

TITLE 20 – DEPARTMENT OF STATE TREASURER

Notice is hereby given in accordance with G.S. 150B-21.2 that the Teachers' and State Employees' Retirement System Board of Trustees intends to adopt the rule cited as 20 NCAC 02B .0405.

Link to agency website pursuant to G.S. 150B-19.1(c): <https://www.nctreasurer.com/inside-the-department-OpenGovernment/proposed-rules/Pages/default.aspx>.

Proposed Effective Date: May 1, 2018

Public Hearing:

Date: January 25, 2018

Time: 2:00 p.m.-4:00 p.m.

Location: 3200 Atlantic Avenue, Raleigh, NC 27604

Reason for Proposed Action: *The Fiscal Integrity/Pension-Spiking Prevention Act, Session Law 2014-88, was enacted by the North Carolina General Assembly in 2014. The Act contained the contribution-based benefit cap (CBBC), which protects all employing public agencies participating in the Teachers' and State Employees' Retirement System (TSERS or the System) from absorbing the costs of certain unforeseen liabilities caused by compensation decisions made by other employing agencies in the System. The law discourages the practice of "pension spiking" and also applies to liabilities caused by non-pension spiking factors such as significant late career promotions. The law allows government entities to maintain the flexibility to set compensation and only applies to employees with an average final compensation of \$100,000 or more, adjusted annually for inflation, and is limited to no more than 0.75% of expected retirements in a given year. (See Section 1 of the Act, codified as G.S. 135-4(jj), 135-5(a3), and 135-8(f)(2)).*

The law established a formula to be used to determine a member's contribution-based benefit cap. The CBBC is then compared to the amount of that member's estimated lifetime retirement benefits, calculated by using the statutory formula for calculating a retirement benefit (total years of membership service x AFC x 1.82%). Under the CBBC law, no retirement benefit may be "capped" or reduced by application of the CBBC unless the member first entered service on or after January 1, 2015. For members who entered the System prior to January 1, 2015, if the amount of estimated lifetime retirement benefits exceeds the member's CBBC, the employer is required to pay the System in a lump sum the difference between the two amounts (i.e., the amount of the member's retirement benefit in excess of that funded by retirement contributions, according to the statutory formula) within 90 days of the date of retirement. In lieu of the lump-sum requirement, the General Assembly has authorized two payment plan options. For members who enter the System on or after January 1, 2015, employers are allowed, but not required, to submit this lump sum payment on members' behalf. If employers choose not to pay, members may elect to submit this payment or accept a pension benefit that is reduced to the amount of their benefit cap.

The General Assembly required the Boards of Trustees of the affected retirement systems to adopt a value recommended by the actuary to be used for the variable in the CBBC statutory formula called the "cap factor." This statute has been interpreted, in accordance with 20 NCAC 02B. 0202, to mean that the TSERS Board shall adopt this actuarial recommendation by motion, as it does with the annual actuarial valuation. The TSERS Board must review the cap factor no less than once every five years, in conjunction with the five-year experience study as required by G.S. 135-6(n).

The TSERS Board of Trustees adopted a contribution-based benefit cap factor based upon the recommendation of its actuary at its regular quarterly meeting in October 2014. A cap factor of 4.8 for TSERS went into effect for retirements commencing on or after January 1, 2015, the effective date of the CBBC law. Subsequently, following a new actuarial recommendation based on actual experience, in October 2015, the Board revised the factor to 4.5 for TSERS. This factor went into effect for retirements commencing on or after January 1, 2016. Pursuant to this action by the TSERS Board of Trustees, the Retirement Systems Division has been administering the CBBC law since January 1, 2015.

Following this action by the Board and the Retirement Systems Division, four local school boards engaged in multiple legal actions designed to avoid paying the CBBC liabilities that have been incurred for five retirements from their school systems. These agencies have received invoices from the state totaling \$1.8 million. On May 30, 2017, on petition of the four school systems, a Wake County Superior Court judge ruled that adoption of the contribution-based cap factor requires rulemaking under the Administrative Procedure Act. The TSERS Board strongly disagrees with the ruling by the Superior Court and has filed a notice of appeal in the case. Out of an abundance of caution, the TSERS Board has decided to engage in rulemaking on the topic in the unlikely event that the four school systems prevail on appeal. The Local Governmental Employees' Retirement System (LGERS) Board of Trustees is undergoing similar rulemaking.

Comments may be submitted to: Laura Rowe, 3200 Atlantic Avenue, Raleigh, NC 27604; email dst.ncac@nctreasurer.com

Comment period ends: March 5, 2018

Procedure for Subjecting a Proposed Rule to Legislative Review: If an objection is not resolved prior to the adoption of the rule, a person may also submit written objections to the Rules Review Commission after the adoption of the Rule. If the Rules Review Commission receives written and signed objections after the adoption of the Rule in accordance with G.S. 150B-21.3(b2) from 10 or

more persons clearly requesting review by the legislature and the Rules Review Commission approves the rule, the rule will become effective as provided in G.S. 150B-21.3(b1). The Commission will receive written objections until 5:00 p.m. on the day following the day the Commission approves the rule. The Commission will receive those objections by mail, delivery service, hand delivery, or facsimile transmission. If you have any further questions concerning the submission of objections to the Commission, please call a Commission staff attorney at 919-431-3000.

Fiscal impact (check all that apply).

- ☒ **State funds affected**
- ☐ **Environmental permitting of DOT affected**
Analysis submitted to Board of Transportation
- ☒ **Local funds affected**
- ☒ **Substantial economic impact (\geq \$1,000,000)**
- ☒ **Approved by OSBM**
- ☐ **No fiscal note required by G.S. 150B-21.4**

CHAPTER 02 - RETIREMENT SYSTEMS

SUBCHAPTER 02B - TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM

SECTION .0400 - EMPLOYER CONTRIBUTIONS

20 NCAC 02B .0405 ANTI-PENSION SPIKING CONTRIBUTION-BASED BENEFIT CAP FACTOR (TSERS)

The contribution-based benefit cap factor for the Teachers' and State Employees' Retirement System is 4.5.

History Note: Authority G.S. 135-4(jj); G.S. 135-5(a3); G.S. 135-6(f).