Department of State Treasurer Should Strengthen Its Oversight of the Firefighters' and Rescue Squad Workers' Pension Fund

Final Report to the Joint Legislative Program Evaluation Oversight Committee

Report Number 2014-03

March 19, 2014

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March 19, 2014

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Honorable Co-Chairs:

The 2013–15 Program Evaluation Division work plan directed the division to review state-administered funds related to fire, rescue, and emergency management services departments, including the eligibility criteria for these funds, benefits received, and oversight of funds. The third report in this series examines the Firefighters' and Rescue Squad Workers' Pension Fund.

I am pleased to report that the Department of State Treasurer cooperated with us fully and was at all times courteous to our evaluators during the evaluation.

Sincerely,

John W. Turcotte
Director

PROGRAM EVALUATION DIVISION
NORTH CAROLINA GENERAL ASSEMBLY

March 2014 Report No. 2014-03

Department of State Treasurer Should Strengthen Its Oversight of the Firefighters' and Rescue Squad Workers' Pension Fund

Summary

As directed by the North Carolina General Assembly's Joint Legislative Program Evaluation Oversight Committee, this evaluation examines the Firefighters' and Rescue Squad Workers' Pension Fund. The Pension Fund provides $170 per month to firefighters and rescue workers after they reach age 55 and have provided 20 years of service, during which time they are required to have paid $10 per month into the fund (for a total of $2,400). In Fiscal Year 2012–13, the State contributed $15.4 million to the fund. The Department of State Treasurer administers the Pension Fund.

The Pension Fund is adequately funded, but the State's annual required contribution now exceeds the amount of property insurance premium tax proceeds going to the General Fund. The State pays its contribution to the Pension Fund out of the General Fund. The 2013 Appropriations Act reduced the amount of insurance premium tax proceeds going to the General Fund by up to 10%. To continue to meet 100% of the State's annual required contribution, the General Assembly will have to draw more heavily on General Fund sources other than the property insurance premium tax.

Legislative inquiries, starting in 2012, revealed problems with the Department of State Treasurer's administration of the Pension Fund.

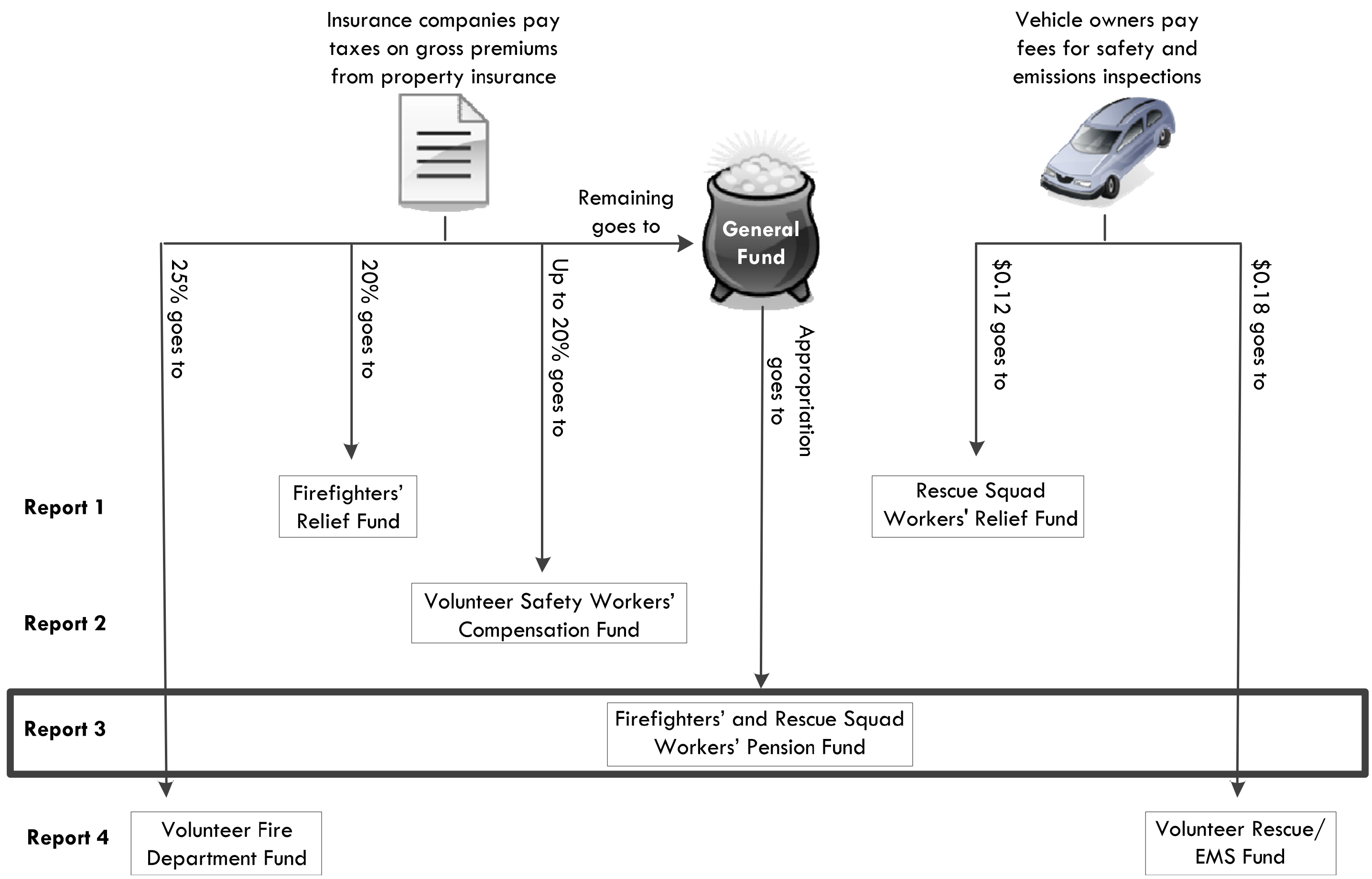
- The department's appropriation requests for the Pension Fund have been overstated due to an overly-conservative actuarial assumption that all current members, regardless of how long it has been since they made their last contribution, will contribute in the future and thus potentially qualify for benefits.
- From 2005 to 2012, the department applied $10 monthly contributions retroactively without collecting any additional costs to compensate for lost investment earnings. Failure to enforce the timely payment of member contributions has cost the Pension Fund at least $508,361.
- The department minimally enforced the prohibition against paying pension benefits to members still working as firefighters or rescue workers.

Because the Department of State Treasurer is taking steps to address these issues, the Program Evaluation Division recommends that the General Assembly require the department to report annually on its progress to the House State Personnel Committee and the Senate Pensions & Retirement and Aging Committee.

Purpose and Scope

This evaluation was directed by the Joint Legislative Program Evaluation Oversight Committee through its 2013–15 Work Plan. This report, the third of a four-part series on state-administered funds related to fire, rescue, and emergency medical services, examines the Firefighters' and Rescue Squad Workers' Pension Fund. The first report examined the Firefighters' Relief Fund and Rescue Squad Workers' Relief Fund, and the second report examined the Workers' Compensation Fund for Volunteer Safety Workers. The final report will examine grants to local volunteer fire, rescue, and EMS departments through the Volunteer Fire Department Fund and Volunteer Rescue/EMS Fund. As shown in Exhibit 1, the common thread linking the six funds is their shared funding sources. State funding for the Firefighters' and Rescue Squad Workers' Pension Fund comes from the General Fund, which receives the remainder of the taxes paid on property insurance premiums after distributions are made to the Volunteer Fire Department Fund, Firefighters' Relief Fund, and Volunteer Safety Workers' Compensation Fund.[1]

Exhibit 1: Sources of Funding for State-Administered Funds Related to Fire, Rescue, and EMS



Notes: Prior to the 2013 Appropriations Act, 30% of the premium tax went to the Volunteer Fire Department Fund, 25% went to the Firefighters' Relief Fund, and none went to the Volunteer Safety Workers' Compensation Fund.

Source: Program Evaluation Division based on N.C. Gen Stat. §§ 20-183.7(c), 58-86-20, and 105.228.5(d)(3) and N.C. Sess. Law 2013-360.

[1] The tax on gross property insurance premiums is 0.74% of 10% of the gross premiums for automobile physical damage coverage and 0.74% of 100% of the gross premiums for all other property coverage (N.C. Gen. Stat. § 105.228.5(d)(3)).

Three research questions guided this evaluation:

1. What are the eligibility criteria and benefits of the fund?
2. What is the financial status of the fund?
3. How is the fund administered, and what are the oversight mechanisms for the fund?

The Program Evaluation Division collected data from the Department of State Treasurer.

Background

In 1959, the General Assembly created the Firemen's Pension Fund to incentivize and induce participation in fire protection services by financially assisting firefighters in retirement.[2] Rescue squad workers were included in the fund beginning in 1982. To be gender-neutral, the General Assembly renamed the fund the Firefighters' and Rescue Squad Workers' Pension Fund (hereafter referred to as the Pension Fund in this report) during the 2013 Session.[3]

Paid and volunteer firefighters and rescue workers are eligible to become active members of the Pension Fund.[4] Firefighters and rescue workers may work for paid departments, volunteer departments, and/or "combination departments," meaning departments consisting of volunteer and paid personnel. Firefighters and rescue workers may be paid personnel at one department and volunteer at another. In addition to being eligible for the Pension Fund, many paid personnel in paid departments are eligible for retirement benefits from the Local Governmental Employees' Retirement System (LGERS).[5]

Eligibility for Pension Membership. To be eligible members of the Pension Fund, firefighters and rescue workers must

- be 18 years old or older and
- attend 36 hours of training sessions each year.

In addition, a firefighter must be affiliated with a fire department that

- is certified to the Commissioner of Insurance by its governing body;
- is rated by the Department of Insurance as not less than a class "9S" department;[6]
- holds training sessions not less than four hours monthly; and
- provides its governing body with a list of firefighters who completed the above training requirements.[7]

[2] N.C. Gen. Stat. Chp. 58, Art. 86. The Pension Fund was originally created in 1957 and was funded from taxes that insurance companies paid on their premiums from fire and lightning insurance (N.C. Sess. Laws, 1957-1420). However, the Supreme Court of North Carolina declared the Pension Fund unconstitutional because of this funding method (American Equitable Assurance Company of New York v. Gold, 249 N.C. 461). The Pension Fund was created again in 1959 with funds appropriated from the General Fund (N.C. Sess. Laws, 1959-1212).
[3] N.C. Sess. Law 2013-284.
[4] Pursuant to N.C. Gen. Stat. § 58-86-2, the number of eligible volunteers from a fire department cannot exceed 25 volunteer firefighters plus one additional volunteer firefighter per 100 population in the area served by their respective departments.
[5] Local governments choose whether or not to participate in LGERS. The Charlotte Fire Department, for example, does not participate in LGERS and instead has its own pension plan.
[6] Department ratings are based on the North Carolina Response Rating System, which has three components: 1) receiving and handling of fire alarm calls, 2) equipment, operations, and training, and 3) water supply.
[7] The fire department's governing body must certify the list to the North Carolina State Firemen's Association, which must provide the list to the State Treasurer by January 31 of each year.

A rescue squad worker must be affiliated with a rescue or emergency medical services squad that

- is eligible for membership in the North Carolina Association of Rescue and Emergency Medical Services, Inc. (NCAREMS) and
- files a list of rescue squad workers who completed the above training requirement to NCAREMS.[8]

An "eligible firefighter" cannot also qualify as an "eligible rescue squad worker," or vice versa, in order to receive double benefits.

To receive credit for their eligible service time, members must contribute $10 per month to the Pension Fund.[9] Some departments opt to make contributions on behalf of their members.

North Carolina has approximately 50,000 firefighters and 33,000 rescue workers. As shown in Exhibit 2, 37,518 firefighters were active members of the Pension Fund as of July 1, 2012, and there were 10,524 retired members. At the same time, 3,352 rescue squad workers were active members of the Pension Fund and there were 1,114 retired members.

Exhibit 2

Pension Fund Membership as of July 1, 2012

	Firefighters	Rescue Squad Workers
Active Members		
Volunteers	15,413	167
Paid personnel	19,901	2,856
Not classified	2,204	329
Subtotal	37,518	3,352
Retired Members	10,524	1,114
Total	48,042	4,466

Source: Program Evaluation Division based on data from the Department of State Treasurer.

Retirement Benefits. Presently, retired members of the Pension Fund receive $170 per month. To receive benefits from the Pension Fund, members must

- be age 55 or older and[10]
- have amassed 20 years of service during which they paid $10 per month into the fund (for a total of $2,400).

The Pension Fund also provides disability benefits. Members who become totally and permanently disabled while performing their duty qualify to receive the monthly benefit after turning age 55 without any further contributions to the fund. After 10 years of service, members who become totally and permanently disabled while performing non-duty-related activities qualify to receive the monthly benefit after turning age 55 if they

[8] NCAREMS must certify the list to the State Treasurer by January 31 of each year.
[9] N.C. Sess. Law 1995-507 increased members' monthly contributions from $5 to $10.
[10] For public safety workers, the Internal Revenue Service considers age 50 or older a normal retirement age, or an age that is not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed.

pay $10 per month into the fund until they have made 20 years' worth of contributions.

Funding sources. The Pension Fund is funded by investment income, state contributions, and member contributions. As a defined benefit plan, the Pension Fund provides retired firefighters and rescue workers with income for the remainder of their lives. Defined benefit plans collect contributions during a member's active service so that when the member retires, those contributions along with investment income will be sufficient to pay for the entire cost of the member's retirement benefits. The basic equation for funding the system is

Investment Income + Member Contributions + State Contributions = Current and Future Pension Benefits + Plan Administration Expenses

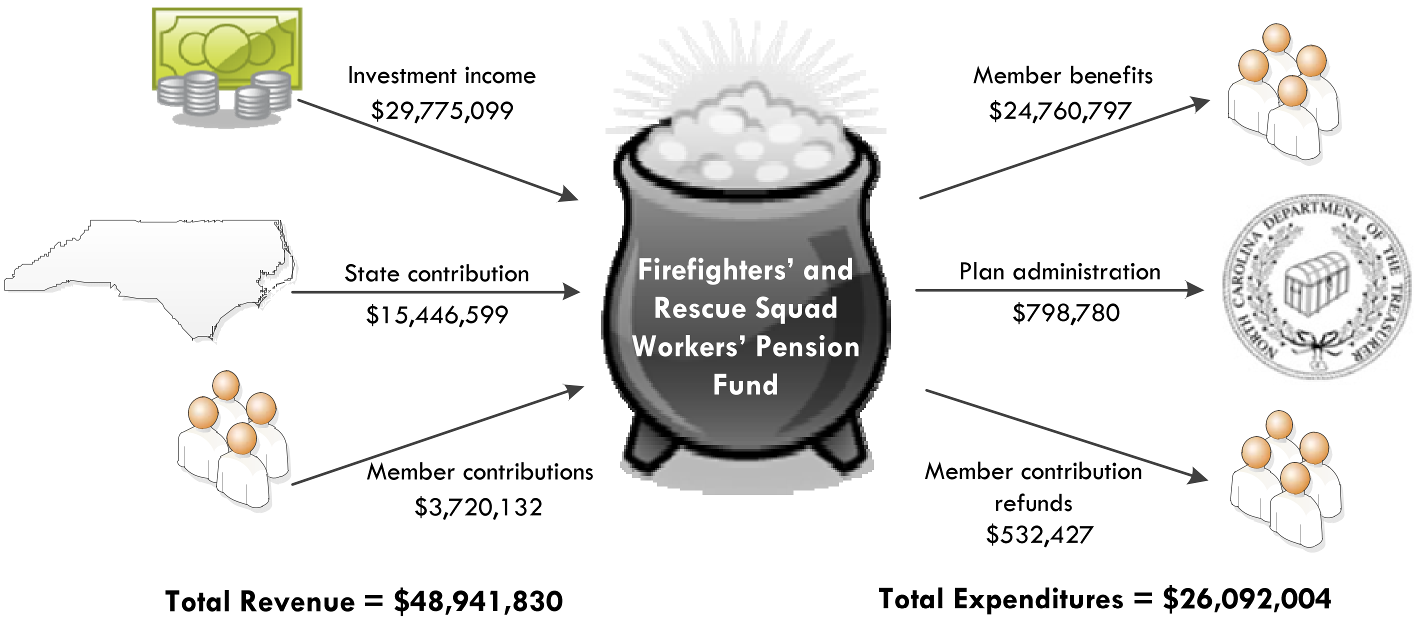
The Pension Fund must ensure that the benefits it pays out plus the cost of administering the system equals the contributions it takes in plus the returns it makes on its investments. Exhibit 3 shows the amounts for each equation variable for the Pension Fund in Fiscal Year 2012–13.

- **Income from investments.** The largest contributor to the Pension Fund was the income generated by the fund's investments, which totaled $29.8 million.
- **Income from state contribution.** The State contributed $15.4 million to the Pension Fund.
- **Income from member contributions.** Members' $10 monthly contributions, along with members' contributions to purchase credit for prior service, amounted to $3.7 million.
- **Cost of member benefits.** The Pension Fund paid out $24.8 million in retirement and disability benefits.
- **Cost of plan administration.** It cost $798,780 to administer the Pension Fund.
- **Cost of member contribution refunds.** The Pension Fund refunded $532,427 to members who withdrew their membership and to survivors of members who died.

In total, the Pension Fund received $48.9 million and spent $26.1 million in Fiscal Year 2012–13.

As shown in Exhibit 4, investment income drives the financial position of the Pension Fund. The amount of investment income the fund generates is influenced by the state of the economy, as shown by investment losses in 2008 and 2009, when most pension plans across the country experienced losses due to the economic downturn. As of September 30, 2013, the five-year rate of return for the fund was 7.8%, compared to a 7.6% five-year rate of return for benchmarked funds.

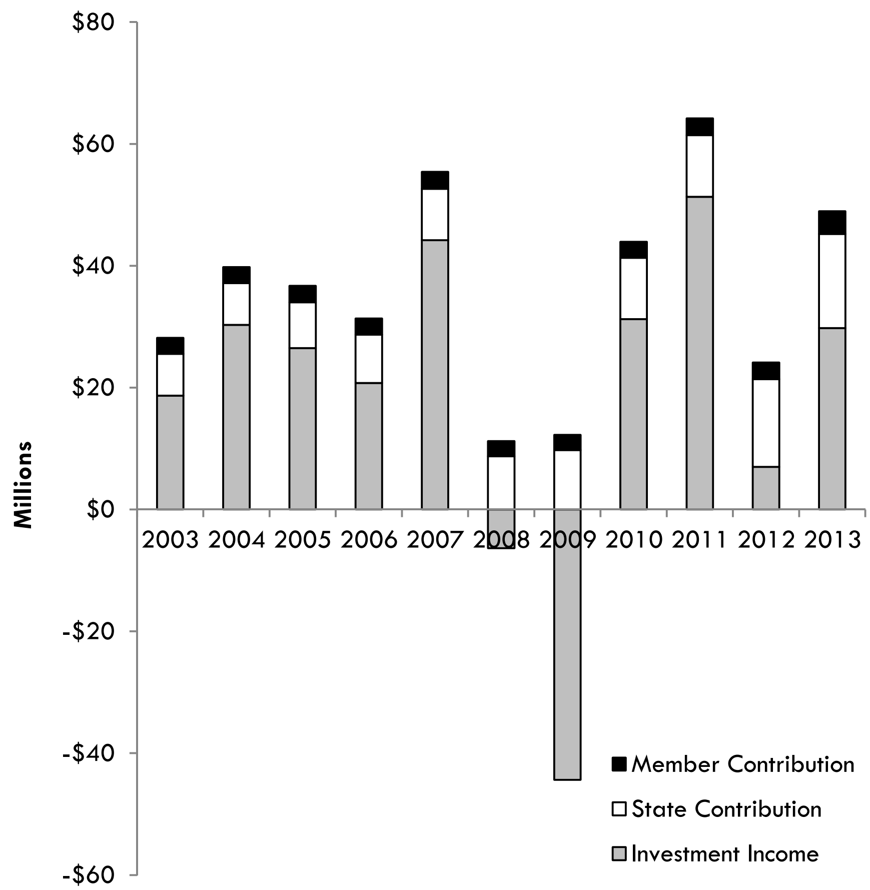
Exhibit 3: Pension Fund Revenues and Expenditures, Fiscal Year 2012–13



Source: Program Evaluation Division based on data from the North Carolina Accounting System.

Exhibit 4

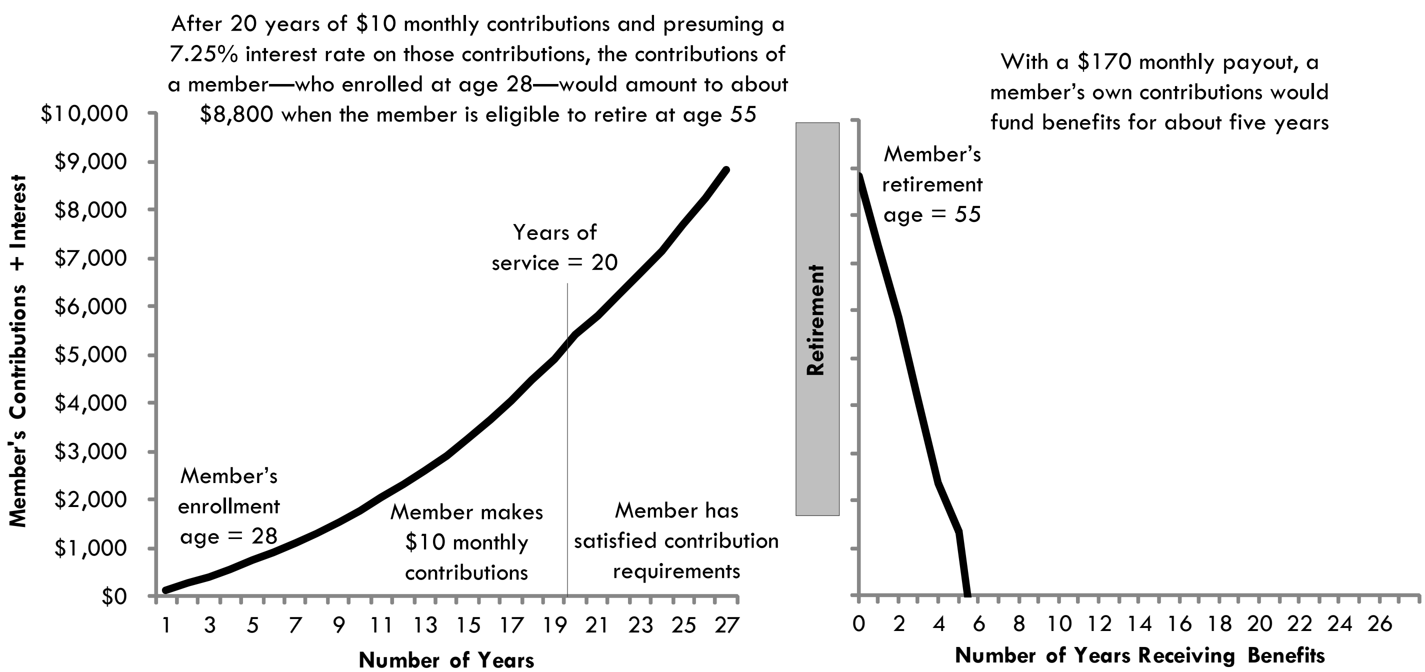
Investment Income Drives the Financial Position of the Pension Fund, Fiscal Years 2002–03 to 2012–13



Source: Program Evaluation Division based on data from the North Carolina Accounting System.

Exhibit 5 provides an example of how long it takes a member to recoup the member's investment in the Pension Fund. Presuming a 7.25% interest rate, a member who consistently makes $10 monthly contributions will contribute about $5,400 to the fund over 20 years. In the example, the member starts making contributions at age 28—the Pension Fund's average enrollment age—and these contributions are valued at about $8,800 when the member is eligible to retire at age 55. If this member retires at age 55, the member will receive that $8,800 in about 62 months, based on a $170 monthly benefit.[11] This recoupment period for the Pension Fund is similar to the recoupment period for the Local Governmental Employees' Retirement System (LGERS) and Teachers' and State Employees' Retirement System (TSERS).[12] The Pension Fund is able to afford this recoupment period because the member contribution only accounts for approximately half of the contribution to pay for benefits accrued in the current year and the fund retains investment income earned on contributions made by members who never vest.[13]

Exhibit 5: Example Recoupment Period for A Member's Contributions



Note: The assumed rate of return used in the Pension Fund annual valuations is 7.25%. The average age of enrollment in the Pension Fund is 28.

Source: Program Evaluation Division.

[11] The recoupment period can vary from 3 years to more than 15 years depending on the age the member first contributes to the plan, whether the member earns service in consecutive years, and the age when the member decides to retire.

[12] Alternatively, one could compare the portion of the annual normal cost borne by members versus the State. The annual normal cost is the portion of the present value of benefits (the total cost of benefits accrued throughout a member's service, including benefits projected to be earned in the future, expressed in today's dollars) that actuaries allocate to each year of service both past and future. In Fiscal Year 2011–12, the State bore 56% of the annual normal cost for the Pension Fund and 46% of the annual normal cost for TSERS.

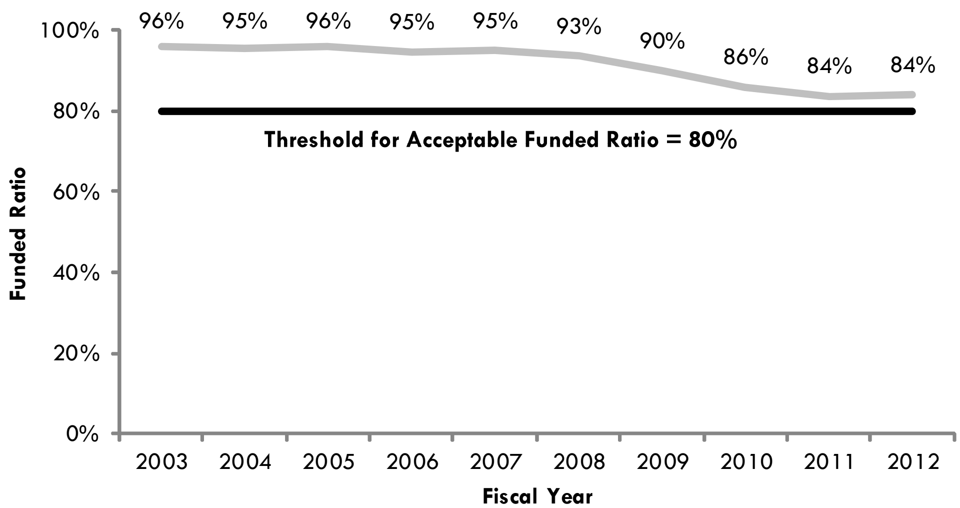
[13] Pursuant to N.C. Gen. Stat. § 58-86-60, members who are no longer eligible or choose not to participate in the Pension Fund for any reason can receive a refund of their contributions after reaching age 55, but the refund does not include any interest that was generated from their contributions.

Financial status. The most commonly used indicator of a retirement plan's fiscal health is the percentage of a plan that is funded, or the ratio between the value of the plan's assets and its accrued liability. Strong performance on this measure indicates the extent to which a plan has sufficient funds set aside to pay for accrued benefits. Although a funded ratio of 80% or more is generally viewed as acceptable to support future pension costs,[14] the target is a 100% funded ratio.

In Fiscal Year 2011–12, the Pension Fund's funded ratio was 84%; the actuarial value of its assets was $338.9 million and its accrued liability was $403.8 million. As shown in Exhibit 6, the funded ratio has been on a downward trend for the last 10 years, but it still remains above the 80% threshold. The funded ratio has decreased recently because monthly retirement benefits were incrementally increased from $100 to $170 between 1994 and 2008 and because investment returns decreased between 2007 and 2009.

Exhibit 6

Pension Fund's Funded Ratio Has Declined But Remains Above 80% Threshold, Fiscal Years 2002–03 to 2011–12



Source: Program Evaluation Division based on data from Pension Fund actuarial valuations.

Fund administration. Prior to the 2013 Session, the Pension Fund was administered by its own board of trustees. However, legislation eliminated the board, transferred administrative responsibility to the Board of Trustees of the Local Governmental Employees' Retirement System (LGERS), and added an active or retired member of the fund to the LGERS board.

The General Assembly also created the Firefighters' and Rescue Squad Workers' Pension Fund Advisory Panel and charged it with making an annual report to the LGERS board regarding the status and needs of the Pension Fund.[15]

Two divisions in the Department of State Treasurer handle the day-to-day operations of the Pension Fund.

[14] U.S. Government Accountability Office. (2007, September). *State and local government retiree benefits: Current status of benefit structures, protections, and fiscal outlook for funding future costs.* Report to the U.S. Senate Committee on Finance.

[15] The advisory panel consists of seven individuals: the director of the Department of State Treasurer's Retirement Systems Division or the director's designee; a designee of the State Insurance Commissioner; and five members appointed by the LGERS board including one paid firefighter, one volunteer firefighter, one paid rescue worker, one volunteer rescue worker, and one person representing the public at large.

- The Investment Management Division manages the Pension Fund's investment portfolio. Its goal is to maintain the long-term strength of North Carolina's public pension plans by providing a consistent long-term rate of return while simultaneously minimizing risk.
- The Retirement Systems Division provides day-to-day administration of the Pension Fund, including processing applications for retirement, maintaining retirement accounts and data, and providing customer service to active and retired employees. Within the division, the equivalent of 6.7 full-time positions are dedicated to the Pension Fund.

Legislative inquiries, starting in 2012, revealed problems with the Retirement System Division's day-to-day administration of the Pension Fund. As a result, the General Assembly made technical and substantive changes to the Pension Fund during this past session. In addition, the Joint Legislative Program Evaluation Oversight Committee directed the Program Evaluation Division to describe and quantify these administrative problems and to determine whether necessary steps are being taken to ensure the long-term sustainability of the Pension Fund.

Findings

Finding 1. The State's annual required contribution now exceeds the amount of insurance premium tax proceeds going to the General Fund.

The annual required contribution, or ARC, is the amount of money that an actuary calculates the State needs to contribute to a retirement plan during the current year for benefits to be fully funded in the future. Despite the use of the word "required," the State can choose to pay more or less than this amount. The General Assembly determines how much of the ARC it is going to meet as part of the budget process. When a government consistently pays the ARC, the benefits accrued by Pension Fund members are paid for by the taxpayers who receive services from those firefighters and rescue workers. When the ARC is not paid in full each year, a portion of the costs of pension benefits accrued that year will fall to future taxpayers. The closer the percentage of the ARC paid is to 100%, the closer the state contribution is to meeting the plan's obligations.

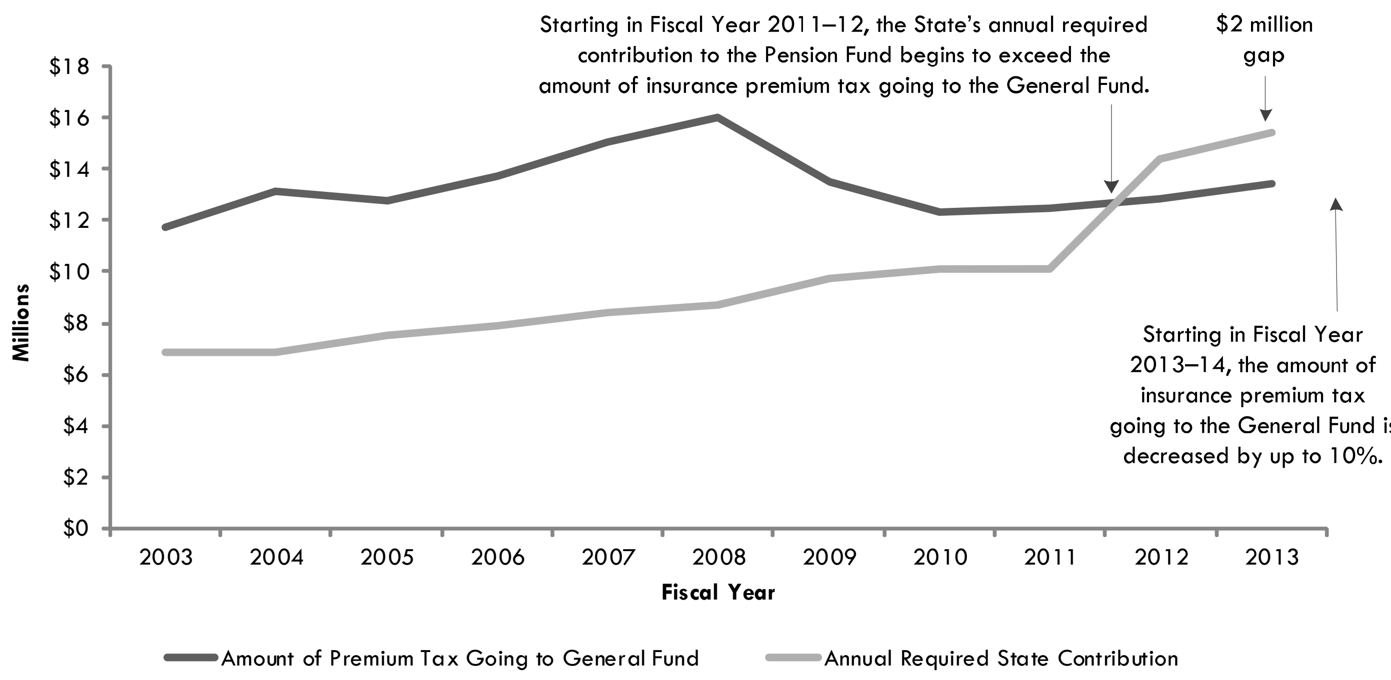
The General Assembly has consistently paid 100% of the State's annual required contribution for the Pension Fund. The General Assembly has met 100% of the ARC every year except Fiscal Year 2010–11, when it paid 83% of the ARC. For Fiscal Year 2011–12, the actuary calculated the ARC as $15.9 million, and the General Assembly appropriated $14.4 million. Although the state contribution was less than the ARC calculated by the actuary, the General Assembly met the ARC by extending the amortization period.[16] In Fiscal Year 2012–13, the ARC was $14.1 million, but because the General Assembly had already budgeted contributing $15.4 million to the fund, it funded the ARC at 110%.

[16] The amortization period is the span of time the plan has to fully pay its unfunded actuarial accrued liabilities. Session Law 2011-145 extended the amortization period from 9 to 12 years. This 12-year amortization period is still shorter than the average amortization period of 26.5 years for statewide pension plans.

The State's annual required contribution for the Pension Fund is now exceeding the amount of insurance premium tax proceeds going to the General Fund. The State pays its contribution to the Pension Fund from the General Fund. As discussed previously, the General Fund receives the remainder of the taxes paid by insurance companies on the gross premiums they collect on property insurance after distributions are made to the Volunteer Fire Department Fund, Firefighters' Relief Fund, and Volunteer Safety Workers' Compensation Fund. Whereas premium tax proceeds are earmarked for these other funds, they are not earmarked for the Pension Fund.

As shown in Exhibit 7, the ARC first exceeded the amount of insurance premium tax going to the General Fund in Fiscal Year 2011–12. The gap between the ARC and the available premium tax was $2 million in Fiscal Year 2012–13. This gap will continue to increase because the 2013 Appropriations Act decreased the premium tax proceeds available for the General Fund by up to 10%, down from 45% to as little as 35%.[17] To continue to meet 100% of the ARC in the future, the General Assembly may have to draw more heavily on General Fund sources other than the property insurance premium tax.

Exhibit 7: State's Annual Required Contribution Exceeded Premium Tax Proceeds by $2 Million in Fiscal Year 2012–13



Note: The drop in premium tax proceeds in Fiscal Year 2008–09 coincided with a change from a 1.33% tax on fire and lightning insurance premiums to a 0.74% tax on property insurance premiums (N.C. Sess. Law 2006-196).

Source: Program Evaluation Division based on data from the Department of Revenue and Pension Fund actuarial valuations.

[17] Prior to the 2013 Appropriations Act, 30% of the premium tax went to the Volunteer Fire Department Fund, 25% went to the Firefighters' Relief Fund, and none went to the Volunteer Safety Workers' Compensation Fund. The 2013 Appropriations Act designated that up to 20% of the premium tax goes to the Volunteer Safety Workers' Compensation Fund and reduced the amount available for the Volunteer Fire Department Fund to 25% and the amount available for the Firefighters' Relief Fund to 20%.

Finding 2. The Department of State Treasurer's failure to question overly conservative actuarial assumptions regarding the Pension Fund has resulted in the department overstating appropriation requests.

Each biennium, the Department of State Treasurer requests that the General Assembly appropriate the State's annual required contribution, or ARC, to the Pension Fund. The ARC is the amount of money that an actuary calculates the State needs to contribute to the Pension Fund during the current year for benefits to be fully funded in the future. Since the Pension Fund was transferred from the Office of the State Auditor to the Department of State Treasurer in 1992, the Pension Fund's Board of Trustees has contracted with the actuarial firm Buck Consultants to calculate the ARC. If the actuarial calculations are accurate, the state contribution each year, when combined with member contributions and investment income, should fully prefund the benefits that active members are expected to earn upon retirement.

The Pension Fund actuary's projections have overstated the ARC because of overly conservative assumptions. In order for firefighters and rescue workers to receive Pension Fund benefits, they have to "vest" in the system, meaning they need to have served for 20 years and paid $10 per month during this period. In determining the ARC, an actuary factors in a lapse assumption, or the likelihood that some number of current members have stopped serving and thus will not make the member contributions necessary to vest. Buck Consultants has based the ARC on the overly conservative assumption that all current members, regardless of how long it has been since they made their last contribution, will contribute in the future and thus potentially receive benefits.[18] Realistically, some number of members who join the fund will not meet the requirements of the 20-year vesting period and therefore will not receive benefits.

The Department of State Treasurer needed to study the vesting behavior of the Pension Fund population to determine an accurate actuarial assumption. The actuary assumed that of non-vested Pension Fund members who did not make contributions in the last year, 0% will fail to make any contributions in the future.[19] In comparison, the same actuary assumed 100% of non-vested members in the Local Governmental Employees' Retirement System (LGERS) and Teachers' and State Employees' Retirement System (TSERS) who did not make contributions in the last year will fail to make any contributions in the future. Because the Pension Fund population is more transient than the TSERS and LGERS populations,[20] a 100% lapse assumption may not be appropriate for the

[18] For example, the actuary's annual valuations assume a non-vested member who has not made any contributions in the last 10 years will immediately resume making contributions.

[19] Whereas a lapse assumption considers some number of current members stopped serving in the past and therefore will never resume making contributions, a withdrawal assumption considers some number of current members will stop serving in the future and therefore will quit making contributions (and request a refund of their contributions). The actuary did incorporate a withdrawal assumption into the Pension Fund valuations. The actuary's calculations assume the following annual withdrawal rates: 3% of firefighters with less than five years of service, 1.5% of firefighters with five or more years of service, 5% of rescue squad workers with less than five years of service, and 2% of rescue workers with five or more years of service.

[20] According to the Department of State Treasurer, TSERS and LGERS members generally accrue a year of service each year, whereas many Pension Fund members do not. TSERS and LGERS members generally notify their employers when they terminate employment and the Department of State Treasurer stops accruing a year of service for them, whereas many Pension Fund members do not notify their affiliated fire and rescue departments and may return after years of absence.

Pension Fund. In the face of uncertainty, actuaries are trained to be conservative. However, by presuming a 0% lapse assumption, the actuary was likely inflating the Pension Fund's future liabilities and, consequently, its ARC.

The Department of State Treasurer, as the administrator of the Pension Fund, should have questioned the actuary's 0% lapse assumption. Because the Firefighters' and Rescue Squad Workers' Pension Fund is small compared to the other pension funds the Department of State Treasurer administers, the department admits the fund has not been a top priority. If the Department of State Treasurer had been more active in overseeing the Pension Fund, the department would have realized it needed a more precise understanding of Pension Fund vesting behavior to substantiate its appropriation requests to the General Assembly.

Due to the Department of State Treasurer's overstated appropriation requests to the General Assembly, the State has been contributing more than necessary to prefund the benefits active members are expected to earn upon retirement. Because appropriations to the Pension Fund come from the General Fund, excess contributions to the Pension Fund mean that the General Assembly could not use those resources for other state-funded programs.

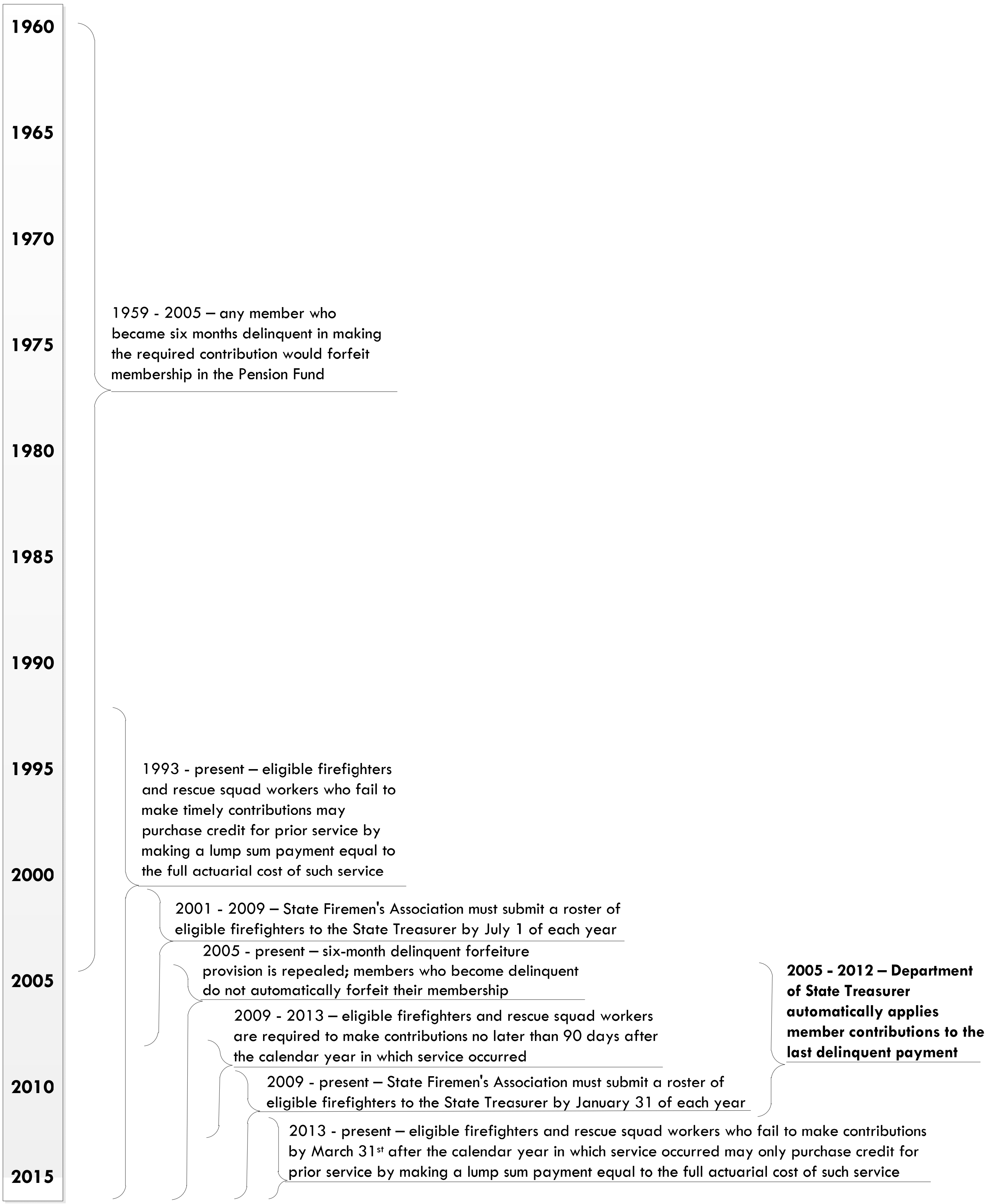
Finding 3. The Department of State Treasurer's failure to enforce the timely payment of member contributions has cost the Pension Fund at least $508,361.

The Department of State Treasurer's interpretation of statute from 2005 to 2012 resulted in members' $10 monthly contributions being applied retroactively without collecting any additional costs to compensate for lost investment earnings. As shown in Exhibit 9, the original statutes in 1959 governing the Pension Fund did not mandate that members' monthly contributions be made within any specific timeframe but provided for forfeiture of membership for any member who became six months delinquent, with no statutory definition of delinquent provided. The General Assembly enacted a provision in 1993 that allowed members who failed to make timely contributions to purchase credit for prior service by making a lump sum payment equal to the full actuarial cost of such service. In 2005, the mandatory forfeiture provision was repealed, and still no statutory timeframe for making member contributions existed.

From 2005 to 2009, when the Department of State Treasurer received payments from existing members,[21] it allowed contributions for all prior months. When the Pension Fund was added to the Online Retirement Benefits through Integrated Technology (ORBIT) system in 2008, the system automatically applied member contributions to the last delinquent payment. The department's explanation was the statutes governing the fund did not include any deadline for accepting payments.

[21] For new members, the department charged any additional fees due under then-existing N.C. Gen. Stat. §§ 58-86-45(a) and 58-86-45(b).

Exhibit 9: Timeline of State Laws Regarding the Pension Fund, 1959–2013



Source: Program Evaluation Division based on North Carolina General Statutes and Session Laws.

In 2009, the General Assembly enacted a statutory deadline for making payments. Members were required to make contributions no later than 90 days after the calendar year in which service occurred, with no statutory language included regarding the repercussions of untimely payments. From 2009 to 2012, the Department of State Treasurer continued allowing contributions from existing members for all prior months.[22] The department's explanation was the statutes were unclear as to what action the department should take when it received a payment more than 90 days subsequent to the end of the immediately preceding calendar year from an existing member with unpaid service from a previous calendar year.

Failure to collect timely member contributions from Fiscal Years 2005–06 to 2011–12 cost the Pension Fund at least $508,361 in lost investment earnings. As shown in Exhibit 10, the Pension Fund has a funding gap due to investment earnings that would have been generated by delinquent member contributions if they had been paid on time. The Program Evaluation Division based this estimate on several assumptions:

- the number of active members was accurate;
- all active members, except those who had accrued at least 20 years of service and thus fulfilled their contribution requirement,[23] needed to pay contributions;[24]
- all member contributions were due by July 1 for service rendered during the previous fiscal year;[25]
- missing contributions would have earned the same rate of return as other investments;
- 50% of members who were delinquent with contributions later paid those contributions in a lump sum, without paying interest or the actuarial value of their service time, at the earlier of four years after their contributions were due or December 31, 2012[26].

[22] For new members aged 35 and older, the department charged the actuarial cost of prior service in accordance with N.C. Gen. Stat. § 58-86-45(a1). For new members under age 35, the department charged $10 retroactively to the time the individual first became eligible plus interest at an annual rate set by the board for each year, in accordance with N.C. Gen. § 58-86-45(b).

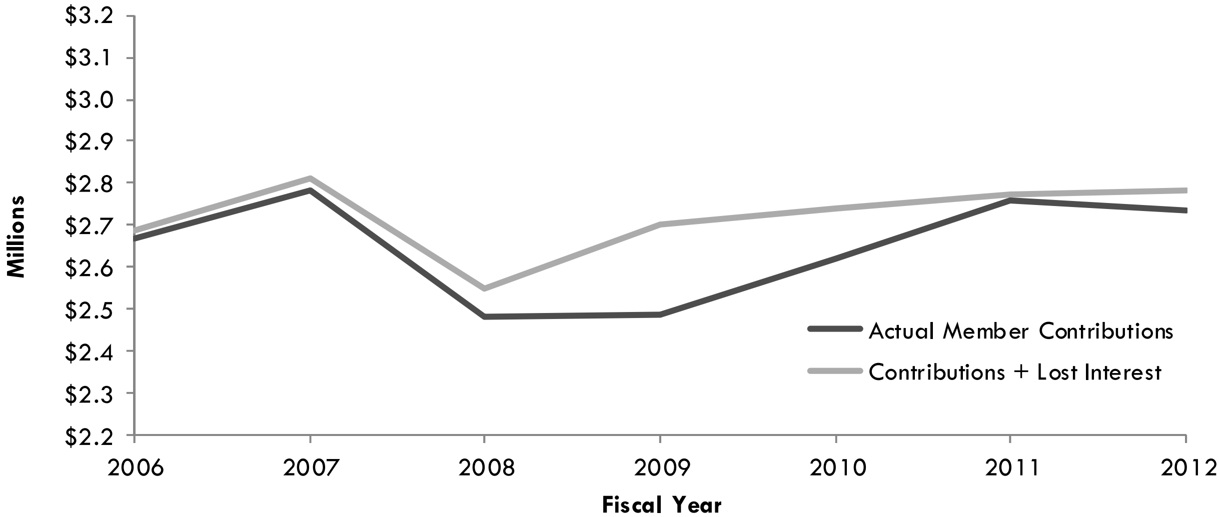
[23] The number of total active members each year was reduced by 13%, which was the average number of active members from Fiscal Years 2005–06 to 2011–12 with at least 20 years of service.

[24] Although some active members pay for their service in advance pursuant to 20 N.C. Admin. Code 02N .0213, these payments are unrelated to the payments the Department of State Treasurer applied retroactively without collecting any additional costs to compensate for lost investment earnings.

[25] Because monthly data was not available, the Program Evaluation Division's analysis was limited to fiscal year timeframes. Although there was no statutory deadline for making member contributions from Fiscal Years 2005–06 to 2008–09, rosters for eligible firefighters were due by July 1 of the year after the calendar year in which service was rendered and rosters for eligible rescue workers were due by January 1 of the year after the calendar year in which service was rendered. From Fiscal Years 2008–09 to 2011–12, firefighters and rescue workers were required to make contributions no later than 90 days after the calendar year in which service was rendered.

[26] In the absence of data to guide this assumption, the Program Evaluation Division had to assume some amount of members who were delinquent with contributions later resumed contributing to the Pension Fund. Although the fund received the entire amount of principal payments, interest income was lost for years in which the member was delinquent with payments. Because the 50% assumption is arbitrary, the Program Evaluation Division did a sensitivity analysis. If just 1% of delinquent members resumed contributing to the Pension Fund, the lost interest would amount to $10,167. If 100% of delinquent members resumed contributing to the Pension Fund, the lost interest would amount to $1,016,722.

Exhibit 10: Pension Fund Has a $508,361 Funding Gap Due to Inadequate Member Contributions



Note: During the time period from Fiscal Years 2005–06 to 2008–09 when there was no statutory deadline for making member contributions, failure to collect timely member contributions cost the Pension Fund $323,179 in lost investment earnings. During the time period from Fiscal Years 2008–09 to 2011–12 when members were required to make contributions no later than 90 days after the calendar year in which service occurred, failure to collect timely member contributions cost the Pension Fund $185,182 in lost investment earnings. Lost Interest was based on actual interest rates from Fiscal Year 2006–07 to December 31, 2012.

Source: Program Evaluation Division based on data from the North Carolina Accounting System and Pension Fund actuarial valuations.

Legislation enacted this past session ensures timely collection of member contributions as long as the Department of State Treasurer correctly administers the provision. Legislators began making inquiries into Pension Fund administrative activities in early 2012. As of May 2012, of the 1,347 departments participating in the Pension Fund

- 70 had unpaid contributions dating back to 2009,
- 28 had unpaid contributions dating back to 2010, and
- 466 had unpaid contributions dating back to 2011.

As a result of legislative inquiries, the Department of the State Treasurer sought the advice of the Attorney General regarding member contributions and service credit. In November 2012, the Special Deputy Attorney General responded through a memorandum with the following unofficial opinions:

- Legislation enacted throughout the history of the Pension Fund indicates a legislative intent to limit the extent to which members can obtain prior service credits at less than actuarial costs, or the full liability the additional service puts upon the fund.
- Pursuant to Session Law 2009-66, the Department of State Treasurer cannot award service credit when monthly contributions are made 90 days after the end of the calendar year in which the month occurred.
- Pursuant to Session Law 1993-429, the Department of State Treasurer can only accept payment from current members for prior service if they pay the actuarial cost of that service time.

This past legislative session, the General Assembly passed Session Law 2013-284, which clarified that members who fail to make contributions by March 31 after the calendar year in which service occurred may only purchase credit for prior service by making a lump sum payment equal to the full actuarial cost of such service. This legislation addresses the problem of the Department of State Treasurer's misinterpretation of statute as long as the department correctly administers the provision.

Finding 4. The Department of State Treasurer minimally enforced the prohibition against paying pension benefits to members still working as firefighters or rescue workers.

The purpose of the Pension Fund is to financially assist volunteer and paid firefighters and rescue workers in retirement. N.C. Gen. Stat. § 58-86-55 specifies no Pension Fund member is entitled to benefits until the member has retired from performing any official duties as a paid firefighter or rescue worker. In other words, the Pension Fund statutes prohibit in-service distributions.[27]

The Department of State Treasurer has minimally enforced the prohibition against in-service distributions. As shown in Exhibit 11, there are four mechanisms the department could use to enforce the prohibition against in-service distributions. The Department of State Treasurer was only using the first mechanism. The application for Pension Fund benefits requires paid firefighters and rescue workers to report the date their paid position was terminated, certify with their signatures that they have retired from their paid position, and have the form notarized. After the form is notarized, employers fill out a section in which they certify with their signature that the member retired from paid employment and provide the retirement date. According to the Department of State Treasurer, stricter enforcement of the prohibition against in-service distributions would create an administrative burden for the department.

[27] The Internal Revenue Service defines in-service distributions as the occurrence of a pension plan permitting payment of benefits upon an employee's attainment of normal retirement age, even if the employee has not yet had a severance from employment with the employer maintaining the plan.

Exhibit 11

Department of State Treasurer Was Only Using One of Four Possible Mechanisms to Enforce the Prohibition Against In-Service Distributions

Mechanisms for Enforcing Prohibition Against In-Service Distribution	Implementation Status until 2013
1. Have members applying for retirement benefits and their department chiefs attest that members are not still working	●
2. Regularly compare Pension Fund retiree data to LGERS active data to verify Pension Fund retirees are not being paid as firefighters or rescue workers by a local government participating in LGERS	○
3. Regularly compare Pension Fund retiree data to NCSFA and NCAREMS data to verify Pension Fund retirees are not listed as active members on department rosters	○
4. Regularly compare Pension Fund retiree data to the Department of Revenue's tax records to verify fire departments are not reporting Pension Fund retirees on their W-2s as active employees	○

● = Fully implemented ○ = Not implemented

Notes: LGERS stands for the Local Governmental Employees' Retirement System. NCSFA stands for the North Carolina State Firemen's Association. NCAREMS stands for the North Carolina Association of Rescue and EMS, Inc. The fourth mechanism would require the Department of State Treasurer to request statutory changes that would give it access to the Department of Revenue's tax records.

Source: Program Evaluation Division based on data from the Department of State Treasurer.

To assess the potential impact of the second enforcement mechanism, the Program Evaluation Division compared individuals who were receiving Pension Fund benefits as of July 1, 2012, to individuals who were listed as active paid firefighters and rescue workers in the Local Governmental Employees' Retirement System (LGERS) as of December 31, 2012.[28] This comparison revealed 53 Pension Fund retirees who were listed in LGERS as paid firefighters or rescue workers.

The Department of State Treasurer examined the work history of these 53 individuals and determined one individual appears to have been receiving pension benefits in violation of the prohibition against in-service distributions.[29] The department made the following determinations regarding the other 52 individuals:

- The department determined 48 were retired in accordance with 20 N.C. Admin. Code 02N .0218, which allows members whose 20 years of service were rendered exclusively through volunteer service to receive pension benefits regardless of their employment as paid firefighters or rescue workers.[30] During the course of this evaluation, the department requested an informal advisory opinion from the Attorney General's Office to determine if 20 N.C. Admin.

[28] Because LGERS does not include volunteer departments or departments in local governments that have chosen not to participate in LGERS (e.g., the Charlotte Fire Department), this comparison does not capture paid employees at these departments.
[29] The department is conducting further investigation on this individual to determine whether the member should have been allowed to receive Pension Fund benefits.
[30] Because department rosters do not indicate whether firefighters or rescue workers earn their service time as paid or volunteer personnel, the Department of State Treasurer had to make assumptions about the individuals' work histories based on the types of departments they served (i.e., volunteer departments, paid departments, and combination departments).

Code 02N .0218 conflicts with the statute prohibiting in-service distributions.

- The department determined two of the individuals met separation of service requirements. Because N.C. Gen. Stat. § 58-86-55 does not contain a return-to-work prohibition, the department applies the LGERS one-month separation of service requirement.[31]
- One individual earned 20 years of service as a rescue worker, and the department determined this individual's paid position as a firefighter does not violate the prohibition against in-service distributions.
- Finally, one individual was erroneously reported as a paid firefighter in LGERS, and the record was corrected to clarify that he was not reemployed as a firefighter.

The Department of State Treasurer requested an agency bill that would have allowed in-service distributions. During the 2013 Session, the Department of State Treasurer asked for the introduction of an agency bill including a provision that removed the prohibition against in-service distributions.

According to the Department of State Treasurer, the prohibition against in-service distribution builds inequity into the Pension Fund. The Pension Fund covers both paid personnel and volunteers. Whereas these two groups are equal in terms of their members having served the same amount of time and having contributed the same amount of money, the prohibition against in-service distributions affects the groups differently. Paid personnel who have not retired at age 55 are not permitted to draw the $170 monthly benefit, whereas volunteers are permitted to draw the $170 monthly benefit at age 55 regardless of whether they have retired from paid employment in another occupation. Because the Pension Fund is a defined benefit plan, meaning it provides retirement income for the remainder of members' lives, the prohibition against in-service distributions makes the Pension Fund more valuable to volunteers than paid personnel.

Legislation enacted this past session confirmed prohibition of in-service distributions. The General Assembly debated the Department of State Treasurer's proposed legislation. Buck Consultants, the Pension Fund's actuary, estimated the fiscal impact of removing the prohibition against in-service distributions would be $1.4 million for Fiscal Year 2013–14. This estimate assumed, if the prohibition was removed, 100% of members (as opposed to 75% of paid members and 100% of volunteer members) would take their distributions immediately upon retirement eligibility at age 55. The final version of the bill, which was enacted as Session Law 2013-284, retained the prohibition against in-service distributions.

[31] N.C. Gen. Stat. § 128-21(19).

Finding 5. The Department of State Treasurer is taking action to resolve the administrative issues identified in this report.

As a result of legislative inquiries and advice from the Attorney General's Office, the Department of State Treasurer has been working this past year to resolve issues with the Pension Fund.

To ensure the State's annual required contribution is appropriate, the Department of State Treasurer is assessing the condition of member data and developing lapse assumptions. As discussed in Finding 2, the annual required contribution, or ARC, is the amount of money that an actuary calculates the State needs to contribute to the Pension Fund during the current year for benefits to be fully funded in the long run. Until now, the ARC has been overstated due to the overly conservative lapse assumption that all current members, regardless of how long it has been since they made their last contribution, will contribute in the future and thus potentially qualify for benefits.

In October 2013, the Department of State Treasurer contracted the Pension Fund actuary, Buck Consultants, to examine member data to develop a more probable lapse assumption. Buck Consultants presented the preliminary results of its analysis to the Board of Trustees in January 2014. Buck Consultants found a third of active members (13,500 of 40,000) in Fiscal Year 2011–12 did not pay their member contributions that year and thus did not earn a year of service credit. By examining the work history of 1,000 of these individuals, Buck Consultants determined a lapse assumption around 20% would be sufficient and accurate. If the Department of State Treasurer has sufficient resources,[32] it will pay Buck Consultants to investigate the work history of all 13,500 lapsed members to refine the lapse assumption.[33]

As shown in Exhibit 12, building in the preliminary 20% lapse assumption could reduce the State's annual required contribution for Fiscal Year 2014–15 by $2.2 million.[34] Because the General Assembly's recommended continuation budget of $14.6 million would have been insufficient to cover the actuary's ARC of $15.1 million, the realized cost savings amount to $1.7 million. Even with these adjustments, the State's annual required contribution is still projected to exceed the amount of insurance premium tax proceeds going to the General Fund (see Exhibit 13). Therefore, to meet the State's annual required contribution, the General Assembly will have to draw from General Fund sources other than the property insurance premium tax.

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[32] The department paid Buck Consultants $139,245 for the preliminary analysis of 1,000 of the 13,500 lapsed individuals. The department estimates it would cost between $900,000 and $1.5 million for Buck Consultants to examine the work history of the other 12,500 individuals.

[33] Concerns have been raised about the integrity of all member data, not just lapsed member data. Investigating the work history of all 40,000 members would be expensive and time-consuming, but it may be beneficial to the Pension Fund in the long run. Currently, when a member applies for benefits, the Department of State Treasurer verifies that the member has 20 years of service and member contributions. However, because members cannot apply for benefits until they are age 55 and may have served long before then (e.g., from age 18 to 38), members trying to retire may find themselves in the difficult position of needing one or two years of service credit they thought they had already earned. By conducting a work history on all members of the Pension Fund, the Department of State Treasurer could inform active members each year of how much service time they have earned toward vesting.

[34] This figure includes the cost of refunding contributions to lapsed members.

Exhibit 12

Using a 20% Lapse Assumption for Fiscal Year 2014–15 Lowers the State's Annual Required Contribution by $2.2 Million

Buck Consultants Unadjusted ARC (0% lapse assumption)	$15.1 million
Buck Consultants Adjusted ARC (20% lapse assumption)	$12.9 million
Difference	$2.2 million

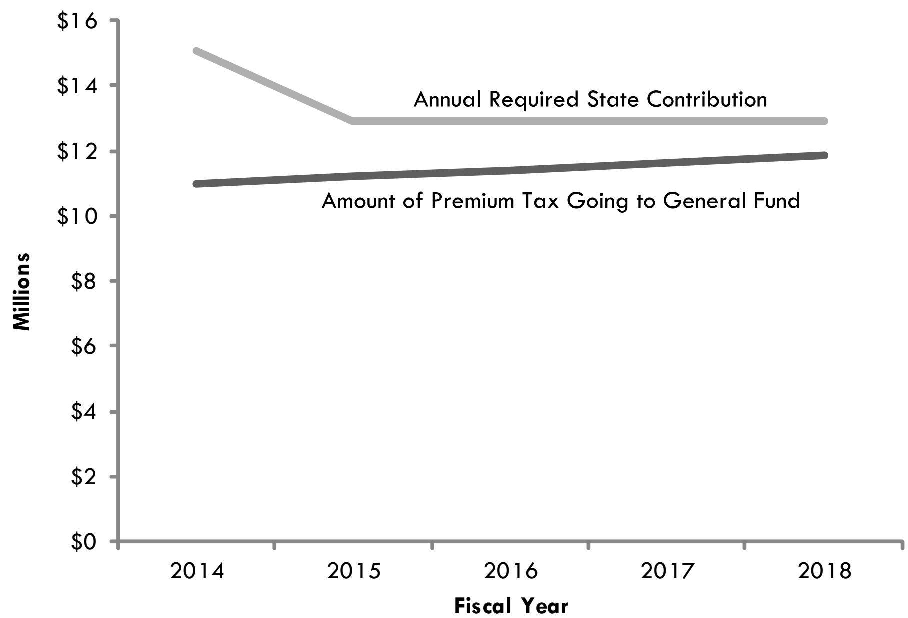
General Assembly's Recommended Continuation Budget	$14.6 million
Buck Consultant's Adjusted Estimated ARC	$12.9 million
Realized Cost Savings	$1.7 million

Notes: Buck Consultants Unadjusted and Adjusted ARCs are based on preliminary results; their full actuarial report is expected in September 2014.

Source: Program Evaluation Division based on data from Buck Consultants.

Exhibit 13

State's Annual Required Contribution is Projected to Exceed Premium Tax Proceeds



Notes: Projections for the amount of insurance premium tax going to the General Fund are based on consensus forecasts developed by the Fiscal Research Division and the Office of State Budget and Management using data from Moody's Analytics and IHS Global Insight. Projections for the State's annual required contribution are based on estimates generated by Buck Consultants and the assumption that, on average, actuarial gains and losses will offset each other.

Source: Program Evaluation Division based on data from the Department of Revenue and Pension Fund actuarial valuations.

To ensure members only receive service credit for timely contributions, the Department of State Treasurer is manually tying payment to service and is working to automate the process. As discussed in Finding 3, the Department of State Treasurer had not been enforcing the 90-day deadline for member contributions. Through Session Law 2013-284, the General Assembly clarified that members who fail to make contributions by March 31 after the calendar year in which service occurred may only purchase credit for prior service by making a lump sum payment equal to the full actuarial cost of such service.

To resolve this problem, the department made personnel changes to its Pension Fund team. As of February 2013, staff began manually matching service time to member contributions because the Online Retirement Benefits through Integrated Technology (ORBIT) system still automatically applies member contributions to the last delinquent payment. The department has contracted with a business analyst to determine the components that need to be built into ORBIT to automate the process. The business analyst's report is expected by August 2014.

Because the Department of State Treasurer is no longer applying member contributions to members' last delinquent payments, firefighters and rescue workers may ask the General Assembly to offer an open-enrollment period, but offering an open-enrollment period would cost the Pension Fund more in lost investment earnings. Throughout the history of the Pension Fund, the General Assembly has offered four open-enrollment periods, which allowed firefighters and rescue workers who failed to make timely contributions to purchase credit for prior service by paying the regular monthly rate together with an interest rate fixed by statute.[35] Outside of an open-enrollment period, firefighters and rescue workers who fail to make timely contributions have to

- pay the full actuarial cost of their prior service[36] or
- serve longer to meet the 20-year vesting requirement to receive benefits.

Because open-enrollment periods allow firefighters and rescue workers to purchase credit for prior service for less than the full actuarial liabilities created due to the additional credit purchased, the General Assembly offering an open-enrollment period would cost the Pension Fund additional lost investment earnings.

To ensure retirement benefits are not paid out to members still working as firefighters or rescue workers, the Department of State Treasurer is now corroborating the employment status of members. As discussed in Finding 4, the Department of State Treasurer was minimally enforcing the prohibition against in-service distributions, which stipulates that no member is entitled to benefits until the member has retired from performing any official duties as a paid firefighter or rescue worker. The department had only required prospective retirees and their department chiefs to certify on a form that the prospective retirees were not still being paid.

Now, the Department of State Treasurer is corroborating those claims with member data in the Local Governmental Employees' Retirement System (LGERS), which is also administered by the Department of State Treasurer. Most paid firefighters and rescue workers are also part of LGERS. The department is determining whether prospective Pension Fund retirees are in LGERS and whether they are currently serving as a paid firefighter or rescue worker so as to preclude payment of Pension Fund benefits.

[35] The last open-enrollment period was from October 2000 to March 2001, when eligible firefighters and rescue workers could receive credit for prior service by making a lump sum payment of $10 per month plus 8% interest per year.
[36] To receive credit for their service, members contribute $120 per year to the Pension Fund. For example, for a firefighter who is 55 and failed to make a timely contribution for prior service, the full actuarial cost of purchasing a year of time is $1,166 as opposed to the timely $120 annual contribution.

In summary, several findings threatened the long-term sustainability of the Pension Fund, but the Department of State Treasurer is taking actions to resolve them.

- The State's annual required contribution began exceeding the amount of insurance premium tax proceeds going to the General Fund in Fiscal Year 2011–12 (see Finding 1).
- The Department of State Treasurer's failure to enforce the timely payment of member contributions has cost the Pension Fund at least $508,361 (see Finding 3).
- The Department of State Treasurer minimally enforced the prohibition against paying benefits to members still working as firefighters or rescue workers (see Finding 4).

Nevertheless, these funding issues are mitigated by two other findings:

- The State's annual required contribution to the Pension Fund has been overstated due to overly conservative actuarial assumptions (see Finding 2).
- The Department of State Treasurer is taking action to resolve data collection and analysis issues and to comply with legislation enacted this past session that addressed member contributions and in-service distributions (see Finding 5).

Recommendation

Because the Department of State Treasurer is taking steps to address all of the issues discussed in this report, the Program Evaluation Division recommends that the General Assembly require the department to report on its progress toward

- building appropriate lapse assumptions into the State's annual required contribution;
- collecting timely member contributions; and
- enforcing the provision against in-service distributions.

Regarding its enforcement of the provision against in-service distributions, the department should develop a plan for implementing the stricter enforcement mechanisms discussed in Finding 4. The implementation plan should describe the necessary steps and resources required for the department to

- regularly compare Pension Fund retiree data to roster data collected by the North Carolina State Firemen's Association and the North Carolina Association of Rescue and EMS, Inc. to verify that Pension Fund retirees are not listed as active members on department rosters and
- regularly compare Pension Fund retiree data to tax data collected by the Department of Revenue to verify that fire departments are not reporting Pension Fund retirees on their W-2s as active employees.

The department should report annually to the House State Personnel Committee and the Senate Pensions & Retirement and Aging Committee, starting with the 2015 Session.

In addition, when the Department of State Treasurer submits its budget request for the State's annual required contribution, or ARC, the chairs of the House Appropriations and Senate Appropriations/Base Budget should request that the Fiscal Research Division provide it with the difference between the ARC and the amount of insurance premium tax proceeds going to the General Fund that year. This information will enable the General Assembly to track the amount of General Fund dollars from other revenue sources used to support the Pension Fund.

Finally, the General Assembly should amend N.C. Gen. Stat. Chp. 58, Art. 86 to conform with practice.

- Statute should clarify that members who earn their service exclusively as volunteers do not violate the prohibition against in-service distributions by being paid firefighters or rescue workers.
- Statute should clarify that members who earn their service exclusively as firefighters do not violate the prohibition against in-service distributions by being paid rescue workers. Similarly, members who earn their service exclusively as rescue workers do not violate the prohibition against in-service distributions by being paid firefighters.
- Statute should reference the one-month separation of service requirement in N.C. Gen. Stat. § 128-21(19) (Local Governmental Employees' Retirement System).

Agency Response

A draft of this report was submitted to the Department of State Treasurer, North Carolina State Firemen's Association, and North Carolina Association of Rescue and Emergency Medical Services, Inc. to review and respond. Their responses are provided following the report.

Program Evaluation Division Contact and Acknowledgments

For more information on this report, please contact the lead evaluator, Kiernan McGorty, at kiernan.mcgorty@ncleg.net.

Staff members who made key contributions to this report include Jim Horne, Meg Kunde, and Sara Nienow. David Vanderweide, in the Fiscal Research Division, also contributed. John W. Turcotte is the director of the Program Evaluation Division.

NORTH CAROLINA
DEPARTMENT OF STATE TREASURER
RETIREMENT SYSTEMS DIVISION

JANET COWELL
TREASURER

STEVE TOOLE
RETIREMENT SYSTEMS DIRECTOR

March 10, 2014

John Turcotte, Director
Program Evaluation Division
300 N. Salisbury Street, Suite 100
Raleigh, NC 27603-5925

Dear Mr. Turcotte:

Thank you for the opportunity to review your division's report titled, *"Department of State Treasurer Should Strengthen Its Oversight of the Firefighters' and Rescue Squad Workers' Pension Fund."* We value the collaborative efforts we have shared with your agency. We agree with this report's overarching conclusion that the Department is taking the necessary steps to address each of the major findings in your study and, as such, appreciate your recognition of the tireless efforts of our staff and their commitment to providing retirement security for public safety workers.

We also salute the diligent efforts of your staff at digging in to evaluate a program that has multiple layers of administrative complexity. As a part of the iterative evaluation process, our staff developed a 17-page technical response to your staff's draft report. Even though your team did not incorporate all of our suggestions, we appreciate that they took the time to discuss all of the significant factual points with us and we feel assured that your team achieved a sufficient level of understanding of the concerns we raised.

We do wish to highlight our concerns regarding two findings in the report. First, with regard to "Finding Three," we disagree with the report's conclusion that the Department should have been enforcing a deadline on payments from calendar years 2005 through 2009, since the report finds on page 15 that no deadline existed during that time period. However, we do agree that the Department should have enforced the deadline beginning in 2010, pursuant to the July 1, 2009 statutory amendment. As the report correctly asserts, our staff are now acting in accordance with the statute. Given the nature of this pension fund as a voluntary participation program, we would like to emphasize that, as noted in footnote 26, there is an absence of data to support the central conclusion of Finding Three. Furthermore, we also note that the sensitivity analysis detailed in footnote 26 shows, given the Report's analysis, that the impact of this issue is minimal.

Second, we can neither justify the significant administrative cost nor the complex enforcement issues that would result from the in-service distribution prohibition as envisioned in "Finding Four." The report finds that only one of 11,638 retirees examined may require further investigation by our staff to determine whether he was placed in payment status erroneously. Since this analysis points to a low error rate of 0.0086 percent in the Division's administration of NCGS 58-86-55, we do not share the conclusion that the pension fund needs to add significant administrative burden in order to enforce this statute. This low error rate demonstrates the existing administrative processes are working. Given that frame of reference, we believe that further analysis on the state's return on investment in the enforcement mechanisms detailed in "Exhibit 11" is warranted before we expend our limited information technology resources on a project with potentially limited utility for taxpayers.

Furthermore, the Department maintains its position that the better policy outcome for the state is to remove the prohibition on in-service distribution as originally envisioned in House Bill 327 and Senate Bill 304 during the 2013 session. Removing this prohibition would simplify administration of the pension fund and ensure that all members are treated equally.

We appreciate the Program Evaluation Division's oversight on behalf of the General Assembly and are committed to administering the state retirement funds consistent with North Carolina law and in a cost-efficient manner for the members of the system and for the taxpayers of our state. Even though we disagree with some findings in the report, we are confident that you agree with us that the true value of the retirement system to most citizens is as a tool to help the state recruit and retain qualified personnel to deliver essential government services. The provision of fire protection and rescue services is essential to the protection of life and property in the state. In the case of the Firefighters' and Rescue Squad Workers' Pension Fund, we are providing retirement security for public servants who put their lives on the line every time they answer a call.

We appreciate being asked to comment on the report.

Cordially,

Steven C. Toole

Steven C. Toole
Retirement Director,
Retirement Systems Division

North Carolina State Firemen's Association

March 7, 2014

Mr. John W. Turcotte
Director
Program Evaluation Division
300 N. Salisbury St. Suite 100
Raleigh, NC 27604

Dear Mr. Turcotte:

On behalf of the staff, Board of Directors, and 50,000 plus members of our Association we appreciate the opportunity to offer comments on the Study of the North Carolina Firefighters' and Rescue Workers Pension Fund by the Program Evaluation Division. It would appear from most of the findings in the report that the Department of the State Treasurer (DST) has or is initiating action to address most of the concerns of the report. The NCSFA staff worked extensively with the DST last year in reviewing and recommending changes to the statutes, and we believe those changes will correct the long term issues addressed in the report.

It is important to note that the Pension Fund has value in recruiting members into the fire and rescue community, but its major benefit serves in the area of retention. While many volunteer services see turnover in the five to seven year mark, the vested time earned in the Pension Fund is a motivator to carry forward for twenty years or more as a volunteer. It also motivates the individual toward receiving at least 36 hours of training annually. For career fire and rescue personnel, it may make the difference between staying in a service as inherently hazardous as firefighting or moving into another area of governmental or private service where the pay is similar, but the physical demands and injury rates are lower. This continuity of service saves money and time as opposed to training replacement personnel, and helps insure coverage in our primarily volunteer communities.

In Finding #1 the report indicates that the State's Annual Required Contribution now exceeds the amount of Gross Premium Tax (GPT) going into the General Fund. While this is true, it is our hope that administrative changes by DST and future evaluations and trends will reverse this gap. It is important to note also from the study that for many year's preceding 2011-2012 the General Fund was benefited overall by the GPT amount going into the General Fund exceeding the ARC. The key point now is that for the small investment of general funds money, the benefits to the state are overwhelming. All North Carolina citizens benefit from fire protection, whether at work, at home, or traveling our roadways. Mutual aid between departments keeps communities protected from major fires, while volunteer and career work side by side to benefit the citizens. Millions of dollars are saved in insurance premiums for citizens because of high levels of fire protection, and millions of dollars of loss are prevented each year which benefits the insurance industry. Protection from loss of life is priceless.

In Finding # 4, some of the suggestions to enforce the prohibition of in-service distributions may be difficult. There are numerous paid members of nonprofit departments that are not in LGERS, which makes an automated systems check of individual retirements difficult. This was one of the reasons fire and rescue associations asked the DST last year to seek relief from the in-service prohibition. This request was removed before debate over concerns of the fiscal note holding up other needed changes to the Pension statutes. In addition, as mentioned earlier, the ability to receive pension at age 55 could allow career departments to retain trained personnel longer. If an individual serves 20 or more years in a dangerous occupation where research (NIST and NIOSH) confirms shortened life spans, high injury rates, higher cancer rates, and higher risk of death than any other occupation, removing the in-service distribution seems a nondiscriminatory option. On page 18 of the report the estimate for the fiscal impact of removing the in-service prohibition may be flawed. It makes the assumption that 100% of paid members would be eligible for retirement at age 55, while in reality, many may have joined the department or Pension Fund after the age of 35 and would not be eligible at 55. This is particularly true on combination departments. Since 55% of the current participants in the fund are career the in-service prohibition against career could be considered vocational discrimination since their benefits are of less value to them than volunteers, bringing to question a potential legal query. It should be noted that in 1907 when the GPT was established, there were only career municipal departments, and the funding mechanism for the majority of this fund from the General Assembly was never meant to be strictly for volunteers.

In regards to a comparison to NCSFA roster records, this may not yield clear information on retiree data without significant individual record review since our rosters deal only with membership related issues. We also have concerns of the legal responsibility since, traditionally, payroll data should be between the employer and the master trust for the retirement system. In addition, our rosters can be changed periodically throughout the year but may only be changed at year end, and an individual may be denied their Pension because our roster has not been timely updated by the Chief of the department, an update we require only annually consistent with dues payment.

In conclusion, we appreciate the opportunity to comment on this report and look forward to working with the PED and General Assembly in continuing to improve the NC Firefighters Pension Fund. We are available to the PED staff at any time to provide additional information or to answer questions that may arise.

Sincerely,

Tim Bradley

Tim Bradley
Executive Director

CC: Board, North Carolina State Firemen's Association
Kiernan McGorty, Principal Evaluator

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Website: www.ncarems.org

March 3, 2014

Director John Turcotte
Program Evaluation Division
300 N. Salisbury St., Suite 100
Raleigh, North Carolina 27603-5925

Dear Director Turcotte:

We appreciate the opportunity to make comments on the Pension Fund.

We are working close with the State Treasurers Office in helping to resolve some of the issues with the administration of the fund.

We have no problems with members who are paid employees and have paid into the Pension Fund the required amount of contributions that are required and have the eligible service credits and reach the required age to draw a pension.

We need to do everything possible to retain the highly trained Emergency Services Personnel who provide services to the citizens of North Carolina.

For the Emergency Service Personnel to meet minimum EMT certification requires 169 hours and if they want to become a Paramedic 1096 hours in a two year program. Basic Fire certification requires 347 hours and Rescue Technician requires 186 hours. Paid or volunteer the certification requirements are the same.

Again these are the personnel we need to keep in the service and the Pension Fund is one benefit if they participate and remain in service.

Advise if we can be of further service.

Gordon A. Joyner
Executive Director