



April 15, 2019

Dear Senator Wells:

Thank you for requesting information about how **SB 374 (Repeal Risky Retirement Payments)** protects the North Carolina Retirement Systems. This bill preserves the ability of retirees to receive the entire payment over their own lifetime, or with 100 percent or 50 percent survivorship. It also reduces risk in three important ways.

1. **Risk to members.** In the next 15 years, the number of retirees and beneficiaries receiving payment will increase by more than 40 percent, from 318,000 to more than 460,000. Further, we expect that half of future retirees will eventually apply for retirement online. Because of this, they will need fewer, simpler options, to avoid making harmful decisions, like choosing Social Security Leveling, without proper advice.

Our office has recently discovered **more than \$10 million** in overpayments and underpayments that were made in the past, under the payment options eliminated by the bill. Correcting errors causes pain and difficulty for our members and is often not noted from the system. For example, if the surviving beneficiary dies first, the system has no way of discovering that fact.

2. **Risk to predictability of funding.** All actuarial calculations assume that pension investments can earn a rate of return that they have not achieved, on average, over the last 20 years, nor are they likely to over the next 20 years thus requiring additional contributions be made by employers and/or employees. Furthermore, our systems are paying out more money than they are taking in every year. Lower returns are especially detrimental when they coincide with increased cash outflows.

For a sense of scale, if employer contributions to the Teachers' and State Employees' Retirement System (TSERS) changed by 5-10 percent because of an adverse experience - like a minor change in investment or life expectancies - it would mean a cost of **\$60-\$120 million per year from the General Fund**. To manage risk, we need to simplify many things about retirement benefits - SB 374 addresses one of those risks.

3. **Risk to administrative efficiency.** Our office estimates that if the payment options repealed by SB 374 had never been in effect, today's administrative costs could be **\$2 million per year** less. However, because we will still have to administer the options for members who elected them in the past, the bill will not immediately achieve these savings. It does eliminate many complicated payment options that are difficult to administer in many areas.

Some have expressed concern that this bill could be challenged in court for impairing a contract. The Department's position is that members will receive the actuarial equivalent benefits that they are entitled to, so their contractual rights have not been impaired.

Additionally, the legislature's authority to repeal payment options has been exercised before and has never been challenged. For example, Session Law 1993-321 repealed two risky options, and the current Governor voted in favor of that law as a member of the Senate.

At the State Treasurer's office, we are finding and fixing problems that create unnecessary cost and risk. SB 374 is one measure toward preserving the defined benefit system for the next generation of public servants. Those who oppose the bill need to understand that we are not here to hurt people, but sustain the system.

Sincerely,

Dale R. Folwell, CPA
North Carolina State Treasurer