



January 28, 2021

Decisions on Local Governmental Employees' 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.”

ADEC Rate: The most recent LGERS actuarial valuation report documents the ADEC rates for the fiscal year ending in 2022. The ADEC for the fiscal year ending in 2022 is the mathematical baseline contribution rate that would fund the system using the Board’s assumptions and methods adopted in January 2016, as further adjusted for the change to the assumed rate of return adopted in April 2018, and using plan population and asset information as of December 31, 2019. For employees other than law enforcement officers (non-LEOs), the ADEC rate is 11.27% of pay. For law enforcement officers (LEOs), the ADEC rate is 12.94% of pay.

Adjustment for Contribution Policy: The Board adopted the *Employer Contribution Rate Stabilization Policy (ECRSP)* on January 21, 2016 and amended it on January 31, 2019. The ECRSP was intended to provide predictable incremental increases in the employer contribution rate to protect against potential adverse experience. **The ECRSP as amended on January 31, 2019, would result in recommended contribution rates for the fiscal year ending in 2022 equal to 11.35% of covered pay for non-LEOs and 12.10% of covered pay for LEOs.**

Under the ECRSP as adopted January 21, 2016, the contributions for non-LEOs were set at 7.25% of covered pay for the fiscal year ending in 2017 (FY 2017) and were scheduled to increase each year by 0.25% of pay through FY 2022, with additional adjustments, if applicable:

1. If the underlying ADEC for non-LEOs for a given fiscal year is 50% greater than the scheduled employer contribution rate, then the scheduled employer contribution rate for that fiscal year and later fiscal years would increase by 0.50% of pay.
2. If the underlying ADEC for non-LEOs for a given fiscal year is 50% less than the scheduled employer contribution rate, then the scheduled employer contribution rate for that fiscal year and later fiscal years would decrease by 0.50% of pay.
3. Contribution rates for LEOs are 0.75% of pay greater than rates for non-LEOs.
4. If the General Assembly grants any additional cost-of-living allowance (COLA) beyond the COLA amount approved by the Board, increases the benefit multiplier for active employees, or changes the benefit structure in a way that results in a cost to LGERS, the schedule of contributions for the current and future fiscal years will be increased to recover the resulting cost.

5. The cost of any allowable COLA granted by the Board under the authority allowed by statute will not impact the scheduled contribution rates.

The contribution rate for non-LEOs was 7.25% for FY 2017, 7.50% for FY 2018, and 7.75% for FY 2019. Under the January 2019 amendment, for the ECRSP's remaining term, the annual increase in the contribution rate is 1.20% of covered pay rather than 0.25%. The contribution rate for non-LEOs was 8.95% for FY 2020, 10.15% for FY 2021, and would be 11.35% for FY 2022, before any adjustments that might be required under #1 through #5 above. Similarly, the contribution rate for LEOs (which is 0.75% greater than the rate for non-LEOs) would be 12.10% for FY 2022, before any adjustments that might be required under #1 through #5 above.

Since the ADEC rate for non-LEOs is within 50% of the rates otherwise set by the ECRSP, there is no automatic adjustment to the ECRSP under items #1 or #2 as previously described.

Valuations completed by the Board's consulting actuary demonstrate that contributions exceeded the ADEC overall during the first five years of the ECRSP. For the fiscal year ending in 2022, which will be the sixth year of the ECRSP, the contribution rate of 11.35% for non-LEOs would slightly exceed the ADEC rate of 11.27%, and the contribution rate of 12.10% for LEOs would be less than the ADEC rate of 12.94%.

Cost of Living Adjustment (COLA). Based on the actuarial losses recognized in this December 31, 2019, valuation, no COLA that would be effective July 1, 2021, may be granted by the Board under G.S. § 128-27(k). Further, based on the methods and assumptions of the projections provided to the Board in October 2020, Cavanaugh Macdonald Consulting has estimated that a potential COLA effective July 1, 2022, may be granted by the Board following the December 31, 2020, valuation as follows. These estimates assume no other offsetting losses in the December 31, 2019, valuation.

1. If calendar year 2020 market value returns exceed 2.5% (or about \$0.7 billion for LGERS), the plan is estimated to have an actuarial investment gain (rather than a loss) and a COLA could be considered; and
2. If calendar year 2020 market value returns exceed 5.7% (or about \$1.6 billion for LGERS), the plan is estimated to have an actuarial investment gain (rather than a loss) and such gain may be enough to provide a 1% recurring COLA.

Policy Option for Consideration by the Board of Trustees. Set the employer contribution rates for the fiscal year ending in 2022 in accordance with the ECRSP as adopted on January 21, 2016 and amended on January 31, 2019. Increase the employer contribution rate from 10.15% to 11.35% for non-LEOs, and from 10.90% to 12.10% for LEOs. The increase in cost to employers, from the fiscal year ending in 2021 to the fiscal year ending in 2022, would be \$84.3 million.¹ This increase would correspond to the contribution rates already set by the Board in amending the ECRSP on January 31, 2019. ***Staff recommends that the Board reaffirm the contribution rates set in the ECRSP as amended January 31, 2019.***

¹ As illustrated in the footnotes to the "Summary" page of this document, the approximate dollar amounts for appropriations effective July 1, 2021, are estimated using the "Estimated State Payrolls for Retirement Appropriations Purposes for the 2020 Session of the North Carolina General Assembly," set forth in a letter from the Director of the Retirement Systems to the State Budget Director and the Director of the Fiscal Research Division of the General Assembly, dated April 20, 2020. For example, the approximate increase in cost (\$84.3 million) is estimated as \$7,023,745,000 (the LGERS payroll from the aforementioned memo) times 1.20 percent (since both the non-LEO and LEO contribution rates would increase by 1.20 percent of pay from FY 2021 to FY 2022). Once a similar payroll letter is finalized for the 2021 Session of the General Assembly, the dollar amounts would change in accordance with the new estimated payroll amounts.

Decisions on the Firefighters' and Rescue Squad Workers' Pension Fund (FRSWPF)

Issue. The Board adopted the State Contribution Rate Stabilization Policy (SCRSP) on January 26, 2017. Under the SCRSP, recommended state contributions are the greater of (1) the prior year's appropriation plus \$350,000 and (2) the actuarially determined contribution (ADC).

For the fiscal year ending in 2022 (FY 2022), item (1) is equal to the appropriation for FY 2021 (\$19,002,208) plus \$350,000, or \$19,352,208. Item (2), the ADC, is \$15,182,523 according to the most recent FRSWPF actuarial valuation report. The ADEC for FY 2022 is the mathematical baseline contribution amount that would fund the system using the Board's assumptions adopted on January 21, 2016 (and April 26, 2018 with respect to the rate-of-return assumption), and plan population and asset information as of December 31, 2019.

Therefore, the SCRSP results in a recommended state contribution of \$19,352,208 for FY 2022, which is the greater of item (1) or item (2).

Benefit Increase. Under the SCRSP, the Board may consider recommending a benefit increase when FRSWPF has undistributed investment gains. According to the consulting actuary's valuation report as of December 31, 2019:

- Undistributed investment gains at December 31, 2019, were approximately \$12.8 million.
- If the General Assembly appropriates the funding indicated by the SCRSP for the fiscal year ending in 2022, then the state contribution for the fiscal year would exceed the actuarially determined amounts by approximately \$4.2 million. This contribution would fully fund the actuarial accrued liability of approximately \$2.8 million associated with a \$1 increase in the monthly benefit (from \$170 to \$171 per month).
- Under the SCRSP, a benefit increase would require an increase in the member contribution rate to achieve a balance of cost sharing closer to 50/50 between members and the state. Members currently contribute \$10 per month over the course of 20 years (a total of \$2,400). Under the SCRSP, the member contribution would be increased to \$15 per month according to the SCRSP if the benefit amount were increased. This increase in the monthly member contribution is sufficient to pay for the increased normal cost of approximately \$42,000 per year that would result from the \$1 monthly benefit increase.
- An increase of \$1 would increase the monthly benefit by 0.6%, which is less than the Consumer Price Index increase that the actuary estimated as 2.3%.

The Retirement Systems' staff actuary estimates that FRSWPF will have net deferred gains of \$22 million to \$26 million as of December 31, 2020, comparable to its approximately \$12.8 million of undistributed investment gains as of December 31, 2019.

Policy Options for Consideration by the Board of Trustees. The following policy options are available to the Board.

- **Option 1.** Recommend an increase in the state contribution to \$19,352,208 for the fiscal year ending in 2022, pursuant to the SCRSP. Recommend an increase in the monthly benefit from \$170 to \$171, and in the monthly member contribution from \$10 to \$15.

Option 2. Recommend an increase in the state contribution to \$19,352,208 for the fiscal year ending in 2020, pursuant to the SCRSP. Recommend that the benefit and contribution rates be unchanged. **Staff recommendation.**

Decisions on Registers of Deeds' Supplemental Pension Fund

Issue. The most recent valuation report shows the recommended Actuarially Determined Employer Contribution (ADEC) for the fiscal year ending in 2022. The ADEC for FY 2022 is the mathematical baseline contribution amount that would fund the system using the Board's assumptions adopted on January 21, 2016. It uses plan population and asset information as of December 31, 2019.

The estimated ADEC of \$0 for the fiscal year ending in 2022 is less than the 1.5 percent of monthly receipts collected pursuant to Article 1 of Chapter 161 of the N.C. General Statutes. (Statutory amounts collected were \$895,784 in calendar year 2019 and \$855,737 in calendar year 2018.) Additionally, the fund is over-funded with a funded ratio of 163.0% as of December 31, 2019.

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.***

Decisions on the 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, 2019, shows that the plan has liabilities of \$58,975,706. Against these liabilities, the plan has current assets of \$88,568,566. Prospective contributions by the participating employers have a present value of \$43,141,531. The present and prospective assets, which amount to \$131,710,097, exceed the liabilities of \$58,975,706 by \$72,734,391.

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, 2019, shows that the plan has liabilities of \$1,266,494,557. Against these liabilities, the plan has current assets of \$271,691,476. Prospective contributions of participants eligible for benefits have a value of \$967,643,306. The total present and prospective benefits amount to \$1,239,334,782, which are less than the liabilities of \$1,266,494,557 by \$27,159,775. 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. Further consideration could be given based on the results of future actuarial valuations and experience studies.

Policy Option for Consideration by the Board of Trustees. Recommend no change to the current premiums, interest rate on return of contributions or benefit structure. ***Making no recommendation does not require a vote of the Board.***

**Summary of Alternatives
For Presentation to the 2020 General Assembly**

Retirement System	Employer Contributions	Enhance Benefits
Local Governmental Employees' Retirement System	Increase employer contribution rate by 1.20 percent for both law enforcement officers and all other members for a cost in the first year to employers of \$84,284,940 ¹	No undistributed gain available for benefit enhancements
Firefighters' and Rescue Squad Workers' Pension Fund	Increase employer contribution ² by \$350,000 ³	See discussion material
Registers of Deeds' Supplemental Pension Fund ⁴	No change to employer contributions	Increases have not been requested or contemplated
Death Benefit Plans	No change	No change

FOOTNOTES:

¹The employer contribution rates for the fiscal year ending June 30, 2021, are 10.15% for employees other than Law Enforcement Officers (non-LEOs) and 10.90% for Law Enforcement Officers (LEOs). For the fiscal year ending June 30, 2022, the Board's Employer Contribution Rate Stabilization Policy calls for contribution rates of 11.35% for non-LEOs and 12.10% for LEOs. The total estimated payroll for the 2020 Session of the General Assembly was \$7,023,745,000, which includes \$5,776,398,000 for non-LEOs and \$1,247,347,000 for LEOs.

²The total appropriated employer contribution for fiscal year ending June 30, 2021, is \$19,002,208.

³Under the State Contribution Rate Stabilization Policy, the contribution increases by \$350,000 instead of decreasing by \$3,819,685.

⁴The total actuarially determined employer contribution for fiscal year ending 2021 is \$0 after taking into account the fund assets in excess of the actuarial accrued liability. Contributions to the fund are set by statute.