

**Frequently Asked Questions About Cost-of-Living  
Adjustments (COLAs) and One-Time Supplements in the N.C.  
Retirement Systems**

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## **General Information**

*Q1. What is a cost-of-living increase in retirement allowances (“COLA”)? What is a one-time supplement (“supplement”)?*

- COLAs and supplements are payments that current retirees and survivor beneficiaries may receive from the Retirement Systems in addition to the defined benefit they are already being paid.
  - COLAs are permanent increases to monthly retirement allowances. For example, if the beneficiary is receiving \$1,800 per month for their lifetime, a 1% COLA would add \$18, making it \$1,818 per month.
  - Supplements are one-time payments that are typically calculated based on the annual retirement allowance. For example, if the person is receiving \$1,800 per month, that equates to \$21,600 per year. A supplement of 1% would be calculated as 1% of \$21,600, which is \$216. So, the beneficiary would receive \$2,016 during one particular month. After that one-time payment, their monthly benefit would go back to \$1,800.
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*Q2. Why are COLAs or supplements an important topic for the Boards to consider?*

- As trustees, the Boards should consider the risks faced by retirees, current employees, and government employers.
  - COLAs and supplements help address the inflation risk faced by retirees. They increase benefits to combat the effects of inflation on someone with a fixed income.
  - The cost of these increased benefits is borne by employers. State and local government employers pay these costs from their funding sources, which are primarily tax revenues. If employer costs became unsustainable, costs could also increase for employees.
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*Q3. Why should the Boards pay particular attention to the inflation risk faced by retirees?*

- Three major financial risks faced by retirees in the U.S. are the risks of:
  - (1) managing investments before and after their retirement,
  - (2) running out of retirement savings in their later years, and
  - (3) inflation consuming their fixed income after retirement.
- TSERS and LGERS have built-in controls that help address the first two risks. When these items start to look more “risky” for the entire retirement system, employers have to pay more to protect retirees and employees. This has been happening over the last 20-30 years.
- TSERS and LGERS do not generally address the third risk, inflation after retirement. That is where COLAs and supplements can have a role.

- Many TSERS and LGERS retirees are partially protected from inflation, because they may receive Social Security or Veterans' Affairs benefits that automatically increase based on inflation every year.
  - TSERS and LGERS allow retirees to transfer pre-tax savings from the NC 401(k) Plan or NC 457 Plan to the Retirement Systems and receive this transferred benefit, in return, as a lifetime retirement benefit. The retiree can choose for the transferred benefit to increase each year with inflation.
  - TSERS and LGERS benefits do not automatically increase based on inflation every year. Retirement allowances are fixed unless a COLA or supplement can be granted.
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*Q4. Have TSERS and LGERS ever promised pensions that automatically keep up with inflation?*

- No. Some public retirement systems in the U.S. have enacted "automatic COLA" provisions over the years. Some that enacted them have since repealed them. North Carolina, by contrast, has kept an "ad hoc" structure where decision-making authorities can approve inflation-based COLAs, after considering risks and economic conditions.
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*Q5. How much has inflation after retirement affected our retirees?*

- It differs from case to case. Please see Appendix A for a more complete discussion of this question with numerical estimates.
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*Q6. What are some other differences between benefits paid to many or most of today's retirees and those currently promised to employees?*

- For most current retirees, the pension calculation became more generous during their career. This has not been true for most current employees.
- For most current retirees, the State pays the full premium for State Health Plan retiree coverage if they worked at least five years for the State. Current employees hired between October 1, 2006 and December 31, 2020 must work at least 20 years to receive full premiums. Those hired January 1, 2021 or later will not receive State-paid retiree health coverage.
- For current retirees who had at least five years of service by August 12, 1989, their pension benefit is exempt from State income taxation. For almost all current employees, their pension benefit will be subject to State income tax.

- Some current retirees were able to “purchase” creditable service by paying much less than the value of the benefit they would receive. Most of these “discounts” on service purchase costs no longer exist for current and future employees.

## Unfunded Liabilities

*Q7. What is an unfunded liability?*

- It is an amount measured by actuaries every year.
  - An unfunded liability means that the past contributions made by members and employers, and all the past investment earnings on those contributions, have not been sufficient to pay all the future pension benefits that have already been promised based on service that retirees and employees have already performed.
  - The unfunded liability is a measure of that shortfall, in dollars.
  - The unfunded liabilities from TSERS and LGERS are disclosed in the State's Annual Comprehensive Financial Report (ACFR) each year. They are also disclosed in offering statements when the State or local governments borrow money. They are looked upon by financial market participants and credit rating agencies as a very important part of the picture of the state or local government's financial health.
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*Q8. Do the unfunded liabilities include any assumption that COLAs or supplements will be paid in the future?*

- No. COLAs or supplements would be new benefits that have not yet been anticipated in actuarial measurements. That means they would further increase the unfunded liability until they can be paid for.
  - They also have not been budgeted or funded by employers.
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*Q9. What are the unfunded liabilities of the Retirement Systems, based on already-promised benefits, before any COLAs or supplements are added?*

- At last measurement, as of December 31, 2024, the unfunded liabilities were:
    - \$12.0 billion (TSERS)
    - \$6.3 billion (LGERS)
  - For comparison:
    - The State budget for the fiscal year ending in 2025 was about \$32 billion.
    - Total annual employee payrolls (not including employer-paid benefits) are about \$20.5 billion (TSERS) and \$10.1 billion (LGERS).
  - One way to think about the unfunded liabilities is that they amount to about seven months' worth of public employee salaries.
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*Q10. Has the State always had such significant unfunded liabilities for TSERS?*

- No. In many of the years leading up to the 2008 financial crisis, there was no unfunded liability. That is, the pension fund was often estimated to be sufficient to pay all promised benefits, and then some. In some years there was an estimated surplus reaching as much as \$4 billion. In all those years, the unfunded liability was never greater than \$2 billion. After the financial crisis, the TSERS unfunded liability grew rapidly for several years. For the past five years, it has been between \$9 billion and \$12 billion.
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*Q11. How much do COLAs or supplements add to the unfunded liabilities?*

- COLAs or supplements add to the unfunded liability of the Retirement System until they can be paid for.
- According to the consulting actuaries, the dollar amounts as of December 31, 2024 were as follows. The amounts are scalable; for example, the unfunded liability for a 3% COLA is triple the unfunded liability for a 1% COLA.

<b>Retirement System:</b>	<b>TSERS</b>	<b>LGERS</b>
Unfunded liability for already-promised benefits	\$12,005,999,930	\$6,250,210,610
Additional unfunded liability for each:		
1% COLA	\$586,739,000	\$221,428,000
1% supplement	\$57,875,000	\$20,914,000

## Paying for the Costs

*Q12. What are the anticipated contribution rates to the Retirement Systems, based on already-promised benefits, before any COLAs or supplements are added?*

- Members pay 6% of their compensation.
  - For the fiscal year beginning July 1, 2026, the anticipated employer contribution rates, before COLAs or supplements are added, are:
    - TSERS: 17.49% of compensation.
    - LGERS: 17.10% of compensation for LEOs; 15.10% for all other employees.
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*Q13. How do those contribution rates stack up against actuarial recommendations?*

- Based on current laws, policies, and accounting guidance, the State's Annual Comprehensive Financial Report (ACFR) in 2027 will likely show:
    - TSERS contributions for the year equal to actuarially determined amounts
    - LGERS contributions for the year less than actuarially determined amounts
      - RSD staff estimates this shortfall will be \$30-\$40 million.
      - It is expected to be largest contribution deficiency reported yet for LGERS.
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*Q14. In general, how can COLAs or supplements be paid for?*

- There are three basic ways:
    - Encumbering investment gains (i.e., taking money held in the pension fund that will not necessarily be needed to pay already-promised benefits, and using that money to pay for COLAs or supplements that have not yet been promised).
    - Increasing employer contributions.
    - Direct appropriations by the legislature.
  - COLAs or supplements can also be paid for by combining any of the above.
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*Q15. Are there investment gains available to pay for COLAs or supplements right now?*

- No, there were not, as of December 31, 2024.

- The total investment return for calendar year 2025 would have to be more than 17% for each system to reach a point where there might be investment gains as of December 31, 2025, however minimal.

*Q16. Given that there are no investment gains, how could COLAs or supplements be paid for under current actuarial approaches?*

- Recall there are three ways to pay for COLAs or supplements:
  - (1) investment gains (not available)
  - (2) increased employer contributions (could be considered)
  - (3) direct legislative appropriations (could be considered)
- If paid via increased employer contributions, then the additional costs are as follows. Note, the cost of a permanent COLA is assumed to be paid over 12 years. The amounts are scalable; for example, the cost for a 3% COLA is triple the cost for a 1% COLA.

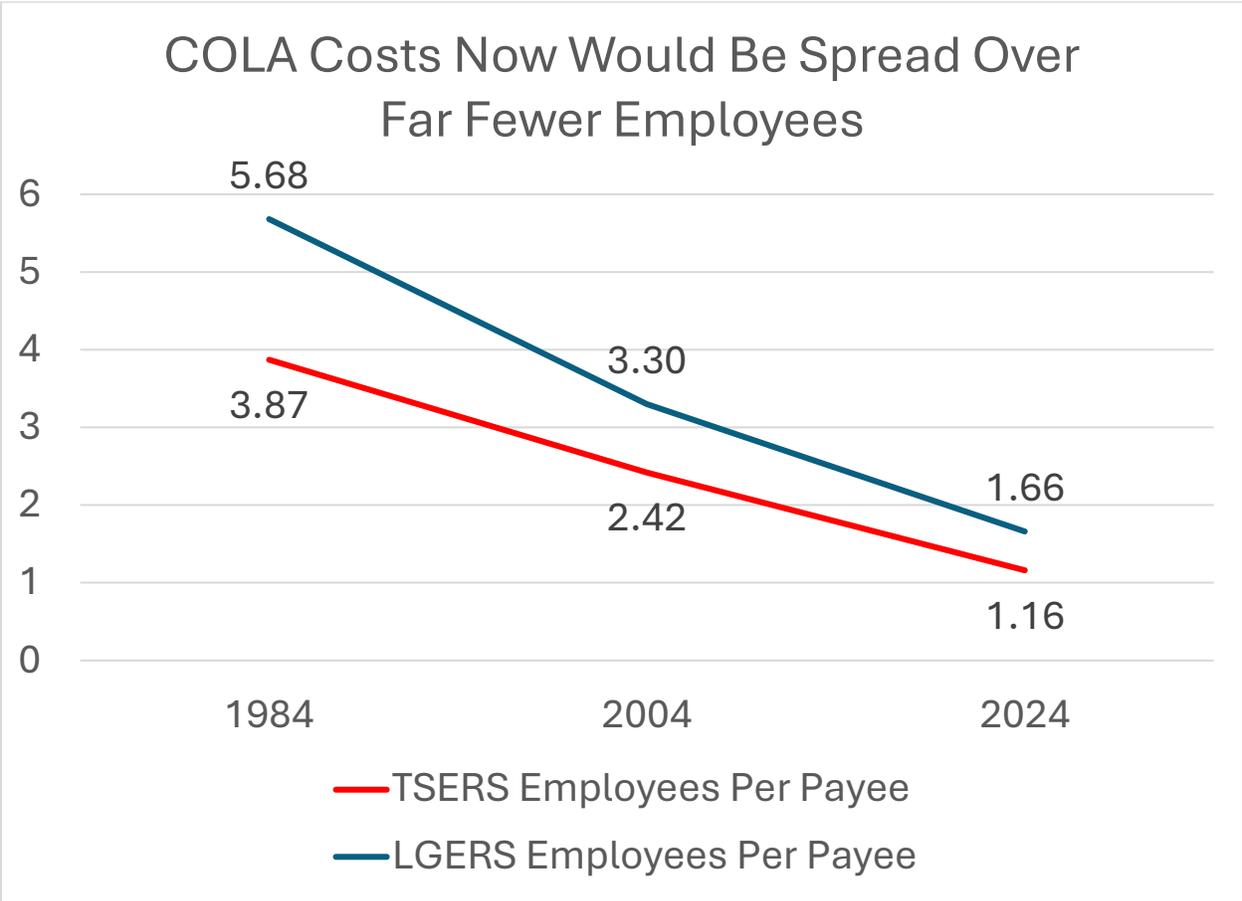
<b>Employer Contribution Rate (Percent of Compensation)</b>	<b>TSERS</b>	<b>LGERS</b>
1% COLA (paid for 12 years 7/1/2026 – 6/30/2038)	0.39%	0.28%
1% supplement (paid for 1 year 7/1/2026 – 6/30/2027)	0.29%	0.20%

- If paid by direct legislative appropriation, the cost would be the dollar amount shown under Unfunded Liabilities. For example, a 1% COLA to TSERS retirees would require total funding of \$586,739,000, with interest from December 31, 2024 until the date(s) paid to TSERS.

*Q17. Why has funding COLAs become more challenging over the years?*

- There are several reasons. One major reason is that the retiree population has grown, while the number of active employees has not grown at the same rate. COLAs are paid to retirees, but they are typically paid for as part of personnel budgets. This means increasing the cost of employing each current employee.
- The cost of COLAs (in dollars) has grown, as the number of retirees has grown.
- The fact that the active employee population has not grown at the same rate means that this higher COLA cost must be spread over fewer and fewer employees.
- The graph below shows how this has worked. For example, 40 years ago, the average COLA for a State retiree could be spread over the labor costs of four (3.87) employees. The retiree population has grown so much that, today, that cost would have to be spread over just one (1.16) employee.
- Other reasons COLAs have become harder to pay for include:
  - the development of significant unfunded liabilities,
  - past investment performance,

- longer life expectancies, and
- the fact that the future long-term investment return assumptions that were used well into the 2010s are no longer reasonable.



## **Decision-Making**

*Q18. Who can authorize COLAs or supplements?*

- For TSERS, only the legislature can authorize a COLA or supplement. Judicial and legislative retirees receive any adjustment enacted for TSERS. The Board can, and does, recommend to the legislature how much of a COLA or supplement (if any) could be funded by investment gains. The Board can also recommend to the legislature that any enacted COLA or supplement be funded through increased employer contributions or direct appropriations.
  - For LGERS:
    - The legislature has delegated to the Board the ability to authorize either a COLA or a supplement in each year, subject to limitations. These limitations include that there must be investment gains available to fund the associated actuarial liabilities, and the COLA or supplement is limited to 4% or the most recent year's inflation, whichever is less.
    - If there were investment gains available, the Board could authorize a COLA or supplement, but could still choose to increase the employer contribution rate to pay for some or all of it.
    - The legislature could authorize a COLA or supplement. The legislature is not bound by the same limitations as the Board. However, if the Board were to request such an action by the legislature, the Board would need to acknowledge the cost that would be associated with the request. By doing so, the Board would be inviting the legislature to mandate adjustments to local government employer contribution rates, which the legislature has not done in modern history.
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*Q19. Given that there are no investment gains, what are the general "boundaries" for Board actions in January 2026?*

- The LGERS Board could not, on its own, authorize a COLA or supplement for the fiscal year beginning July 1, 2026, because there were no investment gains available to pay for it. That is one of the conditions that must be met for the LGERS Board to authorize a COLA or supplement.
- Either the TSERS or LGERS Board could recommend that the legislature enact a COLA or supplement for the fiscal year beginning July 1, 2026.
- Since there are no investment gains available, this would need to come with a recommendation of one or more ways to pay for the COLA or supplement, through increased employer contribution rates or direct legislative appropriations. (See "Paying for the Costs.")
- For LGERS, such a recommendation would amount to inviting the legislature to establish the employer contribution rate for local governments, which the legislature has not done

in modern history. If this occurs, the legislature would not be bound by the LGERS Board's funding policy. For example, the legislature may decide that any further employer contributions for the fiscal year should first be applied to the likely \$30-\$40 million underfunding of the actuarially determined contributions, before further increasing contributions for a COLA or supplement.

- For either TSERS or LGERS, a recommendation of direct legislative appropriations to fund the full cost of a COLA or supplement would create a "mismatch" in funding sources. The personnel budgets typically used to fund TSERS employer contributions include budgets for positions supported by the General Fund, Highway Fund, and employer receipts. The personnel budgets used to fund LGERS employer contributions are local government budgets. A recommendation of direct legislative appropriations, while not impossible, would represent a change in funding sources with respect to many of the contributions.

## Appendix A: Estimated Effect of Historical Inflation on TSERS and LGERS Retirees

As noted in FAQ #5, the effect of inflation on each retiree is a complicated question and varies from case to case. It depends in part on when they retired, inflation levels since then, and how much has been granted in COLAs since then.

Another complicating factor is that for most of today's retirees, the legislature made their eventual pensions more generous during their careers, by increasing the "multiplier" in the pension formula. Most of today's employees, on the other hand, have seen small, if any, increases during their careers. (The multiplier has not changed since 2002 for TSERS, and since 2003 for LGERS.)

The tables below show how much more a retiree is receiving today, compared to what would have been payable based on the terms of TSERS or LGERS when they were hired. This comparison is on row 9. It then compares that increase to inflation since they retired (based on CPI-U). Row 11 shows what percentage of the increase in inflation since retirement has been covered by legislated increases to the TSERS or LGERS benefit during or after the person's career. For example, "100%" in Row 11 would mean that the increases to the retiree's TSERS or LGERS benefit, enacted during or after the retiree's working career, have been equal to the inflation in cost of living that the retiree has experienced since retirement.

The four examples below are for retirees who worked from age 35 to age 65 and retired after 30 years of membership. Their dates of birth, hire, and retirement are all assumed to have occurred at the beginning of the year. The example retirees would be 70, 80, 90, or 95 years old as of 2025. (A 100-year-old in this situation would have been hired before the modern versions of TSERS and LGERS were enacted.)

### TSERS

1. Age in January 2025	95	90	80	70
2. Year of Birth (YOB)	1930	1935	1945	1955
3. Year of Hire (YOH)	1965	1970	1980	1990
4. Year of Retirement (YOR)	1995	2000	2010	2020
5. Benefit Multiplier in YOH (x Service x Avg. Final Comp.)*	1.00%	1.25%	1.55%	1.63%
6. Benefit Multiplier in YOR (x Service x Avg. Final Comp.)	1.73%	1.80%	1.82%	1.82%
7. Legislated Increase in Benefits During Career (6./5.)	73%	44%	17%	12%
8. Cumulative COLA Increases Granted During Retirement**	51%	26%	3%	0%
9. Benefit vs. \$1 Pension from Terms in YOH (( $\$1+7.$ )x( $\$1+8.$ ))	\$2.62	\$1.82	\$1.21	\$1.12
10. Inflation of \$1 in Cost of Living (YOR Through Jan. 2025)	\$2.11	\$1.88	\$1.47	\$1.23
11. Benefit Increases During or After Career Have Covered % of Cost of Living with Postretirement Inflation (9./10.)	124%	97%	83%	91%

LGERS

1. Age in January 2025	95	90	80	70
2. Year of Birth (YOB)	1930	1935	1945	1955
3. Year of Hire (YOH)	1965	1970	1980	1990
4. Year of Retirement (YOR)	1995	2000	2010	2020
5. Benefit Multiplier in YOH (x Service x Avg. Final Comp.)*	1.00%	1.25%	1.55%	1.63%
6. Benefit Multiplier in YOR (x Service x Avg. Final Comp.)	1.71%	1.77%	1.85%	1.85%
7. Legislated Increase in Benefits During Career (6./5.)	71%	42%	19%	13%
8. Cumulative COLA Increases Granted During Retirement**	39%	21%	1%	0%
9. Benefit vs. \$1 Pension from Terms in YOH (((\$1+7.)x(\$1+8.))	\$2.38	\$1.72	\$1.20	\$1.13
10. Inflation of \$1 in Cost of Living (YOR Through Jan. 2025)	\$2.11	\$1.88	\$1.47	\$1.23
11. Benefit Increases During or After Career Have Covered % of Cost of Living with Postretirement Inflation (9./10.)	113%	91%	82%	92%

Notes on tables above:

\* In some years, the benefit multiplier had more than one “tier,” with a higher multiplier applied to earnings above a certain dollar amount. The lower tier is shown.

\*\* Cumulative COLA increases in retirement do not include supplements. They also do not include any amount that the retiree may have received from the “graduated catch-up” LGERS COLA in 2003. However, in certain years when a portion of a COLA was prorated for those who had retired within the prior 12 months, the retiree is assumed to have received the full COLA.

The following two pages provide calculations of “Row 11” for all combinations of “year of hire” and “year of retirement” for individuals hired from the mid-1960s until 2005, who retired after 20-40 years of membership.





## **Appendix B: Statutory Provisions, Board Policies, and Other Reference Documents**

- I. Key Statutory Provisions and Board Policy Provisions for TSERS
  - a. G.S. 135-5(o) provides that TSERS retirees and beneficiaries “shall be entitled to” inflation-based (limited to 4%) adjustments to retirement allowances “provided that any such increase in allowances shall become effective only if the additional liabilities on account of such increase do not require an increase in the total employer rate of contributions.”
  - b. G.S. 135-5(o) further provides that TSERS retirees and beneficiaries “may receive cost-of-living increases in retirement allowances if active members of the system receive across-the-board cost-of-living salary increases. Such increases in post-retirement allowances shall be comparable to cost-of-living salary increases for active members in light of the differences between the statutory payroll deductions for State retirement contributions, Social Security taxes, State income withholding taxes, and federal income withholding taxes required of each group. The increases for retired members shall include the cost-of-living increases provided in this section [i.e., in I.a. above]. The cost-of-living increases allowed retired and active members of the system shall be comparable when each group receives an increase that has the same relative impact upon the net disposable income of each group.”
  - c. Under the Board’s [Employer Contribution Rate Stabilization Policy \(ECRSP\)](#), the Board should recommend a contribution rate for FY ending 2027 at least equal to the recommended contribution rate for FY ending 2026 plus 0.35% of compensation. For this purpose, the recommendation for FY ending 2026 “should be adjusted for the effect of any benefit change enacted by the General Assembly, taking effect during [FY ending 2027], including COLA supplements, that was not incorporated in the Board’s recommendation for [FY ending 2026].”
- II. Key Statutory Provisions and Board Policy Provisions for LGERS
  - a. G.S. 128-27(k) provides that LGERS retirees and beneficiaries “shall be entitled to” inflation-based (limited to 4%) adjustments to retirement allowances “provided that any such increase in allowances shall be contingent upon the total fund providing sufficient investment gains to cover the additional actuarial liabilities on account of such increase. The determination of whether there are sufficient investment gains to cover the possible postretirement increase in allowance shall reside exclusively within the discretion of the Board of Trustees and shall be informed by the findings within the annual actuarial valuation reports. In considering whether to grant a postretirement increase, the Board of Trustees shall take into account both the rate of inflation as determined by the Consumer Price Index and the record of investment gains or losses during the preceding three-year period.”

- b. G.S. 128-27(k) further provides that “[n]otwithstanding the foregoing linkage between increases in the Consumer Price Index and correlative contingent increases in retirement benefits determined by the availability of sufficient investment gains to cover the additional actuarial liabilities arising from those increased benefits, the Board of Trustees, may in any year, considering an increase, if any, in the Consumer Price Index, fund a cost-of-living increase in a percentage amount, measured in tenths of one percent (1/10 of 1%), of up to four percent (4%), provided that the Board may use only investment gains to fund such an increase.”
- c. G.S. 128-27(k1) provides that LGERS retirees and beneficiaries “shall be entitled to” inflation-based (limited to 4%) one-time pension supplement payments, “provided that any such one-time pension supplement shall be contingent upon a determination by the Board of Trustees under subsection (k) of this section that a permanent increase in benefits will not be paid during the same fiscal year as the one-time pension supplement, but the total fund is providing sufficient investment gains to cover the additional actuarial liabilities on account of such one-time pension supplement. The determination of whether there are sufficient investment gains to cover the one-time pension supplement shall reside exclusively within the discretion of the Board of Trustees and shall be informed by the findings within the annual actuarial valuation reports. In considering whether to grant a one-time pension supplement, the Board of Trustees shall take into account both the rate of inflation as determined by the Consumer Price Index and the record of investment gains or losses during the preceding three-year period.”
- d. Under the Board’s [Employer Contribution Rate Stabilization Policy \(ECRSP\)](#), the employer contribution rate for FY ending 2027 should be adjusted “for the effect of any enacted benefit change taking effect before or during [FY ending 2027] that was not incorporated in the Policy Contribution [for FY ending 2026].”

### III. Reports

- a. [TSERS actuarial valuation report](#) published October 2025, describing the funded status of TSERS as of December 2024.
- b. [LGERS actuarial valuation report](#) published October 2025, describing the funded status of TSERS as of December 2024.
- c. Consumer Price Index history through November 2025 from the U.S. Bureau of Labor Statistics. ([Link will open Excel spreadsheet.](#))
- d. Website with reports made to the [N.C. Investment Authority Board](#).