North Carolina National Guard Pension Fund (NCNGPF)
State Contribution Rate Stabilization Policy (SCRSP)

I. Policy Purpose

This policy is developed as directed by the Board of Trustees of the Teachers' and State Employees' Retirement System, which administers the provisions of the North Carolina National Guard Pension Fund as set forth in G.S. § 127A-40. At its meeting on January 31, 2019, the Board voted to ***"direct Retirement Systems Division staff to develop a proposed State Contribution Rate Stabilization Policy for the fund, which would include both a multi-year contribution pattern and conditions under which the Board would recommend benefit improvements"***.

II. Policy Objectives

This policy establishes how the Board will develop an annual appropriation amount to recommend to the General Assembly to fund the NCNGPF, and the conditions under which the Board will consider or recommend benefit improvements for the NCNGPF.

III. Annual Appropriation Recommendation

In the actuarial valuation as of December 31, 2017, the funded percentage of the NCNGPF was calculated to be 70.7 percent, which was at least 15 percentage points less than any of the other North Carolina Retirement Systems.

To fund the NCNGPF over time, an underlying actuarially determined employer contribution (ADEC) is developed each year by the Board's consulting actuaries based on the Board's adopted assumptions and methods. As of the effective date of this policy, such methods include a level-dollar payment to amortize any newly arising actuarial losses over a 12-year period.

This policy is intended to improve the funded percentage of the NCNGPF more rapidly than the 12-year period would indicate, and to protect the NCNGPF against possible volatility in investment returns or discount rates during the period necessary to address the underfunding.

Accordingly, for each year that this policy is in effect, the appropriation to be recommended by the Board for the upcoming fiscal year, prior to any increase for benefit enhancements as described in the next paragraph, will be the greater of (1) the appropriation that the Board recommended for the current fiscal year, or (2) the underlying ADEC for the upcoming fiscal year plus $2 million[1], whichever is greater. Part (1) of this definition should exclude any portion

[1] The amount of $2 million corresponds to approximately one percent of the actuarial accrued liability that is expected to exist during the period of this policy. Therefore, the appropriation amount recommended under this policy, if enacted, will improve the funded percentage by at least one percentage point in each year, relative to what the funded percentage would have been if only the underlying ADEC had been contributed.

of the Board's appropriation recommendation for the current fiscal year that was specifically intended to cover a one-year payment of the costs of a benefit improvement, as described in the following paragraph. Part (2) should exclude any portion of the underlying ADEC for the upcoming fiscal year that is attributable to a one-year payment of costs of a benefit improvement. If the General Assembly appropriates contributions that exceed the ADEC, such excess contributions, and the earnings thereon as estimated by the consulting actuary, should be excluded in future years when estimating the unfunded actuarial accrued liability that must be amortized. This provision is intended to ensure that any contributions exceeding the ADEC are not used to reduce the ADEC in a subsequent year within the term of this policy.

The Board intends that any appropriation recommended under the previous paragraph, in excess of the underlying ADEC, be used solely to improve the funded percentage of the NCNGPF rather than to fund benefit improvements. Therefore, the appropriation recommended by the Board for the upcoming fiscal year will be further increased if the Board recommends to the General Assembly any change to the benefits provided by the NCNGPF that increases the cost of benefits. Such increase will be equal to the full increase in the NCNGPF's actuarial accrued liability that is expected from the change in benefits, as well as any increase in the normal cost. For this purpose, the actuarial accrued liability and the normal cost will be measured by the Board's consulting actuaries based on the Board's assumption for long-term investment return without regard to any "direct rate smoothing" that may apply to that assumption. Under such a recommendation, the full actuarial cost of any benefit improvement would be funded within one year through the upcoming year's appropriation, rather than amortized over multiple years.

If the NCNGPF develops net unrecognized investment gains, such that the market value of assets exceeds the actuarial value of assets under the Board's adopted asset valuation method, the Board does not intend for those investment gains to be used to reduce any recommended appropriation during the term of this policy. Rather, the Board intends such gains in the NCNGPF to be used as protection against investment losses that may occur in the future.

IV. <u>Recommended Increases to Benefit at Retirement</u>

This section of the policy describes the conditions under which the Board may consider a recommendation of an improvement to the benefit formula, meaning the calculation of the initial pension benefit for members who have not yet retired.

As of April 2019, the NCNGPF provides a pension equal to $105 per month for members with 20 years of creditable service, plus $10.50 per month for each additional year of such service, provided that the total pension shall not exceed $210 per month.

Under this policy, the Board may consider a recommendation to the General Assembly that the benefit amounts be improved, provided that the following conditions are met:

1. The full actuarial accrued liability and normal cost related to any recommended benefit increase is added to the appropriation recommended by the Board for the upcoming fiscal year, as described in Section III.

2. The increase in the benefit amount is not greater than the most recent June-over-June one-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.

In any event, if the General Assembly approves an increase to the benefit formula with or without the Board's recommendation, then as described in Section III of this policy, the Board will recommend that the cost of that increase be funded within one year through the upcoming year's appropriation, rather than amortized over multiple years.

V. Recommended Increases for Cost-of-Living Adjustments (COLAs)

This section of the policy describes the conditions under which the Board may consider a recommendation of a COLA, meaning an increase to existing retirees' pension amounts, whether that be a permanent, ongoing increase to each retiree's pension or a one-time supplemental payment.

- If the funded percentage of the NCNGPF as shown by the most recent published annual actuarial valuation report is less than 90 percent, the Board may consider a recommendation of a COLA for NCNGPF retirees only under the conditions described in Section IV above. That is, any COLA recommendation must not be greater than the inflationary increase described in Section IV, and it must be accompanied by a recommended appropriation increase at least equal to the full increase in actuarial accrued liability associated with the COLA.

- If the funded percentage of the NCNGPF as shown by the most recent published annual actuarial valuation report is at least 90 percent, then any recommendations of the Board regarding (1) whether a COLA increase should be granted, (2) the percentage increase in retirement benefits due to the COLA, and (3) the term of amortization will be the same as the Board's recommendations taking effect at the same time regarding the Teachers' and State Employees' Retirement System (TSERS). If it is not administratively feasible for Retirement Systems Division staff to implement the same adjustment for the NCNGPF as for TSERS, then the Board will recommend that some pension adjustment of similar value for retirees be implemented.

In any event, if the General Assembly approves a COLA with or without the Board's recommendation, then as described in Section III of this policy, the Board will recommend that the cost of that increase be funded within one year through the upcoming year's appropriation, rather than amortized over multiple years.

VI. Policy Effective Date

This policy, if adopted by the Board, will be effective through the fiscal year ending June 30, 2022. The Board may vote to extend it for any period of time.