



**North Carolina**  
Total Retirement Plans



*Dale R. Folwell, CPA*  
STATE TREASURER OF NORTH CAROLINA  
DALE R. FOLWELL, CPA

## MINUTES

### **BOARD OF TRUSTEES OF THE TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM**

The regular quarterly meeting of the Board of Trustees was called to order at 9:41 a.m., January 28, 2021, by the Chair, State Treasurer Dale R. Folwell, CPA. The meeting was held in the Dogwood Conference Room of the Longleaf Building at 3200 Atlantic Avenue, Raleigh, NC 27604. The Chair thanked the members of the Board for their service. The Chair indicated there would be a public comment period for organizations and individuals to address the Board later in the agenda.

#### **Members Present in Person or via Telephone**

Treasurer Dale R. Folwell, Lentz Brewer (via telephone), John Ebbighausen, Vernon Gammon, Dirk German (via telephone), Barbara Gibson (via telephone), Linda Gunter, Oliver Holley (via telephone), Kathryn Johnston (designee for Catherine Truitt, via telephone), Greg Patterson (via telephone), Margaret Reader (via telephone), Joshua Smith (via telephone), and Jeffrey Winstead (via telephone).

#### **Members Absent**

None.

#### **Guests in Attendance via Telephone**

Jonathan Craven, Larry Langer, and Wendy Ludbrook of Cavanaugh Macdonald Consulting LLC.

Bill Porter, Flint Benson, Ronan Burke, Michael McCann, Paul Devenish, Anne D. DarConte, David Vanderweide, Richard Rogers, Suzanne Beasley, Lanier McRee, Sarah Collins, Laresha Fortson, and Ken Noland.

#### **Department of State Treasurer Staff Present in Person or Via Telephone**

The staff members present were: Thomas Causey, Christy Farrelly (via telephone), Joan Fontes (via telephone), Ben Garner (via telephone), Elizabeth Hawley (via telephone), Patrick Kinlaw, Fran Lawrence (via telephone), Richard Lopez, Lisa Norris, Paul Palermo (via telephone), Vicki Roberts (via telephone), Laura Rowe (via telephone), Alisia Smith (via telephone), Christina Strickland (via telephone), and Sam Watts.

#### **Ethics Awareness and Identification of Conflicts or Potential Conflicts of Interest**

The Acting Chair asked, pursuant to the ethics rules, about conflicts of interest of Board members. No conflicts of interest were identified by the Board members.

## **Approval of the State Minutes from the October 29, 2020 Board Meeting and the December 9, 2020 Special Session Board Meeting**

It was moved by Vernon Gammon and seconded by Oliver Holley that the minutes from the Board meeting held on October 29, 2020 and the Special Session Board meeting held on December 9, 2020 be approved. Dale Folwell, Barbara Gibson, Dirk German, Greg Patterson, Jeffrey Winstead, John Ebbighausen, Joshua Smith, Kathryn Johnston (designee for Catherine Truitt), Lentz Brewer, Linda Gunter, and Margaret Reader voted in support of the motion.

## **Consulting Actuary's Presentation of 2020 Experience Study**

The Chair recognized Larry Langer, Jonathan Craven, and Wendy Ludbrook from Cavanaugh Macdonald Consulting LLC (CMC) to present the findings of the 2020 Experience Study. Mr. Langer began by stating that experience studies are done at least once every five years and are a very important part of the duties of the Boards of Trustees. Mr. Langer provided a brief review of the process for the experience study, noting that the purpose of the process is to set assumptions that are reasonable and likely to remain viable over a five-year period. Mr. Langer stated that five years ago the inflation assumption was 3%, and in the current review, CMC has recommended reducing the inflation assumption to 2.5%. CMC believes that continuing to use 3% would be aggressive and reducing it to 2.5% would keep the inflation assumption in neutral territory. Mr. Langer stated that there was no information suggesting that the assumed investment returns in excess of inflation (4% per year) should change, so as a result, the CMC recommends reducing the investment return assumption by the same amount as the inflation assumption, that is, reducing it from 7% to 6.5% per year. Mr. Langer stated that regarding the various actuarial assumptions of a demographic nature, it is very common for retirement systems to regularly review those assumptions to see if recent experience has matched up with the assumption, and to adjust them to more neutral future expectations if necessary. Further, Mr. Langer stated that CMC recommends maintaining a 12-year level-dollar amortization method for unfunded liability, noting that the relatively short period is one of the reasons North Carolina has among the best-funded retirement systems in the country.

The floor was opened for comments and questions from the Boards.

A Board member stated that although CMC has projected that future employer contribution rates will decrease if the proposed assumptions are met, the experience study report still shows that the proposed assumptions will increase the employer contribution rate by 3.01% of pay for the Teachers' and State Employees' Retirement System (TSERS), compared to what they would have been under the current assumptions. Mr. Langer confirmed CMC's view that the current investment return assumption of 7% per year is borderline aggressive, and by shifting to a 6.5% assumption, the Boards would anticipate less investment returns in the future and therefore would require more contributions.

A Board member stated that he believes adopting the proposed assumptions would be a prudent action. The Board member stated that in an environment of low interest rates, it has become difficult to find yield through financial instruments to meet the expected return, and this environment has affected not only retirement systems, but also insurance companies and individuals making investments.

A Board member stated that he was hesitant to reduce the assumed rate of return, when compared to the assumptions made by privately-sponsored multi-employer retirement plans, and based on concern about how benefits will be funded when life expectancies are increasing. Mr. Langer encouraged the Boards to view the setting of assumptions, and the policies established to fund benefits under those assumptions, as two separate

decisions. Mr. Langer stated that it is important that actuarial assumptions be reasonable. He discouraged the Boards from comparing North Carolina's retirement system to private or other retirement plans. Mr. Langer also noted that increasing life expectancies are built into the recommended assumptions.

The Chair noted that today's agenda included the decision on whether to accept the recommendations from the experience study. The Chair agreed that it will be important to set good policies for funding any changes in the future. The Chair stated his view that the assumed rate of return should have been regularly adjusted over the past 20 years. The Chair stated that the decision to adopt recommended assumptions is about sustaining and preserving the Retirement Systems for the next generation, especially for lower-wage public employees.

The Board member who had expressed hesitancy about reducing the assumption noted that he would feel more comfortable with an assumption between 6.5% and 7%.

A Board member asked why the previous change to the assumed rate of return, from 7.2% to 7% per year in 2018, was gradually recognized in employer contribution rates over three years, and the current recommendation is for five years. Patrick Kinlaw, Director of Policy, Planning, and Compliance, recognized to respond, stated that the smoothing period is intended to give employers time to adjust to the change, and that the length of the smoothing period has corresponded with the expected length of time until the next experience study. The Board member noted that the Boards could always revisit the assumption if there is a problem in the next five years.

Sam Watts, Public Policy Director, recognized to provide additional remarks, noted that if the recommendation is not followed, the consulting actuary may consider it necessary to state in their annual valuation reports that the assumption is a board-selected assumption which the actuary would not have selected had the actuary been free to select it. Mr. Watts noted that such a disclosure could affect the State's financial reporting, and the credit rating of the State and local governments.

The Chair stated that funding of the Retirement Systems comes from employee contributions, employer contributions, and investment gains. The Chair stated that he does not support increasing employee contributions and there is limited control over the amount of future investment returns in the financial markets. This means that the necessary funding from making assumptions more realistic will need to come from employer contributions.

The Board member who had expressed hesitancy about reducing the assumption noted that the information provided by Mr. Watts improved his understanding of the issue.

A member of the Local Board requested information about how the proposed assumptions could affect counties and their budgets, expressing particular concern for local governments that are not as well-funded as others. The Chair stated that the funding discussion will continue during the Boards' meeting in April with a goal of making the funding policy palatable for local governments. Mr. Kinlaw, recognized to provide additional information, noted that under the projection CMC provided for today's meeting, employer contribution rates under LGERS would remain fairly level if the proposed assumptions were adopted, and if they were met.

A member of the Local Board echoed the concerns of those who previously spoke, particularly regarding rural communities that could see pressure on property taxes due to increased pension funding requirements. The Chair stated that he understands the concerns for rural communities, noting for example Tyrell County's property tax rate, comparatively small population, and trend in sales tax revenues.

A Board member stated that it is imperative that while making these important decisions, the Boards keep in mind both large and small counties, and remember that beginning teachers are earning only \$35,000 per year.

A Board member stated that she is grateful for the wonderful Retirement System, and that she supports both maintaining strong benefit offerings to offset the comparatively low salaries of public employees, and taking actions that would support the opportunity to provide cost-of-living retirement increases in the future. The Board member stated her opinion that the recommended decrease in the rate of return assumption was a large one, and asked if the risk Mr. Watts had outlined earlier in the discussion meant that moving to a mid-point, or adjusting the timing of the decision, was not feasible. Mr. Watts, recognized to respond, stated that it was important for a decision to be made to keep the annual actuarial valuation process on time, so that the General Assembly and local governments can have sufficient notice for budgeting, and in order to safeguard the credit rating as this is the single most important decision that the Board makes every five years. The Board member asked if that means that moving to an assumption of 6.75% is not viable. The Chair responded that in his opinion, it is not viable.

The Board member who had inquired earlier about the 3.01% contribution rate increase requested that CMC describe the risk if the recommended assumption of 6.5% is not adopted. Mr. Langer stated there are three risks that come to mind. First, it would increase the risk of being forced into reducing the rate again within the next five years. Second, the financial market conditions support that the inflation underlying the investment rate of return should be reduced by 0.5% per year, as noted also by another actuarial firm performing work for the Office of the State Auditor. Third, if assumptions are too optimistic, it only puts off addressing the problem and makes it a burden for future generations. The same Board member summarized that he understands if the recommendation is not adopted, it will only result in the State, public employers, or employees having to pay later at an even higher rate. The Chair agreed with this summary, noting that adopting the recommendation would be the smoother, more certain, approach.

### **Adoption of Proposed Assumptions as Set in 2020 Experience Review**

Greg Patterson made a motion and Linda Gunter seconded the motion to adopt the proposed assumptions as set in the 2020 Experience Review. Dale Folwell, Barbara Gibson, Dirk German, Jeffrey Winstead, John Ebbighausen, Joshua Smith, Kathryn Johnston (designee for Catherine Truitt), Margaret Reader, Oliver Holley, and Vernon Gammon voted in support of the motion.

### **Public Comments**

The Chair recognized Sarah Collins of the North Carolina League of Municipalities for public comment.

### **Retirement System Division Administration Update**

The Chair recognized Rick Lopez, Director of Operations, Vicki Roberts, Director of Member Services and Patrick Kinlaw, Director of Policy, Planning, and Compliance, for an update on the Division's operations.

The Chair recognized Director of Operations, Rick Lopez, to provide an update on Operations. Mr. Lopez began by stating that the team processed 809 retirements in December and 2,360 retirements in January, noting that over the past three months, the proportion of retirement requests made using the online capability has been approximately 36%. Mr. Lopez moved on to discuss death notifications stating staff processed 1,194 death notifications in December and 1,176 in January, both higher than historical norms. Mr. Lopez discussed the implementation of another report that helps the department identify more deaths more quickly. Mr. Lopez reported that there were 254 new disability applications for December with an average 13.7-day turnaround, and 969 refund requests in December with an average 9.9-day turnaround. Mr. Lopez closed by discussing monthly payroll and

Orbit Self-Service usage, noting 1.3 million hits for retirement estimates, 321,208 hits for beneficiary updates for active employees, and 52,172 hits for direct deposit changes.

The Chair recognized Director of Member Services, Vicki Roberts, for a presentation on the metrics for Member Services. Ms. Roberts began by discussing efforts made by the Education Retirement Group noting they received over 15,000 letters for the quarter, a 150% increase from last year, and still achieved an average turn-around time of five-days . Ms. Roberts discussed Retirement education meetings, noting that year to date the team has held 73 total meetings and has reached over 5,000 members and 89 employers, with the efforts including twenty webinars a month and a pre-recorded presentation available online 24/7. Ms. Roberts mentioned scheduled one-on-one counseling sessions, noting there were 705 sessions last quarter, a 40% increase over the number of sessions held from the previous quarter. Ms. Roberts further noted that the team responded to over 14,000 emails which was a 149% more than last year, and all of Member Services, including trainers, quality coaches, team leads and all counselors pulled together and responded to these emails within an average of 2 days. Lastly, Ms. Roberts mentioned the call center’s 4-minute average speed of answer. Ms. Roberts explained that the average call time increased due to the depth of the questions being asked and the need to fill a void due to the absence of on-site HR staff at many locations during this pandemic. Ms. Roberts added that staff had studied the frequently asked questions and added helpful information to the website and voice response system, allowing members to find answers more easily without waiting for a counselor to be available. Ms. Roberts concluded by reminding the Board about the Call Back Assist tool, explaining that if people use it when there is a wait time, the system will call them back when they are next in line or they have the option to schedule a callback at a time that is most convenient for them.

The Chair recognized Director of Policy, Planning & Compliance, Patrick Kinlaw. Mr. Kinlaw discussed overpayments collected, noting that just over \$9.5 million has been collected in the past 12 months and approximately \$37.5 million in outstanding overpayments remain to be collected. Mr. Kinlaw discussed contribution-based benefit cap (CBBC) liabilities, noting that 356 total invoices have been sent since 2015 totaling \$33.9 million, and of that amount more than \$26.8 million has been collected. Mr. Kinlaw briefly discussed the North Carolina’s Comprehensive Annual Financial Report published by the Office of the State Controller and the “Actuarial Review of the 2020 Accounting Disclosures” report prepared by the actuarial firm GRS Consulting for the Office of the State Auditor. Mr. Kinlaw also noted that the materials for today’s meeting include the letter received from Governor Roy Cooper, Speaker Tim Moore, and Senator Philip Berger in December 2020, and discussed at the Boards’ special meeting on December 9, 2020, regarding the Public Pensions Coordinating Council’s 2020 Standards Awards for Funding and Administration.

### **Legislative Update**

The Chair recognized Sam Watts to provide an update on the legislative session. Mr. Watts noted that the Department of State Treasurer’s highest legislative priority regarding the Retirement Systems and State Health Plan continues to be ensuring funding in accordance with Board of Trustees policies and actuarial recommendations. Mr. Watts noted that when retirement-related proposals are made to the legislature, the Department’s goal is to promote the sustainability of the Retirement Systems. He noted that the Department expected to request a bill that would continue the process of restructuring the service purchase statutes under the State and Local systems, following on the legislation enacted in that area in 2020. Finally, Mr. Watts discussed other potential topics that may arise during the legislative session affecting local government finance.

### **Increase in the Amount of Reemployment Earnings Before Suspension of Retirement Allowance**

The Chair recognized Thomas Causey for a presentation on increasing the amount of reemployment earnings a retiree can make before the suspension of their retirement allowance. Mr. Causey stated that according to statute, the amount increases by a defined inflationary measure each year, and it increased from \$34,340 to \$34,800 effective January 1, 2021. Mr. Causey stated that the Board could authorize staff to use the new amount in administration and communication during 2021.

John Ebbighausen made a motion and Linda Gunter seconded the motion to increase the amount of reemployment earnings before suspension of retirement allowance. Dale Folwell, Barbara Gibson, Dirk German, Greg Patterson, Jeffrey Winstead, Joshua Smith, Kathryn Johnston (designee for Catherine Truitt), Lentz Brewer, Margaret Reader, Oliver Holley, and Vernon Gammon voted in support of the motion.

### **Update on the Investment Advisory Committee (IAC) Meetings**

The Chair recognized Greg Patterson to provide an update on the IAC meetings. Mr. Patterson noted the Advisory Committee met on November 18, 2020 and he wanted to provide a brief overview of the meeting noting the meeting minutes can be found online for further information. Mr. Patterson stated the meeting began with an update on cost efficiencies to date within the system and moved on to discuss benchmarking performed by BNY Mellon relative to public funds in excess of \$20 billion. Mr. Patterson noted that for the twelve months ended September 30, 2020, the North Carolina Retirement Systems (NCRS) ranked in the 36th percentile in returns gross of fees (with 1st percentile being the highest returns), and the comparison likely would have been even more favorable if it had considered returns net of fees, given the low fees incurred by NCRS. For the same period, NCRS ranked in the 95th percentile in risk (with 1st percentile being the highest risk). Mr. Patterson further noted that analysis presented to the IAC indicated that 40 basis points (0.4% of the portfolio) of the return for the twelve-month period was attributable to added value from active management. Mr. Patterson stated the meeting contained an extensive presentation by CEM Benchmarking noting that the five-year average return from 2015 to 2019 was 6.5% per year, as compared to a peer average of 7.5% per year. Mr. Patterson noted that CEM found the difference was due to NCRS' conservative investment approach, and also found that the total NCRS investment cost of 32 basis points per year was the lowest in the peer group, while the peer average was 52 basis points.

### **Application of Charter School for Full Participation in State System (Discovery Charter School)**

The Chair recognized Patrick Kinlaw to discuss the application of Discovery Charter School, of Durham, for continued participation as an employer in TSERS. Mr. Kinlaw stated Discovery Charter School joined TSERS under provisional status in 2019. Mr. Kinlaw discussed the statutory conditions under which the Board may grant an application for continued participation under G.S. 135-5.3(b7), and summarized staff's review, including a financial review. Mr. Kinlaw stated that staff recommends approval of the school's application for continued participation.

Linda Gunter moved to approve the application of Discovery Charter School and John Ebbighausen seconded the motion. Dale Folwell, Barbara Gibson, Dirk German, Greg Patterson, Jeffrey Winstead, Kathryn Johnston (designee for Catherine Truitt), Lentz Brewer, Margaret Reader, Oliver Holley, and Vernon Gammon voted in support of the motion.

### **Actuarially Determined Employer Contribution (ADEC) Projections for State System**

The Chair recognized Jonathan Craven of Cavanaugh Macdonald Consulting for a presentation on the actuarially determined employer contribution (ADEC) projections for the State System. Mr. Craven presented charts demonstrating the effect of the assumption and method changes resulting from the experience study (including

6.5% assumed return per year in the future) and the actual return during calendar year 2020, which was estimated to be 11%. Mr. Craven stated that if all assumptions are met in 2021 and beyond, the actuarially determined employer contribution rates would stabilize or decline in the coming years, and the funded ratio would reach 100% by the end of 2029.

### **Presentations on the 2021 Alternatives for the General Assembly**

The Chair recognized Patrick Kinlaw to present the recommendations to the General Assembly for the appropriate contribution rates or contribution amounts to fund the Retirement Systems effective July 1, 2021. Mr. Kinlaw noted that the recommendations are based on the findings of the actuarial valuation reports from Cavanaugh Macdonald Consulting as of December 31, 2019, that the Board adopted at its October 2020 meeting, as well as the funding policies that the Board has adopted.

Mr. Kinlaw presented the recommendation for TSERS, noting that the contribution rate called for under the Board's funding policy effective July 1, 2021 is 15.74%, which is equal to the actuarially determined employer contribution (ADEC) in this case and greater than the current year's contribution rate of 14.78%. The Board's funding policy essentially says that the recommended contribution rate should be the greater of the ADEC (15.74% of pay) or the current rate plus a step increase of 0.35% (15.13% of pay). Mr. Kinlaw stated that since the ADEC of 15.74% is greater than 15.13%, it would be recommended that 15.74% would be the contribution rate at current benefit levels to be effective July 1, 2021. Mr. Kinlaw stated that the year-over-year contribution rate increase corresponds to an increase in General Fund appropriations of \$107.2 million, and Highway Fund costs of \$3.2 million, to fund benefits at current levels.

Mr. Kinlaw presented the recommendation for the Consolidated Judicial Retirement System, noting that the ADEC was 38.70% of pay, which is greater than the current year's contribution rate of 36.44%. Mr. Kinlaw stated that the year-over-year contribution rate increase corresponds to an increase in General Fund appropriations of \$1.7 million to fund benefits at current levels.

Mr. Kinlaw presented the recommendation for the Legislative Retirement System, noting that the ADEC was 27.15% of pay, which is less than the current year's contribution rate of 27.30%. Mr. Kinlaw stated that the year-over-year contribution rate decrease corresponds to a decrease in General Fund appropriations of roughly \$5,000 to fund benefits at current levels.

Mr. Kinlaw presented the recommendation for the Disability Income Plan of North Carolina, noting that the ADEC was 0.09% of pay, equal to the current year's contribution rate. Mr. Kinlaw stated that there would be no change in the year-over-year contribution rate to fund benefits at current levels.

Mr. Kinlaw presented the recommendation for the North Carolina National Guard Pension Fund, noting that the ADEC amount was approximately \$6.4 million. The funding policy the Board adopted in April 2019 calls for the Board to recommend a contribution that is at least \$2 million greater than the ADEC, but it also calls for the recommendation to be at least equal to the current year's appropriation. Mr. Kinlaw noted that the current year's appropriation is \$11,031,715, and therefore, that would be the Board's recommendation under its policy.

Mr. Kinlaw presented the recommendations for the Death Benefits Plans where the State Board has oversight, noting that staff does not believe it is necessary for the Board to make a recommendation to change either the contribution rates or the benefit structures.

Gregg Patterson moved to approve the recommendations and Lentz Brewer seconded the motion. Dale Folwell, Dirk German, Jeffrey Winstead, John Ebbighausen, Linda Gunter, Margaret Reader, Oliver Holley, and Vernon Gammon voted in support of the motion.

### **Informational Update on Board Policies**

The Chair recognized Patrick Kinlaw. Mr. Kinlaw discussed two policies, the TSERS Employer Contribution Rate Stabilization Policy (ECRSP) and the North Carolina National Guard Pension Fund State Contribution Rate Stabilization Policy (SCRSP), noting that both policies are set to expire June 30, 2022, and staff recommends that planning begin now for the period after their expiration. Mr. Kinlaw noted that staff expects to present alternatives or recommendations at the Board's meeting in April 2021.

### **Board of Trustees Comments**

Oliver Holley thanked Retirement Systems staff, and asked those present to remember and support all state employees, teachers, and school staff maneuvering through the COVID situation. Linda Gunter thanked staff for everything they do especially for the patience and assistance they show the Board members during tough decisions. John Ebbighausen thanked the Chair for his leadership. Kathryn Johnston stated this would be her last meeting and that it has been a true honor to serve over the last several years. Ms. Johnston further thanked her fellow board members for their courage in making difficult decisions and their respect for differing viewpoints, and thanked staff for their professionalism in supporting Board members.

The Chair thanked Ms. Johnston for her service and support. He asked those present to honor the memories of Retirement Systems members who have passed away due to COVID, including a warden and associate warden at a North Carolina correctional facility.

### **Adjournment**

There being no further business before the Board, John Ebbighausen moved to adjourn, which was seconded by Linda Gunter. Dale Folwell, Dirk German, Jeffrey Winstead, Lentz Brewer, Linda Gunter, Margaret Reader, and Vernon Gammon voted in support of the motion and the meeting was adjourned at 1:02 p.m.