

GENERAL ASSEMBLY OF NORTH CAROLINA

Session 2015

Legislative Retirement Note

BILL NUMBER: House Bill 1134 (Second Edition)

SHORT TITLE: Admin. Changes Retirement System/Treasurer.

SPONSOR(S): Representatives McNeill and Ross

FUNDS AFFECTED: State General Fund, State Highway Fund, other State employer receipts; local government funds

SYSTEM OR PROGRAM AFFECTED: Teachers' and State Employees' Retirement System (TSERS), Consolidated Judicial Retirement System (CJRS), Legislative Retirement System (LRS), Local Governmental Employees' Retirement System (LGERS), Disability Income Plan (DIP), National Guard Pension Fund (NGPF), Firefighters' and Rescue Squad Workers' Pension Fund (FRSWPF), and the North Carolina Public School Teachers' and Professional Educators' Investment Plan (NC 403(b)).

BILL SUMMARY:

Section 1: Extends the monthly benefit in the FRSWPF to the named beneficiary of a member killed in the line-of-duty (as defined in G.S. 143-166.2(c) for the \$50,000 death benefit). The benefit is payable for 300 months or until the beneficiary's death, whichever comes first. Also allows all members to name a beneficiary for the return of contributions, which goes to the spouse, children, or estate, in that order, under current law.

Section 2: Amends statutes governing the FRSWPF, TSERS, and LGERS to improve the Retirement Systems Division's ability to collect repayment of overpaid benefits.

Section 3: Defines a Normal Retirement Age (NRA) and changes the date at which unreduced benefits are payable in TSERS, LGERS, and CJRS for those who become members on or after January 1, 2017. Does not change benefits for any current members. The following table shows the changes:

Retirement System	Unreduced Retirement Eligibility for Current Members (Earliest of Conditions Shown)	Unreduced Retirement Eligibility for Those who Become Members after 2016 (Earliest of Conditions)
TSERS/LGERS Law-Enforcement (LEO)	Age 55 with 5 years of service Any age with 30 years	Age 55 with 5 years of service Age 50 with 30 years
TSERS/LGERS Non-LEO	Age 65 with 5 years of service Age 60 with 25 years Any age with 30 years	Age 65 with 5 years of service Age 60 with 25 years Age 50 with 30 years
CJRS	Age 65 with 5 years of service Age 50 with 24 years	Age 65 with 5 years of service Age 50 with 30 years

The Second Edition does not change eligibility for early (reduced) retirement benefits. However, it does change the reduction formula, as discussed further below in the estimated impact.

The Second Edition also directs the Program Evaluation Division to complete a study comparing compensation and benefits in NC to those in states that have implemented a NRA.

Section 4: Extends the Retirement System Division (RSD)'s access to an employing agency's persons and records when RSD staff is conducting a compliance investigation to detect errors and ensure accountability. RSD currently has access to these persons and records when conducting an investigation of fraud.

Section 5: Clarifies the time period during which an employing agency may make payments under the Contribution Based Benefit Cap provision in TSERS and LGERS. The Cap is intended to more accurately distribute the cost of "pension spiking", i.e. large increases in compensation during the four years that are used in calculating the benefit. With this change the employing agency could choose payment without interest between 3 and 15 months after the member's retirement or with interest between 3 and 27 months after retirement.

Section 6: Clarifies that factors that apply to the Cap do not have to be set through the rule making process under Chapter 150B and changes the timing of the inflation indexing of the minimum earnings below which the Cap does not apply.

Section 7: Allows members of several Systems to elect beneficiaries on-line, rather than by paper form, regardless of the amount of service they have. Currently beneficiaries cannot be elected on-line if the member has 10 or more years of service.

Section 8: Replaces a higher education appointee as a member of the TSERS Board of Trustees with the Director of the Office of State Human Resources. Also establishes the State Treasurer as the chairperson of the Boards and gives the Treasurer authority to appoint the director of the Retirement System.

Section 9: Creates an exemption to State classification and compensation rules for employees with specialized retirement administration skills.

Section 10: Creates a fund under the control of the Boards of Trustees of TSERS and LGERS that can be used to pay for the cost of implementing any legislated benefit changes that will result in future reductions in contributions. The maximum amount that can be directed into the fund is 0.01% of compensation.

Section 11: Separates statutes governing what is public within membership records held by the Retirement Systems Division from statutes governing what is public record within employment files held by employing agencies.

Section 12: Clarifies that certain documents can be transmitted by means other than physical mail.

Section 13: Modifies statutes allowing the Retirement Systems Division to deduct payments to employees' and retirees' associations from retiree benefit payments. The required membership count for some associations is increased from 2,000 to 10,000 and proof of authorization from the member to deduct the payment must be made available upon request.

Sections 15-17: Affect Department of State Treasurer operations unrelated to the Retirement Systems, so are not addressed in this note.

Section 18: Clarifies governance statutes for the NC 403(b) Plan.

Section 19: Requires that employers who receive a report that they are likely to owe an additional contribution under the Contribution Based Benefit Cap must forward that report to certain governing bodies of the employer.

Section 20: Eliminates conversion of additional benefits to salary from the definition of Compensation for retirement purposes for those who become members of TSERS or LGERS after 2016. The section does not affect the definition for any current members.

Section 21: Grants the Retirement Systems Division additional flexibility in requiring reports of earnings from DIP recipients.

EFFECTIVE DATE: Section 1 becomes effective July 1, 2018. Sections 2, 3, 7, 9, and 20 become effective January 1, 2017. Sections 4, 5, 6, 8, 11, 12, 13, 14, 16, 17, 18, 19, and 21 become effective when they become law. Sections 10 and 15 become effective October 1, 2016.

ESTIMATED IMPACT ON STATE:

Section 1:

Buck Consultants, the actuary for the Retirement Systems, estimates that the line-of-duty death provision of this section will increase the actuarially determined contribution for the FRSWPF by \$96,000 per year. Buck Consultants estimates that the contribution would increase by \$103,000 per year if the benefits were paid for the life of the beneficiary, without the 300 month cap.

Hartman & Associates, the actuary for the General Assembly, estimates that the line-of-duty death provision of this section will increase the actuarially determined contribution for the FRSWPF by approximately \$50,000 per year.

Both the House budget (HB 1030, Fourth Edition) and the Senate budget (HB 1030, Sixth Edition) contain a revised net appropriation to the FRSWPF of \$17.6 million. Based on a June 10, 2016 letter from Buck Consultants revising the actuarially determined contribution for FY 2016-17, this amount is sufficient to cover the contribution increase due to this section and adopt a contribution stabilization policy similar to those adopted for TSERS and LGERS.

Section 3: Buck Consultants and Hartman & Associates estimate the following long-term increase/(reduction) in the normal cost (and therefore the actuarially determined contribution) due to this section:

System	Buck Consultants	Hartman & Associates
TSERS	0.00% of pay	0.04% of pay
LGERS	(0.01%) non-LEO, (0.11%) LEO	0.05%
CJRS	(0.66%)	(0.67%)

Under current law, a reduction of the lesser of 3% per year prior to age 65 or 5% per year prior to 30 years of service applies to those retiring after age 60 in TSERS and LGERS. In the Second Edition, the second reduction is changed to 5% per year prior to NRA. For a small group of individuals, this can result in a lower reduction and higher benefit. For example, an individual who retires at age 61 with 24 years of service would be reduced by 5% in the Second Edition (from NRA of 62 with 25 years), but by 3% x 4 = 12% (from age 65) under current law. Buck Consultants assumed that this was a drafting error and ignored the change, while Hartman & Associates evaluated the bill as written. We believe this is the primary reason why Buck Consultants estimates a small reduction in normal cost and Hartman & Associates estimates a small increase in normal cost.

Both actuaries agree that this section will have no impact on the actuarially determined contribution in FY 2016-17.

Both actuaries estimate that the other sections of the Second Edition will have no material impact on the contribution rates or liabilities of any of the systems affected. However, Buck Consultants further notes with regard to Sections 4, 5, 7, 9, 10, and 12 that these measures could possibly result in more contributions or lower administrative costs for the Retirement System, which would be a positive outcome for the Retirement System. That being said, within the actuarial framework, they are unable to quantify the actuarial impact based on the information provided.

ASSUMPTIONS AND METHODOLOGY:

The cost estimates of the System's Actuary are based on the employee data, actuarial assumptions and actuarial methods used to prepare the December 31, 2014 actuarial valuations. Significant membership and financial statistics, assumptions, and methods are shown in the following tables:

Membership Statistics (as of 12/31/2014 unless otherwise noted, M = millions)				
	<u>TSERS</u>	<u>LGERS</u>	<u>CJRS</u>	<u>FRSWPF</u>
Active Members				
Count	307,313	123,184	566	43,134
General Fund Compensation	\$9,865M		\$70M	
Valuation Compensation (Total)	\$13,737M	\$5,652M	\$71M	Not applicable
Average Age	45	44	55	40
Average Service	10.7	10.3	13.0	11.7

Inactive Members				
Count	134,871	55,298	50	153
Retired Members				
Count	194,607	60,408	610	12,730
Annual Benefits	\$4,058M	\$1,109M	\$37M	\$26M
Average Age	70	68	72	68
New Retirees During 2015	11,400	4,100	50	600

Financial Statistics (as of 12/31/2014 unless otherwise noted, M = millions)				
	<u>TSERS</u>	<u>LGERS</u>	<u>CJRS</u>	<u>FRSWPF</u>
Accrued Liability (AL)	\$67,715M	Not meaningful	\$567M	\$419M
Actuarial Value of Assets (AVA)	\$64,734M	\$22,682M	\$534M	\$381M
Market Value of Assets (MVA)	\$64,587M	\$22,745M	\$534M	\$383M
Unfunded Accrued Liability (AL - AVA)	\$2,981M	Not meaningful	\$33M	\$38M
Funded Status (AVA / AL)	96%	Not meaningful	94%	91%
Annual Required Contribution (ARC) for FY 2016-17 (as % of pay)	9.50% (new assumptions)	7.25% (non-LEO)	28.53%	\$17.6M (prior to new lapse assumption)
Assumed Rate of Investment Return	7.25%	7.25%	7.25%	7.25%
Salary Increase Assumption (includes 3.50% inflation and productivity)	3.50% - 6.86%	3.50% - 6.71%	3.50% - 5.50%	Not applicable
Cost Method	Entry Age Normal	Frozen Entry Age	Entry Age Normal	Entry Age Normal
Amortization	12 year, closed, flat \$	Not applicable	12 year, closed, flat \$	12 year, closed, flat \$
Demographic assumptions based on 2010-2014 experience, RP-2014 mortality, and projection of future mortality improvement with scale MP-2015				

Benefit Provisions				
	<u>TSERS</u>	<u>LGERS</u>	<u>CJRS</u>	<u>FRSWPF</u>
Formula	1.82% x Service x 4 Year Avg Pay	1.85% x Service x 4 Year Avg Pay	3.02% to 4.02% x Service x Final Pay	\$170 per month

Unreduced retirement age/service	Any/30; 60/25; 65 (55 for LEO)/5	Any/30; 60/25; 65 (55 for LEO)/5	50/24; 65/5	55/20
Employee contribution (as % of pay)	6%	6%	6%	\$10 per month

Further detailed information concerning these assumptions and methods is shown in the actuary's report, which is available upon request from David Vanderweide.

SOURCES OF DATA:

Buck Consultants, “Administrative Changes Retirement System/Treasurer – House Bill 1134 (Committee Substitute Favorable 5/31/16)”, June 15, 2016, original of which is on file in the General Assembly’s Fiscal Research Division.

Hartman & Associates, LLC, “House Bill 1134 Committee Substitute 5/31/16: An Act to Make Administrative Changes to the Retirement System and to Make Other Changes Affecting the State Treasurer”, June 2, 2016, original of which is on file in the General Assembly’s Fiscal Research Division.

Buck Consultants, “Adjusted Actuarially Determined Contribution for the FRSWPF for FYE 2017”, June 10, 2016, original of which is on file in the General Assembly’s Fiscal Research Division.

TECHNICAL CONSIDERATIONS:

FISCAL RESEARCH DIVISION: (919) 733-4910.

The above information is provided in accordance with North Carolina General Statute 120-114 and applicable rules of the North Carolina Senate and House of Representatives.

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DATE: June 20, 2016



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