



January 25, 2018

Decisions on Teachers' and State Employees' Retirement System (TSERS)

Issue. The most recent TSERS actuarial valuation report documents the recommended Actuarially Determined Employer Contribution (ADEC) rate for the fiscal year ending in 2019. The ADEC for FY 2019 is the mathematical baseline contribution rate that would fund the system using the Board's assumptions adopted on January 21, 2016, (and April 20, 2017, with respect to the rate-of-return assumption), and using plan population and asset information as of December 31, 2016.

The ADEC rate for FY 2019 is 11.98 percent. The ADEC is greater than the appropriated employer contribution rate in the state budget of 10.78 percent for the fiscal year ending in 2018. It is also greater than the currently appropriated employer contribution rate in the state budget of 11.87 percent for the fiscal year ending in 2019.

Further, the Board adopted the *Employer Contribution Rate Stabilization Policy (ECRSP)* on January 21, 2016, a policy that serves to provide predictable incremental increases in the employer contribution rate to ameliorate any potential adverse experience. Under the ECRSP, contributions will be 0.35 percent of payroll greater than the appropriated contribution from the prior fiscal year, with the following bounds:

1. Contributions may not be less than the ADEC rate, and
2. Contributions may not be greater than a contribution rate determined using the same assumptions used to calculate the ADEC but with a discount rate equal to the long-term Treasury bond yield, resulting in approximately 64.12 percent.

The appropriated employer contribution rate for the fiscal year ending in 2018 is 10.78 percent. The ECRSP would indicate an employer contribution rate of 11.13% for the fiscal year ending in 2019 (equal to 10.78% plus 0.35%), subject to the lower bound of the ADEC rate (11.98%) and the upper bound equal to the ADEC-type calculation using a long-term Treasury discount rate (approximately 64.12%). Therefore, the recommended employer contribution rate is equal to the ADEC, 11.98% of payroll, which is the lower bound of the allowable contribution rates pursuant to the terms of the ECRSP. The state budget allocated from the General Fund would need to increase by \$121.9 million to meet the new contribution under the ECRSP for fiscal year ending 2019.

Cost of Living Adjustment (COLA). Based on the actuarial losses recognized in this December 31, 2016, valuation, no COLA effective July 1, 2018, could be funded by actuarial gains. Based on the methods and assumptions used for the projections presented by Conduent

in October 2017, we estimate that a potential COLA effective July 1, 2019, could be funded by actuarial investment gains following the December 31, 2017, valuation as follows:

1. If calendar year 2017 market value returns exceed 16.9 percent (or about \$10.7 billion for TSERS), 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 2017 market value returns exceed 20.7 percent (or about \$13.1 billion for TSERS), the plan is estimated to have an actuarial investment gain (rather than a loss) and such gain may be enough to provide a one percent COLA.

These estimates assume no other offsetting actuarial losses in the December 31, 2017, valuation.

Policy Option for Consideration by the Board of Trustees. Recommend an Increase to Current Appropriation to Fund the Employer Contribution Required by the Employer Contribution Rate Stabilization Policy: Recommend the legislature increase the appropriation to 11.98 percent. The additional appropriation needed from the General Fund would be \$121.9 million. ***Staff Recommendation.***

Decisions on Consolidated Judicial Retirement System (CJRS)

Issue. The most recent valuation report shows that the recommended ADEC of 32.35 percent for the fiscal year ending in 2019 is greater than the state budget of 31.05 percent for the fiscal year ending in 2018. Therefore, the state budget allocated from the General Fund will need to increase by \$976,001 to meet the new ADEC for fiscal year ending 2019.

Policy Option for Consideration by the Board of Trustees. Recommend an Increase to Current Appropriation to Fund the ADEC: Recommend the legislature increase the appropriation to 32.35 percent. The additional appropriation needed from the General Fund would be \$976,001. ***Staff Recommendation.***

Decisions on Legislative Retirement System (LRS)

Issue. The most recent valuation report shows that the recommended ADEC of 21.74 percent for the fiscal year ending in 2019 is greater than the state budget of 19.04 percent for the fiscal year ending in 2018. Therefore, the state budget allocated from the General Fund will need to increase by \$97,740 to meet the new ADEC for fiscal year ending 2019.

Policy Option for Consideration by the Board of Trustees. Recommend an Increase to Current Appropriation to Fund the ADEC: Recommend the legislature increase the appropriation to 21.74 percent. The additional appropriation needed from the General Fund would be \$97,740. **Staff Recommendation.**

Decisions on the Disability Income Plan

Issue. Based on assumptions adopted in April 2016, which include an assumed rate of return on investments of 3.75 percent, the most recent valuation report shows that the recommended Annual Required Contribution (ARC) is 0.13 percent of state payroll for the fiscal year ending in 2019. This is lower than the fiscal year 2018 contribution rate of 0.14 percent. The General Assembly could lower the contribution rate to the ARC without negatively impacting the funding of the plan.

Benefit enhancements are not being considered at this time.

Policy Option for Consideration by the Board of Trustees. Recommend Lowering the Employer Contribution Rate to 0.13 Percent: Recommend that the General Assembly lower the Employer Contribution Rate from 0.14 percent of payroll to 0.13 percent of payroll for a cost savings of \$1.7 million. ***Staff Recommendation.***

Decisions on North Carolina National Guard Pension Fund

Issue. The most recent valuation report shows that the recommended ADEC of \$9,071,933 for the fiscal year ending in 2019 is greater than the state budget of \$8,923,153 for the fiscal year ending in 2018. Therefore, the state budget allocated from the General Fund will need to increase by \$148,780 to meet the new ADEC for the fiscal year ending in 2019.

Two Policy Options for Consideration by the Board of Trustees. Two policy options are available to the Board:

- **Option 1.** Recommend an Increase to Current Appropriation to Fund the ADEC: Recommend the legislature increase the appropriation to \$9,071,933. The additional appropriation needed from the General Fund would be \$148,780.
- **Option 2.** Recommend an Increase to Current Appropriations of \$2 million above the ADEC: Recommend the legislature increase the appropriation to \$11,071,933. This increase would provide for an accelerated payment schedule that would pay off the unfunded liability on this pension plan in about 8.5 years instead of the current 12-year schedule. This option assumes that the additional \$2 million was appropriated each year until it was paid off, and it serves as a means to more rapidly improve the funded status. The additional appropriation needed from the General Fund would be \$2,148,780. **Staff Recommendation.**

Summary of Alternatives For Presentation to the 2018 General Assembly

Retirement System	Employer Contributions	Enhance Benefits
Teachers' and State Employees' Retirement System	Increase employer contribution rate ¹ by 1.20 percent for a cost in the first year to the General Fund of \$121,904,388 and to the Highway Fund of \$3,625,188	No undistributed gain available for benefit enhancements
Consolidated Judicial Retirement System	Increase employer contribution rate ² by 1.30 percent for a cost in the first year to the General Fund of \$976,001	No undistributed gain available for benefit enhancements
Legislative Retirement System	Increase employer contribution rate ³ by 2.70 percent for a cost in the first year to the General Fund of \$97,740	No undistributed gain available for benefit enhancements
Disability Income Plan	Decrease employer contribution rate by 0.01 percent of payroll for a savings of \$1.7 million	N/A
National Guard Pension Fund	Increase employer contribution ⁴ by \$148,780	No undistributed gain available for benefit enhancements

FOOTNOTES:

¹The total appropriated employer contribution rate for fiscal year ending June 30, 2018, is 10.78 percent. The estimated payrolls for the 2017 Session of the General Assembly were \$10,158,699,000 for the General Fund and \$302,099,000 for the Highway Fund.

²The total appropriated employer contribution rate for fiscal year ending June 30, 2018 is 31.05 percent. The estimated payroll for the 2017 Session of the General Assembly was \$75,077,000.

³The total appropriated employer contribution rate for fiscal year ending June 30, 2018 is 19.04 percent. The estimated payroll for the 2017 Session of the General Assembly was \$3,620,000.

⁴The total appropriated employer contribution for fiscal year ending June 30, 2018, is \$8,923,153.