

GENERAL ASSEMBLY OF NORTH CAROLINA

Session 2011

Legislative Actuarial Note

RETIREMENT

BILL NUMBER: House Bill 656 (Third Edition)

SHORT TITLE: Allow Sheriffs' Assn. in LGERS.

SPONSOR(S):

FUNDS AFFECTED: Funds of the North Carolina Sheriffs' Association

SYSTEM OR PROGRAM AFFECTED: Local Governmental Employees' Retirement System

EFFECTIVE DATE: July 1, 2011

BILL SUMMARY: House Bill 656 (Third Edition), includes uncodified language generally declaring the N.C. Sheriffs' Association an instrumentality of the State, and further amends G.S. 128-21 to include the Sheriffs' Association under the definition of "employer" for purposes of allowing the Sheriffs' Association to elect to participate in the Local Governmental Employees' retirement System, thus allowing its employees to become participating members of the Local Governmental Employees' Retirement System.

ESTIMATED IMPACT ON STATE: Both the consulting actuary to the Retirement Systems Division of the Department of State Treasurer, Buck Consultants, and the consulting actuary to the General Assembly's Fiscal Research Division, Hartman & Associates, estimate that there would be no cost to the State as a result of the expectation that the North Carolina Sheriffs' Association will pay the required employer contributions to provide their employees a defined benefit from the Local Governmental Employees' Retirement System.

There are possible issues with respect to the proposed legislation affecting the Local Governmental Employees' Retirement System's governmental plan status under Internal Revenue Service requirements as noted in the comments in the "Technical Considerations" section below.

ASSUMPTIONS AND METHODOLOGY: Local Governmental Employees' Retirement System: 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, 2009 actuarial valuation of the fund. The data included 123,398 active members with an annual payroll of \$5.2 billion, 46,557 retired members in receipt of annual pensions totaling \$795.8 million and actuarial value of assets equal to \$17.7 billion. Significant actuarial assumptions used include the following: (a) an investment return rate of 7.25% which includes inflation of 3%; (b) projected salary increases between 4.25% to 8.55% which includes inflation of 3.5%; (c) RP-2000 Mortality tables for retirees are set forward two years for male general employees, firemen and law enforcement and unadjusted for female general employees; (d) RP-2000 Mortality tables for disabled retirees are set back six years for males and set forward one year for females; (e) RP-2000 Mortality tables for active employees are set forward two years for male general

employees, firemen and law enforcement officers and unadjusted for female general employees; and (f) rates of separation from active service based on System experience. The actuarial cost method used was the frozen entry age. Gains and losses are reflected in the normal rate. Detailed information concerning these assumptions and methods is shown in the actuary's report, which is available upon request from the General Assembly's Fiscal Research Division.

SOURCES OF DATA: Buck Consultants
Hartman & Associates, LLC

TECHNICAL CONSIDERATIONS: The status of the N.C. Sheriffs' Association as a non-profit organization may conflict with Internal Revenue Service guidance provided in 2001 to the Retirement Systems Division regarding the participation of non-profit organizations in the Local Governmental Employees' Retirement System where the State or a political subdivision does not exert a degree of control over that organization's everyday operations. Deeming the N.C. Sheriffs' Association as an instrumentality of the State may not be sufficient in meeting the Internal Revenue Service's test in determining whether an organization is, in fact, an instrumentality of the State as outlined in Revenue Ruling 89-49, 1989-1 C.B. 117. Per the ruling, for an organization to meet the instrumentality test the State or other political subdivision must exert a degree of control over the organization in question. Additional opinions of the N.C. Attorney General issued in June 2011 have also raised concerns regarding the effect of the Sheriffs' Association's participation in the Local Governmental Employees Retirement System on the plan's governmental status and tax treatment. A plan which is a governmental plan is entitled to special tax treatment, and is also exempt from many provisions of Title I of ERISA.

The N.C. Attorney General cited several factors in reaching its opinion, including the lack of statutes creating or limiting the actions of the Sheriffs' Association, the fact that over 90% of the Sheriffs' Association's funding comes from sources other than direct governmental appropriations, and the lack of evidence that employees of the Sheriffs' Association are considered to be or are treated as employees of the local governments. Previously local non-profit volunteer fire departments have been required to cease participation in the Local Governmental Employees Retirement System based on a private letter ruling from the Internal Revenue Service indicating participation by these non-profits risked the loss of the benefit plan's governmental status.

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 17, 2011



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