TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM (TSERS)

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Employer Contribution Rate Stabilization Policy (ECRSP) Summary

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Agenda

- Background: ECRSPs in General; TSERS ECRSP for FY 2017-2022
- Summary of Proposed Version for FY 2023-2027
- Hypothetical Examples

Background: History of TSERS ECRSP

- TSERS Board adopted January 21, 2016
- Effective through the fiscal year ending June 30, 2022
- Describes annual appropriation recommendation
- G.S. 135-8(d)(3a), added by S.L. 2017-129, provides: “Notwithstanding Chapter 150B of the General Statutes, the total amount payable in each year to the pension accumulation fund shall not be less than the sum of the rate per centum known as the actuarially determined employer contribution rate of the total earned compensation of all members during the preceding year as adjusted higher under a contribution rate policy adopted by the Board of Trustees and known as the ‘required employer contribution’ rate. The Board of Trustees shall not adopt a contribution rate policy that results in a rate less than the normal contribution rate.”
- Policy to set required contribution rate is not subject to rule-making; G.S. 135-8(d)(a3) and 150B-1(d)(30)
- Does not describe recommendation about cost-of-living allowances (COLAs) or other benefit improvements – separate decision guided by statute

Background: General Goals of ECRSPs

- ECRSPs are designed to address volatility in budgets as well as actual contributions
- Goals – some of which are in tension with each other
  - Contribute at least the actuarially determined rates (ADECs) over the policy period
  - Do not burden governments with contributions far in excess of ADEC
  - Increase predictability as much as possible so governments know rate far in advance
  - Attempt to limit year-over-year contribution increases and spread them out over time
  - Position budgets as well as possible for what may be required after policy period
  - Reduce volatility by avoiding “V” or “W” shape in contribution rates
- All this is accomplished by calling for contributions greater than the ADEC in some years, in order to offset any future sudden increases
- May allow decline in contributions if there is a sustained and sustainable ADEC decline
- May address related issues (COLAs, unexpected plan or assumption changes, etc.)

Background: Policy Contribution for FY 2017-2022

- Annual appropriation recommendation in January, for an upcoming fiscal year
  - Greater of (1) or (2)
    - (1): Underlying actuarially determined employer contribution rate (ADEC) for upcoming year
    - (2): Appropriation for current year increased by 0.35% of pay
  - But no greater than (3)
    - (3): Underlying ADEC determined using discount rate equal to yield on 30-year U.S. Treasury securities as of actuarial valuation date

Looking Ahead: Rationale for Continued Gradual Increases

- 12-year amortization policy and 2020 investment return have tempered the forecast of underlying ADEC increases
- Consulting actuary's projection as of Jan. 2021 shows underlying ADECs level/decreasing starting FYE 2023 if all assumptions are met (including 6.50% annual rate of return)
- However, significant risk of steep increases remains:
  - Volatility of capital markets (investment returns)
  - Increasing ratio of pension liability to current employee payroll
- In event of significant increases, providing for 0.35% escalation in advance will help to limit the increases and spread them out over time
  - Staff actuary's estimate: If policy recommended simply the underlying ADEC, 45%-55% probability of a year-over-year increase of at least 1.00% of pay at some point during the five-year period; with the 0.35% annual escalation, this becomes a 20%-30% probability [1]
- Providing some minimum contribution rate prevents occurrence of "V" shape in contribution recommendations / appropriations; staff actuary estimates more than 50% likely during five-year period if contribution were equal to underlying ADEC [1]

[1] Methodology description and actuarial certification available upon request from Retirement Systems.

Summary of Proposed ECRSP for FY 2023-2027

- Maintains basic pattern of calling for contribution rates at least equal to underlying ADEC, and at least equal to prior year's policy rate plus 0.35% of pay
- Clarifies how the Board's current year recommendation (generally a year old by the time of the decision for upcoming year) and the underlying ADEC (generally calculated months prior) should be adjusted for intervening events, such as enacted benefit changes or assumption/method changes
- Clarifies that the maximum contribution rate in part (3) of the definition applies only to limiting part (2); it cannot limit part (1) because statute requires that the policy contribution rate be at least equal to the Underlying ADEC
- Defines terminology
- Updates the policy with specific references to statutory provisions added in 2017

Examples – Policy Recommendation Jan. 2025 for FYE 6/30/2026

	[1]	[2]	[3]	[4]	[5]
(1) Underlying ADEC for FYE 6/30/2026 (from 12/31/2023 actuarial valuation report adopted Oct. 2024)	18.00%	18.00%	**10.00%**	18.00%	18.00%
Adjustment: Enacted benefit change not in actuary's report	0.00%	0.00%	0.00%	0.00%	0.00%
Adjusted (1)	18.00%	18.00%	10.00%	18.00%	18.00%
(2) Appropriation recommended for FYE 6/30/25	17.50%	**17.80%**	17.50%	17.80%	17.50%
Adjustments:					
(a) NCGA-enacted benefit change not in FYE 6/30/25 rec.; excludes one-time supplements effective for FYE 6/30/25 unless recurring approp.	0.00%	0.00%	0.00%	0.00%	**0.50%**
(b) Effect of actuarial assumption/method changes not incorporated in FYE 6/30/25 recommendation	0.00%	0.00%	0.00%	0.00%	0.00%
Adjusted (2)	17.50%	17.80%	17.50%	17.80%	18.00%
(3) Underlying ADEC for FYE 6/30/2026, 30-Yr Treas. Rate	60.00%	60.00%	60.00%	**18.05%**	60.00%
Adjustment: Enacted benefit change not in actuary's report	0.00%	0.00%	0.00%	0.00%	0.00%
Adjusted (3)	60.00%	60.00%	60.00%	18.05%	60.00%
Greater of Adj. (1), or Adj. (2) + 0.35% Limited to Adj. (3)	18.00%	18.15%	17.85%	18.05%	18.35%

[1] Recommendation equal to Underlying ADEC since it exceeds current-year recommendation by more than 0.35%.
[2] Recommendation equal to current-year recommendation plus 0.35%, since that exceeds Underlying ADEC.
[3] Recommendation equal to current-year recommendation plus 0.35%, although it far exceeds Underlying ADEC.
[4] Assumes significant increase in 30-year Treasury yields causing part (3) to limit the recommendation under part (2).
[5] Assumes COLA enacted after Jan. 2024 (Board's current year recommendation) but before Oct. 2024 (actuary's report).