NOTE 11: RETIREMENT PLANS

The State reports ten retirement plans as pension trust funds. Section A of this note describes the seven defined benefit public employee retirement plans and one defined contribution plan administered by the State. The remaining plans, described in Note 12, are defined contribution plans administered by a third party under the auspices of the State. The State may or may not make supplementary contributions to these plans. Although the assets of the administered plans are commingled for investment purposes, each plan's assets may be used only for payment of benefits to the members of that plan and for administrative costs in accordance with the terms of the plan. The plans in this note do not issue separate financial statements, nor are they reported as part of other entities. The financial statements and other required disclosures are presented in Note 15 and in the *Required Supplementary Information* section of this *CAFR*. The State also provides an optional retirement plan for certain university employees and a special separation allowance for eligible sworn law enforcement officers.

A. Plan Descriptions and Contribution Information

1. *TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM*

This plan is a cost-sharing, multiple-employer, defined benefit plan established by the State of North Carolina to provide pension benefits for employees of the State, its component units, and local boards of education not in the reporting entity. Membership is comprised of employees of state agencies and institutions, local boards of education, universities and community colleges and certain proprietary component units. At June 30, 2006, the number of participating local boards of education and component unit employers was 194 as shown below:

Local boards of education	115
Community colleges	58
University of North Carolina System	18
Proprietary component units	3

Benefits and administrative expenses are funded by member contributions of 6% of compensation, investment income, and by an actuarially required employer contribution established by legislation. For the fiscal year ended June 30, 2006, the State made the actuarially based required contribution of 2.34% of covered payroll. Benefit and contribution provisions are established by General Statutes 135-5 and 135-8 and may be amended only by the North Carolina General Assembly.

The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains of the plan.

2. *CONSOLIDATED JUDICIAL RETIREMENT SYSTEM*

This plan is a single-employer, defined benefit plan established by the State of North Carolina to provide pension benefits for employees of the State Judicial System. Membership is comprised of judges, district attorneys and clerks of court. The plan provides retirement, disability and death benefits. Benefits and administrative expenses are funded by member contributions of 6% of compensation, investment income, and by employer contributions. For the fiscal year ended June 30, 2006, the State made a statutory contribution of 12.59% of covered payroll. This was greater than the actuarially required contribution of 12.06%. The difference of .53% was applied against the State's net pension obligation to this plan. Benefit and contribution provisions are established by General Statutes 135-57, 135-58, 135-68 and 135-69 and may be amended only by the North Carolina General Assembly.

The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains of the plan.

3. *LEGISLATIVE RETIREMENT SYSTEM*

This plan is a single-employer, defined benefit plan established by the State of North Carolina to provide retirement and disability benefits for members of the General Assembly.

The benefit will not be payable while the member is employed in a position making him eligible to participate in either the Teachers' and State Employees' Retirement System, Consolidated Judicial Retirement System or the Local Governmental Employees' Retirement System. Benefits and administrative expenses are funded by member contributions of 7% of compensation, investment income, and by actuarially based employer contributions. For the fiscal year ended June 30, 2006, there was no actuarially based required contribution and none was made. Benefit and actuarially based contribution provisions are established by General Statutes 120-4.21, 120-4.19 and 120-4.20 and may be amended only by the North Carolina General Assembly.

The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains of the plan.

NOTES TO THE FINANCIAL STATEMENTS

OTHER STATE ADMINISTERED SYSTEMS

The State also administers the following pension and retirement plans for persons who are not considered employees of the State or its component units.

4. *FIREMEN'S AND RESCUE SQUAD WORKERS' PENSION FUND*

This plan is a defined benefit pension plan established by the State of North Carolina to provide pension benefits for all eligible firemen and rescue squad workers. Membership is composed of both volunteer and locally employed firemen and emergency medical personnel who elect membership. At June 30, 2006, there were 1,491 participating fire and rescue units. This is a special funding situation in that the State is not the employer but is legally obligated to contribute to the plan.

Benefits and administrative expenses are funded by a ten dollar monthly contribution by the member, investment income and an actuarially based state appropriation. Benefit and contribution provisions are established by General Statute 58-86 and may be amended only by the North Carolina General Assembly.

5. *NORTH CAROLINA NATIONAL GUARD PENSION FUND*

This plan is a defined benefit plan established by the State of North Carolina to provide pension benefits for members of the North Carolina national guard. This also is a special funding situation because the State is not the employer, but is legally obligated to contribute to the plan.

Benefits and administrative expenses are funded by an actuarially based state appropriation and investment income. Benefit and contribution provisions are established by General Statute 127A-40 and may be amended only by the North Carolina General Assembly.

6. *REGISTERS OF DEEDS' SUPPLEMENTAL PENSION FUND*

This plan is a cost-sharing, multiple-employer, defined benefit plan established by the State of North Carolina to provide supplemental pension benefits for all eligible, retired county registers of deeds. Membership is composed of registers who are retired from the Local Governmental Employees' Retirement System or an equivalent local plan and have met the statutory eligibility requirements. At June 30, 2006, there were 100 registers enrolled in the plan with all 100 counties participating. An individual's benefits for the year are calculated as a share of accumulated contributions available for benefits for that year, subject to certain statutory limits. An individual's eligibility is based on minimum years of service as a register with the individual's share increasing with years of service. Because of the statutory limits noted above, not all contributions available for benefits are distributed. The State Treasurer administers the plan and *Section B* of this note describes the accounting and investing for the plan. The State's only cost in the plan is administration.

Benefits and administrative expenses are funded by investment income and 4.5% of the receipts collected by each County Commission under Article 1 of Chapter 161 of the North Carolina General Statutes. The statutory contribution currently has no relationship to the actuary's required contribution. Registers do not contribute. The actuarially required contribution and percentage of that contribution actually made is in the *Required Supplementary Information* section of this report. All benefit and contribution provisions are established by General Statute 161-50 and may be amended only by the North Carolina General Assembly.

7. *SHERIFFS' SUPPLEMENTAL PENSION FUND*

This plan is a defined contribution plan established by the State of North Carolina to provide supplemental pension benefits for all eligible, retired county sheriffs. Membership is comprised of sheriffs who are retired from the Local Governmental Employees' Retirement System and beneficiaries that meet the statutory eligibility requirements. At June 30, 2006, there were 76 sheriffs and two beneficiaries enrolled in the plan with all 100 of the State's counties eligible to participate.

An individual's benefits for the year are calculated as a share of accumulated contributions available for benefits for that year, subject to certain statutory limits. An individual's eligibility is based on minimum years of service as a sheriff with the individual's share increasing with years of service. Because of the statutory limits noted above, not all contributions available for benefits are distributed. The North Carolina Department of Justice administers the plan. If the plan purchases any investments, they are held as part of the State Treasurer's Investment Pool. *Section B* of this note describes the accounting and investing for the plan. The State's only cost in the plan is administration.

Receipts collected by each county's Clerk of Superior Court under General Statutes 7A-304(a)(3a), along with investment income, support the plan's benefits and administrative expenses. Sheriffs do not contribute to the plan. For the fiscal year ended June 30, 2006, the Clerks remitted $1.24 million. All benefit and contribution provisions are established by General Statute 143-166 and may be amended only by the North Carolina General Assembly.

8. *LOCAL GOVERNMENTAL EMPLOYEES' RETIREMENT SYSTEM*

This plan is a cost-sharing, multiple-employer, defined benefit plan established by the State of North Carolina for employees of local governments. Membership is comprised of general employees and local law enforcement officers of participating local governmental entities.

At June 30, 2006, the number of participating local governments was 924, as shown below:

Cities	427
Counties	100
Special districts	397

The plan provides retirement benefits nearly identical to the benefits that accrue to members of the Teachers' and State Employees' Retirement System. This plan also provides disability benefits for members who become totally and permanently disabled from performing their usual job. Benefits and administrative expenses are funded by employee contributions of 6% and actuarially based employer contributions. The annual required contribution (ARC) for all employers was 4.75% of covered payroll for law enforcement officers and 4.28% for general employees and firemen. Actual contributions were 5.27% of covered payroll for law enforcement officers and 4.8% for general employees and firemen. In addition, employers with an unfunded liability, established when the government initially enters the system, must make additional contributions towards that liability. The State's responsibility is administrative only. Benefit and contribution provisions are established by General Statutes 128-27 and 128-30 and may be amended only by the North Carolina General Assembly.

The plan does not provide for automatic post-retirement benefit increases. Increases are contingent upon actuarial gains.

The following table summarizes membership information by plan at the actuarial valuation date:

Employee Groups	Teachers' and State Employees'	Judicial	Legislative	Firemen's and Rescue Squad	North Carolina National Guard	Registers of Deeds'	Local Govern-mental
Retirees and beneficiaries currently receiving benefits	134,719	449	250	9,495	2,640	79	38,448
Terminated employees entitled to benefits but not yet receiving them	54,003	44	86	151	4,076	1	18,240
Active plan members	321,513	497	170	33,520	5,853	99	123,015
Total	510,235	990	506	43,166	12,569	179	179,703
Date of valuation	12-31-05	12-31-05	12-31-05	6-30-05	12-31-05	12-31-05	12-31-05

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PLAN ASSET MATTERS

BASIS OF ACCOUNTING

The financial statements of these plans are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

INVESTMENTS /SECURITIES LENDING

Pursuant to North Carolina General Statutes, the State Treasurer is the custodian and administrator of the retirement systems. The State Treasurer maintains various investment portfolios in its Investment Pool. The investment balance of each system represents its share of the fair value of the net assets of the various portfolios within the pool. Additionally, the securities lending balance represents assets occurring from securities lending transactions that result from the systems' participation in the pool. The investments of the State Treasurer and securities lending are fully discussed in Note 3.

C. Actuarial Methods and Assumptions

The latest actuarial valuations are dated December 31, 2005 (June 30, 2005, for Firemen's and Rescue Squad Workers' Fund). The actuarial accrued liability and the schedule of funding progress are presented by system in the *Required Supplementary Information* section of this report. The actuarial value of assets for all systems is based on a five-year smoothed market value. Under this method, realized and unrealized gains and losses on investments are smoothed over five years. Below are listed the various actuarial methods and significant assumptions for these valuations that will be used to determine future annual required contributions.

Retirement System	Valuation Date	Actuarial Cost Method	Amortization Method	Remaining Amortization Period	Period Open/Closed	Asset Valuation Method	Actuarial Assumptions: Investment Rate of Return	Actuarial Assumptions: Projected Salary Increase
Teachers' and State Employees'	12/31/05	Entry age	Level dollar	9 years	Open	5 year smoothed	7.25%	4.50-16.10%
Consolidated Judicial	12/31/05	Projected unit credit	Level percentage	9 years	Open	5 year smoothed	7.25%	5.75-11.75%
Legislative	12/31/05	Projected unit credit	Level dollar	8 years	Open	5 year smoothed	7.25%	7.50%
Firemen's and Rescue Squad	6/30/05	Entry age	Level dollar	9 years	Open	5 year smoothed	7.25%	N/A
North Carolina National Guard	12/31/05	Entry age	Level dollar	9 years	Open	5 year smoothed	7.25%	N/A
Registers of Deeds'	12/31/05	Entry age	Level dollar	N/A	Open	5 year smoothed	7.25%	4.50-14.65%
Local Governmental Employees'	12/31/05	Frozen entry age	Level percentage	Various	Closed	5 year smoothed	7.25%	4.50-14.73%

N/A-Not applicable

The valuations for the Teachers' and State Employees' system, Legislative system, and Consolidated Judicial system reflect a 3% cost of living increase for retirees in these systems. The Firemen's and Rescue Squad Workers' Fund increases retirement benefits by $2 (from $163 to $165). The National Guard system increases basic benefits from $75 to $80 and total potential benefits from $150 to $160. The Local Governmental Employee's system reflects a 2.8% cost of living increase. All of the benefit enhancements listed in this paragraph reflect legislation enacted by the North Carolina General Assembly effective July 1, 2006.

As of this valuation, the unfunded actuarial accrued liability for the Registers of Deeds' system, when amortized over 40 years is less than zero. This situation, which is not allowable under generally accepted accounting principles, is redefined by the actuary to effectively mean there is no liability to be amortized.

The projected investment returns and projected salaries for all systems, except the Legislative, include a 3.75% inflationary factor within the actuarial assumption. The assumption for the Legislative system does not identify an inflationary factor.

CURRENT FISCAL YEAR ASSUMPTIONS

Unless otherwise noted in this footnote or in the required supplementary schedules, the actuarial values, methods and significant assumptions for the current year's required contributions are the same as those presented in the table shown on the prior page. The annual required contributions (ARC) for the fiscal year ended June 30, 2006, were developed from various prior year valuations. The Teachers' and State Employees', Local Governmental Employees', Consolidated Judicial, and National Guard systems' valuations were as of December 31, 2003, the Legislative system was valued at December 31, 2004, and the Firemen's and Rescue Squad Worker's Fund was valued at June 30, 2004. These valuations used amortization periods of eight years for Legislative and nine years for all the other systems. Registers of Deeds' was valued at December 31, 2003, but effectively had no liability to be amortized. The Local Governmental Employees' system is an aggregate of numerous employers, and consequently, has various amortization periods. The rate of investment return and projected salary increases used in these valuations assumed essentially the same increases as in the most current valuations reported on the prior page.

For the fiscal year ended June 30, 2006, retirees in the Local Governmental Employees' system received a 2.5% cost of living adjustment. The Teachers' and State Employees' system, Legislative Retirement system and the Consolidated Judicial system provided a 2% cost of living increase for retirees. The Firemen's and Rescue Squad Workers' Fund increased retirement benefits from $161 to $163. All of these benefit enhancements reflect legislation enacted by the North Carolina General Assembly effective July 1, 2005. These enhancements were either reflected as liabilities in the December 31, 2004, valuations, or the systems paid for them through actuarial gains.

D. Annual Pension Cost and Net Pension Obligation

The annual pension costs and net pension obligations for the State's single-employer and special funding defined benefit plans for the current fiscal year are as follows (dollars in thousands):

	Consolidated Judicial Retirement System	Legislative Retirement System	Firemen's and Rescue Squad Workers' Pension Fund	North Carolina National Guard Pension Fund
Annual required contribution	$ 6,448	$ —	$ 7,926	$ 5,944
Interest on net pension obligation	99	(1)	49	(28)
Adjustment to annual required contribution	(176)	5	(105)	58
Annual pension cost	6,371	4	7,870	5,974
Less: Contributions made	6,732	—	7,926	6,042
Increase (decrease) in net pension obligation	(361)	4	(56)	(68)
Net pension (asset) obligation beginning of year	1,368	(21)	676	(386)
Net pension (asset) obligation end of year	$ 1,007	$ (17)	$ 620	$ (454)

NOTES TO THE FINANCIAL STATEMENTS

The following table presents the required three year trend of pension costs for the State's single-employer and special funding defined benefit plans and the annual required contributions (ARC) the State made to the Teachers' and State Employees' Retirement System (the System), a cost-sharing, multiple-employer plan. Except for (A) below, the State's statutory annual contribution to the System equals its total annual payment to the System and equals the State's pension cost in these financial statements. The State does not make any contributions to the Local Governmental Employees' System; therefore, it has no related pension cost.

State of North Carolina's Annual Pension Cost (APC) and Annual Required Contributions (ARC) as an Employer

For the Years Ended June 30, 2004 through June 30, 2006 (dollars in thousands)

	Teachers' and State Employees'	*Judicial*	*Legislative*	*Firemen's and Rescue Squad*	*North Carolina National Guard*
Primary Government:					
2006	$ 66,873	$ 6,371	$ 4	$ 7,870	$ 5,974
2005	59,021	6,432	4	7,460	1,431
2004 (A)	35,762	5,404	6	6,730	1,043
Component units:					
Universities:					
2006	$ 35,445				
2005	31,037				
2004	3,038				
Community Colleges:					
2006	$ 14,990				
2005	13,037				
2004	1,211				
Proprietary Funds:					
2006	$ 481				
2005	410				
2004	38				
Total Primary Government and Component Units:					
2006	$ 117,789	$ 6,371	$ 4	$ 7,870	$ 5,974
2005	103,505	6,432	4	7,460	1,431
2004	40,049	5,404	6	6,730	1,043
Percentage of APC Contributed:					
2006		106%	0%	101%	101%
2005		101%	0%	101%	109%
2004		112%	0%	102%	290%
Percentage of ARC Contributed:					
2006	100%				
2005	100%				
2004	100%				
Net Pension (Asset) Obligation:					
2006		$ 1,007	$ (17)	$ 620	$ (454)
2005		1,368	(21)	676	(386)
2004		1,449	(25)	737	(253)

(A) - The State's contribution/pension cost for the Teachers' and State Employees' Retirement System equals the actuarially required contribution plus $30 million in additional appropriations mandated by the N.C. General Assembly.

Yearly pension liabilities for the systems are shown in the *Required Supplementary Information* section of this report. Beginning with the accounting transition year of 1997, liabilities were determined in accordance with Governmental Accounting Standards Board Statement No. 27 (GASB 27). As presented here, each system's yearly APC and net pension (asset) obligation were computed retroactively to 1993 in accordance with GASB 27 and contain the cumulative effect of applying that statement.

E. Optional Retirement Plan

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Faculty and administrators with faculty rank in universities of the UNC System may join the Program instead of the Teachers' and State Employees' Retirement System. At June 30, 2006, the Plan had 11,239 participants.

Benefits are provided by means of contracts issued and administered by the privately-operated Teachers' Insurance and Annuity Association and the College Retirement Equities Fund (TIAA/CREF), Valid, Fidelity Investments and Lincoln National Life Insurance Company. Participants' eligibility and contributory requirements are established in General Statutes 135-5.1. Participants contribute 6% of compensation and the university contributes 6.84%. There is no liability other than the universities' required contributions. The universities contributed $67.09 million for the fiscal year ended June 30, 2006. Annual covered payroll was $980.88 million and employer contributions expressed as a percentage of annual covered payroll were the required 6.84% for the fiscal year ended June 30, 2006. Employee contributions expressed as a percentage of annual covered payroll were the required 6%, with actual employee contributions of $58.85 million for the fiscal year ended June 30, 2006.

Participants are vested after five years of service, but the company must return the value of the universities' contributions to the State if termination occurs prior to five years of service. The participant chooses his/her own investment products with the company of choice.

F. Special Separation Allowance

The State provides a special separation allowance (SSA), an agent multiple-employer, defined benefit pension plan, for sworn law enforcement officers as defined by General Statutes 135-1(11b) or General Statutes 143-166.30(a)(4) that were employed by State agencies and component units and retired on a basic service retirement under the provisions of General Statutes 135-5(a). To qualify for the allowance, each retired officer must: (1) have completed 30 or more years of creditable service or have attained 55 years of age and completed five or more years of creditable service; and (2) not have attained 62 years of age; and (3) have completed at least five years of continuous service as a law enforcement officer immediately preceding a service retirement. Each eligible officer is paid an annual separation allowance equal to .85% of the officer's most recent base rate of compensation for each year of creditable service. For the fiscal year ended June 30, 2006, the State and its component units paid $12.21 million for 897 retired law enforcement officers. These benefits are funded on a pay-as-you-go basis with each employer (the State or component unit) responsible for the benefits to their former employees. There is no statewide administration of the SSA and there is no actuarial valuation performed. Funds for this allowance are appropriated annually in the budget of each affected state agency or paid from the component unit's operations. These benefits are established in General Statute 143-166.41 and may be amended only by the General Assembly.