Local Governmental Employees' Retirement System Board of Trustees

State Contribution Rate Stabilization Policy for the Firefighters' and Rescue Squad Workers' Pension Fund

I. Policy Purpose

This policy provides for the continued operation of a State Contribution Rate Stabilization Policy (SCRSP) for the Firefighters' and Rescue Squad Workers' Pension Fund (FRSWPF). The SCRSP was first adopted by the Local Governmental Employees' Retirement System (LGERS) Board of Trustees (Board) on January 26, 2017, as required by Section 5 of S.L. 2016-108. The 2017 version of the SCRSP provided that it would be in effect "until the next experience review and [would] then be reset based on the results of that review." Having adopted the Experience Study of the 2015-2019 calendar years on January 28, 2021, which will be effective for plan funding purposes for fiscal years ending 2023 and later, the Board wishes to institute an SCRSP effective for contributions during the five fiscal years ending 2023 through 2027.

II. Policy Objectives

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

III. Definitions

<u>Actuarial Measurement:</u> The result of an analysis by the Board's consulting actuary, presented to the Board in a public report, based on actuarial assumptions and methods adopted by the Board for purposes of funding of the FRSWPF, without regard to any "direct rate smoothing" of changes in the Board's assumptions and methods.

<u>Benefit Improvement Funding Requirement:</u> An amount equal to (1) the Actuarial Measurement of the full increase in the FRSWPF actuarial accrued liability and normal cost expected from a proposed benefit increase, <u>plus</u> (2) the FRSWPF actuarial accrued liability according to the most recently accepted valuation report of the consulting actuary, <u>less</u> (3) the FRSWPF actuarial value of assets according to the most recently accepted valuation report of the consulting actuary, <u>plus</u> (4) the Underlying ADEC for the upcoming fiscal year, <u>less</u> (5) the Policy Contribution Without Benefit Increase for the upcoming fiscal year. However, the Benefit Improvement Funding Requirement will be no less than $0, and no greater than the amount in part (1) of the definition prior to adjustment for parts (2) through (5). The intention of parts (2) through (5) is to provide for a possible reduction in the Benefit Improvement Funding Requirement if there is a funding surplus (parts (2) and (3)) or if the Board's appropriation recommendation under this policy will exceed the Underlying ADEC (parts (4) and (5)).

Policy Contribution Without Benefit Increase: The State appropriation to be recommended by the Board under this policy, prior to any increase for the cost of benefit improvements that the Board may recommend under Section V of this policy.

Target Member Contribution Rate: The member contribution rate that would result in the total member contributions being closest to 50% of the Actuarial Measurement of the FRSWPF normal cost for the upcoming fiscal year, subject to the constraint that the monthly member contribution rate should be a multiple of $5.

Underlying Actuarially Determined Employer Contribution (Underlying ADEC): The amount developed annually by the Board's consulting actuary, representing a funding requirement according to the Board's actuarial assumptions and methods before applying this policy.

IV. Annual Appropriation Recommendation

Changes in the Underlying ADEC from year to year can result in roller-coaster appropriations which are difficult for budget and appropriation planning. In particular, "V"-shaped underlying ADEC patterns create incentives within the appropriations process for programs that compete with FRSWPF over a limited pool of revenue to increase their recurring funding requirements, even though a reduction to the FRSWPF would effectively be nonrecurring due to the "V" shape. To avoid a roller-coaster pattern, this policy provides for continuing the pattern of minimum recommended increases to the annual recommended appropriation. This may result in an appropriation recommendation exceeding the Underlying ADEC.

Accordingly, for each year that this policy is in effect, the Policy Contribution Without Benefit Increase recommended by the Board for an upcoming fiscal year will be the greater of (1) the appropriation that the Board recommended for the current fiscal year plus $350,000[1], or (2) the Underlying ADEC for the upcoming fiscal year.

In developing Parts (1) and (2) of this definition, this policy provides the following guidance:

- In Part (1), the appropriation that was recommended for the current fiscal year should exclude any portion of the Board's recommendation specifically intended to cover a one-year payment of the costs of a benefit improvement, as described below under "Further Increase to Fund Benefit Improvement."
- In Part (1), the appropriation that was recommended for the current fiscal year should be adjusted (increased) to include the cost of any benefit improvements enacted by the General Assembly, for which the General Assembly did not appropriate funding during the current fiscal year at least equal to the Benefit Improvement Funding Requirement. This increase should be equal to the Benefit Improvement Funding Requirement,

[1] The amount of $350,000 was described in the initial SCRSP adopted January 2017 as "designed to mirror the estimated growth rate of the tax on gross property insurance as provided for under G.S. 105-228.5(d)(3)…. Currently the tax on premiums is 0.74% of 10% of the gross premiums for automobile physical damage coverage and 0.74% of 100% of the gross premiums for all other property coverage. Three other programs benefiting firefighters and rescue squad workers are paid for directly out of the proceeds of this tax, with the remainder being transferred to the General Fund to partially offset the cost of the FRSWPF."

reduced for any funding appropriated by the General Assembly during the current fiscal year toward the enacted benefit improvement.

- In Part (1), the appropriation that was recommended for the current fiscal year should be adjusted (either increased or reduced) for the effect of any changes in actuarial assumptions or methods adopted by the Board that were not incorporated in the Board's recommendation for the current fiscal year. The adjustment should be equal to the Actuarial Measurement of the effect on the Underlying ADEC, except that it may include direct rate smoothing to the extent the Board adopted direct rate smoothing of the relevant assumption or method change for FRSWPF funding purposes.
- In Part (1), the appropriation that was recommended for the current fiscal year should be adjusted (reduced) for the effect of any increase to member contributions ($10 per month as of April 2021) that was not incorporated in the Board's recommendation for the current fiscal year, but has since been enacted. The reduction should be equal to the Actuarial Measurement of the decrease in the State's share of FRSWPF normal cost that would have been incorporated in the Board's recommendation for the current fiscal year had it been enacted.
- In Part (2), the Underlying ADEC for the upcoming fiscal year should exclude any portion attributable to a one-year payment of costs of a benefit improvement.

<u>Further Increase to Fund Benefit Improvement:</u> The appropriation recommended by the Board for the upcoming fiscal year will be further adjusted if the Board recommends to the General Assembly a benefit improvement as described in Section V of this policy. Such adjustment will be at least equal to the Benefit Improvement Funding Requirement. It may be further increased by an amount to account for any prospective change to the statutory terms for tax on gross property insurance. 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.

The Policy Contribution Without Benefit Increase, added to the Benefit Improvement Funding Requirement associated with any benefit improvement enacted by the General Assembly effective for a fiscal year, will be deemed by the Board to be the annual actuarially determined employer contribution (funding ADEC) for the FRSWPF.

V. Recommended Increases to Benefit Formula

As of April 2021, the FRSWPF provides a pension equal to $170 per month. This section of the policy describes the conditions under which the Board may consider a recommendation of an improvement to the formula for calculating FRSWPF benefits in any year. The intent of the policy is that the satisfaction of all of the conditions described below would not bind the Board to recommend a benefit improvement, but rather, would allow the Board to consider recommending a benefit improvement.

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

1. 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.

2. The Benefit Improvement Funding Requirement is included in the appropriation recommended by the Board for the upcoming fiscal year.

3. Together with any recommended benefit improvement, the Board recommends to the General Assembly that the member contribution rate (which is $10 per month as of April 2021) be increased or maintained at an amount at least equal to the Target Member Contribution Rate.

4. If there has been a change to the tax on gross property insurance from the statutory terms effective April 29, 2021, the Board has considered the anticipated effect on the funding of FRSWPF and recommends additional funding if necessary to account for the effect of this change.

VI. <u>Policy Effective Date</u>

This policy, if adopted by the Board, will be effective through the fiscal year ending June 30, 2027. The Board may vote to extend it for any period of time.