Assembly, the dollar amounts would change in accordance with the new estimated payroll amounts.

- The cost of a COLA or supplement authorized by the Board is limited to the actuarial investment gains. Notwithstanding the amount of investment gains experienced in a year, the ECRSP provides that the employer contribution for any year through fiscal year ending in 2027 will be adjusted for the effect of any benefit change taking effect during the year. This would include the cost of COLAs or supplements.

In the latest actuarial valuation report, the Board's consulting actuary stated that "an actuarial investment loss was incurred during 2022, and there are no investment gains available to support authorization by the LGERS Board of Trustees of either of the following: (1) a Cost-of-Living Adjustment (COLA) that would take effect on July 1, 2024; or (2) a one-time supplement to participants in receipt of benefits on September 1, 2024, payable October 2024."

Policy Option for Consideration by the Board of Trustees. Establish the employer contribution rates in accordance with the ECRSP for the fiscal year ending in 2025, equal to 15.10% for LEOs and 13.60% for all other employees. This requires an increase of approximately $67 million in employer contributions as compared to the fiscal year ending in 2024.

Firefighters' and Rescue Squad Workers' Pension Fund (FRSWPF)

Issue. The Board adopted the State Contribution Rate Stabilization Policy (SCRSP) on April 29, 2021. Under Section IV of the SCRSP, the recommended State contribution for the fiscal year ending in 2025, prior to any adjustment for benefit changes, is the greater of (1) the appropriation for the fiscal year ending in 2024, plus $350,000; or (2) the underlying actuarially determined contribution (ADEC) determined by the consulting actuary for the fiscal year ending in 2025. The ADEC for the fiscal year ending 2025 is the mathematical contribution amount that would fund the system using the Board's assumptions adopted on January 28, 2021, and plan population and asset information as of December 31, 2022.

Item (1) is equal to the recommended and actual appropriation for the fiscal year ending 2024 ($20,052,208) plus $350,000, or $20,402,208. Item (2), the underlying ADEC, is $2,350,959 according to the most recent FRSWPF actuarial valuation report. Therefore, the SCRSP results in a recommended State contribution of $20,402,208 for the fiscal year ending in 2025, which is the greater of item (1) or item (2). This is $350,000 greater than the appropriated amount for the fiscal year ending in 2024. The SCRSP provides that adjustments to this recommendation should be considered in relation to benefit increases as described below.

Benefit Increase. Under Section V of the SCRSP, the Board could recommend that the General Assembly increase the pension amount of $170 per month by up to $5, subject to two conditions.[4]

- The first condition is that, along with any recommended benefit increase, the Board would recommend that the member contribution rate be increased from $10 to $15 per month. This would increase the members' share of the cost of ongoing benefit accruals from about 33% (the current figure) to about 48%-49% (depending on the amount of the recommended benefit increase).
- The second condition is that, along with any increase in the benefit, the Board would recommend an additional appropriation at least equal to the "benefit improvement funding requirement" (BIFR). The consulting actuary has estimated that based on the funded position of the plan, the BIFR would be $0 for any increase in benefits up to $5 per month, as outlined in the table below.

Table 1: Benefit Improvement Costs (BIFR) Based on Buck's 12/31/2022 Actuarial Valuation

Monthly Benefit	A: Full Actuarial Cost	B: Actuarial Surplus at 12/31/22	C: FY 2025 SCRSP Funding > ADEC	D: Net Funding Requirement (BIFR), A + B + C if Positive
$170 (Current)	$0	($20,360,629)	($18,051,249)	$0
$171	$2,952,826	($20,360,629)	($18,051,249)	$0
$172	$5,905,651	($20,360,629)	($18,051,249)	$0
$173	$8,858,477	($20,360,629)	($18,051,249)	$0
$174	$11,811,303	($20,360,629)	($18,051,249)	$0
$175	$14,764,128	($20,360,629)	($18,051,249)	$0

[4] The SCRSP provides that the Board may recommend a benefit increase if all of four conditions are met. The first condition is that the benefit increase is not greater than the most recent June-over-June increase in the Consumer Price Index. That increase was 2.97%, which would equate to an increase in the pension from $170 to $175 (i.e., $176 would exceed this limit). The second condition is that the Board recommends an additional appropriation if required, as outlined in these materials. The third condition is that the Board recommends an adjustment to the member contribution rate as outlined in these materials. The fourth condition is that the Board consider any change that has been made to the tax on gross premiums on property insurance. This tax is provided under G.S. 105-228.5. Under S.L. 2023-7 (House Bill 76, "Access to Healthcare Options"), the General Assembly expressed its intention to fund the nonfederal share of the cost of NC Health Works in part by applying anticipated revenue increases from the gross premium tax that would result from the implementation of NC Health Works. Under Section 30.4.(a) of S.L. 2023-134 (House Bill 259, "2023 Appropriations Act"), the General Assembly redirected a portion of the revenue from the gross premium tax, for the 2023-2025 fiscal biennium only, from the Workers' Compensation Fund under G.S. 58-87-10 to the Firefighters' Health Benefits Pilot Program established in Section 30.4A of S.L. 2021-180. In the judgment of Retirement Systems staff, these legislative changes are not material to the Board's analysis.

In assessing the durability of the funding surplus as of December 31, 2022, the Board may wish to consider that, as of December 31, 2022, the market value of assets was $48 million less than the actuarial value. That is, although there was a funding surplus of $20 million on an actuarial value basis (column B), there was a funding shortfall of $28 million on a market value basis.

Policy Options for Consideration by the Board of Trustees.

- The Board could recommend a State appropriation for the fiscal year ending in 2025, equal to $20,402,208, with no benefit improvement recommended. This would require an increase of $350,000 in the appropriation as compared to the fiscal year ending in 2024.
- The Board may recommend a benefit improvement based on Table 1 above, in conjunction with increasing the member contribution rate from $10 to $15 per month. In this scenario, the Board's policy does not require any additional request of State appropriations (since the BIFR is $0 for all rows in Column D of Table 1). However, the SCRSP also does not prevent the Board from requesting additional State appropriations, and it would be reasonable to request an appropriation in any amount up to the Full Actuarial Cost (Column A of Table 1).

Registers of Deeds' Supplemental Pension Fund (RODSPF)

Issue. The most recent valuation report shows the recommended Actuarially Determined Employer Contribution (ADEC) for the fiscal year ending in 2025. The ADEC for FY 2025 is the mathematical contribution amount that would fund the system using the Board's assumptions adopted on January 28, 2021, and plan population and asset information as of December 31, 2022. The estimated ADEC of $0 for the fiscal year ending in 2025 is less than the 1.5% of monthly receipts collected pursuant to Article 1 of Chapter 161 of the N.C. General Statutes. (Statutory amounts collected were $1,041,096 in calendar year 2022 and $1,213,547 in calendar year 2021.) Additionally, the fund is over-funded with a funded ratio of 155.8% as of December 31, 2022.

Based on these facts, the monthly benefit amount could be increased. However, increasing the maximum monthly benefit would make it more likely that the ADEC in a future year would be greater than $0.

Policy Option for Consideration by the Board of Trustees. Recommend no change to the current benefit structure. ***Making no recommendation does not require a vote of the Board.***

Death Benefit Plans

Death Benefit Plan for Members of LGERS

Issue. The actuarial valuation of the Death Benefit Plan for members of LGERS as of December 31, 2022, shows that the plan has liabilities of $54.2 million. Against these liabilities, the plan has current assets of $77.5 million. Prospective contributions by the participating employers have a present value of $42.4 million. The present and prospective assets, which amount to $119.9 million, exceed the liabilities of $54.2 million by $65.7 million.

Policy Option for Consideration by the Board of Trustees. Recommend no change to the current contribution rates or benefit structure. ***Making no recommendation does not require a vote of the Board.***

Retirees' Contributory Death Benefit Plan

Issue. Benefits payable under the Retirees' Contributory Death Benefit Plan are supported entirely by the contributions of the participants and the investment earnings on those contributions. The actuarial valuation as of December 31, 2022, shows that the plan has liabilities of $1,497,531,423. Against these liabilities, the plan has current assets of $245,073,375. Prospective contributions of participants eligible for benefits have a value of $1,025,054,657. The total present and prospective benefits amount to $1,270,128,032, which are less than the liabilities of $1,497,531,423 by $227,403,391. The Board's consulting actuary has advised that, based on the assumptions of the actuarial valuation, the current assets and contribution rates of the plan are not adequate with the current plan provisions and contribution rates. Pursuant to S.L. 2020-29, no decision of either the State Board or the Local Board related to this plan can take effect unless and until the same decision has been made and voted on by the other Board.

In January 2022, the Boards directed RSD staff to engage with the consulting actuary to identify and study alternative actions that would help to address the projected funding shortfall. This study was presented to the Boards in January 2023. In April 2023, the Boards voted unanimously (among those present) to recommend that the General Assembly enact legislation to add the State Employees' Benefit Trust (SEBT) described in G.S. 135-7(g) to the list of "Retirement Systems" funds in G.S. 147-69.2(b)(8). This would allow the funds to be invested in the Retirement Systems pool. Buck estimated that this alternative would have improved the measured shortfall/surplus of the Contributory Death Benefit Plan by $281 million as of December 31, 2021.

Policy Option for Consideration by the Board of Trustees. The Boards have already recommended the legislative action described in the previous section, and the recommendation has been communicated to the General Assembly. ***Making no further recommendation does not require a vote of the Board.***

Summary of Alternatives
For Presentation to the 2024 General Assembly

This draft is prepared under the assumption that the Board adopts a motion to recommend a benefit improvement for the FRSWPF from $170 to $175 per month, in conjunction with increasing the member contribution rate from $10 to $15 per month, with no additional State contribution. If the Board takes different actions, it is suggested that the Board direct staff to make any updates necessary to conform to Board decisions prior to communicating this summary to the legislature.

Retirement System	Employer Contributions	Enhanced Benefits
Local Governmental Employees' Retirement System **(Actions by Board of Trustees)**	Increase employer contribution rate by 0.75% for non-LEOs and 1.00% for LEOs, increasing the cost to employers from fiscal year ending 2024 to fiscal year ending 2025 by $66,850,973.[1]	None
Firefighters' and Rescue Squad Workers' Pension Fund	Increase appropriation from fiscal year ending 2024 to fiscal year ending 2025 by $350,000, to $20,402,208.[2]	Amend G.S. 58-86-55 to change $170 to $175. Amend G.S. 58-86-35, -40, -45, and -55 to change $10 to $15.
Registers of Deeds' Supplemental Pension Fund	No change[3]	None
Death Benefit Plans	No change	None

<u>FOOTNOTES</u>:

[1]The employer contribution rates for the fiscal year ending June 30, 2024, are 12.85% for employees other than Law Enforcement Officers (non-LEOs) and 14.10% for Law Enforcement Officers (LEOs). For the fiscal year ending June 30, 2025, the Board's Employer Contribution Rate Stabilization Policy calls for contribution rates of 13.60% for non-LEOs and 15.10% for LEOs. The total estimated payroll for the 2023 Session of the General Assembly was $8,430,350,000, which includes $6,981,011,000 for non-LEOs and $1,449,339,000 for LEOs.

[2]The total appropriated employer contribution for fiscal year ending June 30, 2024 is $20,052,208. For the fiscal year ending June 30, 2025, the Board's State Contribution Rate Stabilization Policy calls for a contribution at least equal to $20,402,208, which is an increase of $350,000.

[3]The total actuarially determined employer contribution for fiscal year ending June 30, 2025 is $0 after taking into account the assets in excess of the actuarial accrued liability. Contributions to the fund are set by statute.