

**NOTES TO THE FINANCIAL STATEMENTS**

**NOTE 13: OTHER POSTEMPLOYMENT BENEFITS**

The State administers two postemployment benefit plans, the Retiree Health Benefit Fund and the Disability Income Plan, as pension and other employee benefit trust funds. 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 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. The financial statements and other required disclosures are presented in Note 15 and in the *Required Supplementary Information* section of this *CAFR*.

governments that are not part of the financial reporting entity also participate. At June 30, 2008, the number of participating employers was 258 as shown below:

State of North Carolina.....	1
LEAs and miscellaneous units.....	164
Community Colleges.....	58
University of North Carolina System.....	18
Proprietary component units.....	3
Local governments.....	14

**A. 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. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits are recognized when due and payable in accordance with the terms of each plan.

The Plan, (also referred to as the State Health Plan) is reported as an employee benefit trust fund. It is administered by the Executive Administrator and Board of Trustees of the Plan, which establishes premium rates except as may be established by the General Assembly in an appropriation act. Plan benefits received by retired employees and disabled employees are other post employment benefits (OPEB). The healthcare benefits for retired and disabled employees are the same as for active employees as described in Note 14, except that the coverage becomes secondary when former employees become eligible for Medicare.

*INVESTMENTS /SECURITIES LENDING*

Pursuant to North Carolina General Statutes, the State Treasurer is the custodian and administrator of the other postemployment benefits funds. The State Treasurer maintains various investment portfolios in its Investment Pool. Investments are reported at fair value, which is based on quoted market prices. The investment balance of the Disability Income Plan represents its share of the fair value of the net assets of the various portfolios within the pool. The Retiree Health Benefit Fund currently does not have investments.

Those former employees who are eligible to receive medical benefits are long-term disability beneficiaries of the Disability Income Plan of North Carolina (DIPNC) and retirees of the Teachers' and State Employees' Retirement System (TSERS), the Consolidated Judicial Retirement System (CJRS), the Legislative Retirement System (LRS), and the University Employees' Optional Retirement Program (UEORP), with five or more years of contributory membership service in their retirement system prior to disability or retirement, with the following exceptions. For employees first hired on and after October 1, 2006, and members of the General Assembly first taking office on or after February 1, 2007, future coverage as retired employees and retired members of the General Assembly is subject to the requirement that the future retiree have 20 or more years of retirement service credit in order to receive coverage on a noncontributory basis. Employees first hired on and after October 1, 2006 and members of the General Assembly first taking office on or after February 1, 2007 with 10 but less than 20 years of retirement service credit are eligible for coverage on a partially contributory basis. For such future retirees, the State will pay 50% of the State Health Plan’s total noncontributory premium. There is no impact of this legislation in the current fiscal year.

Additionally, the securities lending balance represents assets occurring from securities lending transactions that result from the funds’ participation in the pool. The investments of the State Treasurer and securities lending are fully discussed in Note 3.

**B. Plan Descriptions and Contribution Information**

*1. HEALTH BENEFITS*

Pursuant to North Carolina General Statutes, the State makes available a Comprehensive Major Medical Plan (the Plan), a cost-sharing multiple-employer defined benefit healthcare plan, exclusively for the benefit of employees and former employees of the State, the University of North Carolina System, community colleges, and certain other component units. In addition, Local Education Agencies (LEAs), miscellaneous educational units, and some select local

The Plan’s benefit and contribution provisions are established by Chapter 135-7, Article 1, and Chapter 135, Article 3 of the General Statutes and may be amended only by the North Carolina General Assembly. The plan does not provide for automatic post-retirement benefit increases.

By General Statute, a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those

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contributions shall be used to provide health benefits to retired and disabled employees and their applicable beneficiaries. By statute, the Fund is administered by the Board of Trustees of the Teachers' and State Employees' Retirement System and contributions to the Fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and their applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. However, Fund assets may be used for reasonable expenses to administer the Fund, including costs to conduct required actuarial valuations of State-supported retired employees' health benefits. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are determined by the General Assembly in the Appropriations Bill.

For the current fiscal year, the State and the other employers contributed the legislative mandated 4.1% of active employee salaries. The Fund is reported as an employee benefit trust fund. The State's total payments are shown in the following table. Actuarially required contributions and the percentage received from all employers can be found in the *Required Supplementary Information* section of this report.

## 2. DISABILITY INCOME

As discussed in Note 14, short-term and long-term disability benefits are provided through the Disability Income Plan of North Carolina (DIPNC), a cost-sharing, multiple-employer defined benefit plan, to the eligible members of the Teachers' and State Employees' Retirement System which includes employees of the State, the University of North Carolina system, community colleges, certain participating proprietary component units and Local Education Agencies (LEAs) which are not part of the reporting entity, and the University Employees' Optional Retirement Program. Long-term disability benefits are payable as an other postemployment benefit from DIPNC after the conclusion of the short-term disability period or after salary continuation payments cease, whichever is later, for as long as an employee is disabled. An employee is eligible to receive long-term disability benefits provided the following requirements are met: (1) the employee has five or more years of contributing membership service in the Teachers' and State Employees' Retirement System (TSERS) or the University Employees' Optional Retirement Program, earned within 96 months prior to the end of the short-term disability period or cessation of salary continuation payments, whichever is later; (2) the employee must make application to receive long-term benefits within 180 days after the conclusion of the short-term disability period or after salary continuation payments cease or after monthly payments for Workers' Compensation cease (excluding monthly payments for permanent partial benefits), whichever is later; (3) the employee must be certified by the Medical Board to be mentally or physically disabled for the further performance of his/her usual occupation; (4) the disability must have been continuous, likely to be permanent, and incurred at the time of active employment; (5) the employee must not be eligible to receive an unreduced retirement benefit from the TSERS; and (6) the employee must

terminate employment as a permanent, full-time employee. An employee is eligible to receive an unreduced retirement benefit from the TSERS after (1) reaching the age of 65 and completing five years of creditable service, or (2) reaching the age of 60 and completing 25 years of creditable service, or (3) completing 30 years of creditable service, at any age.

The monthly long-term disability benefit is equal to 65% of one-twelfth of an employee's annual base rate of compensation last payable to the participant or beneficiary prior to the beginning of the short-term disability period, plus the like percentage of one twelfth of the annual longevity payment to which the participant or beneficiary would be eligible. The monthly benefits are subject to a maximum of \$3,900 per month reduced by any primary Social Security disability benefits and by monthly payments for Workers' Compensation to which the participant or beneficiary may be entitled, but the benefits payable shall be no less than \$10 a month. When an employee qualifies for an unreduced service retirement allowance from the TSERS, the benefits payable from DIPNC will cease, and the employee will commence retirement under the Teachers' and State Employees' Retirement System or the University Employees' Optional Retirement Program.

Although the DIPNC operates on a calendar year, disability income benefits are funded by actuarially determined employer contributions that are established in the Appropriations Bill by the General Assembly and coincide with the state fiscal year. For the fiscal year ended June 30, 2008, the State and the other employers made a statutory contribution of .52% of covered payroll. This was greater than the actuarially required contribution of .49%. The State's total payments are shown in the following table. Actuarially required contributions and the percentage received from all employers can be found in the *Required Supplementary Information* section of this report.

The contributions cannot be separated between the amounts that relate to other postemployment benefits and employment benefits for active employees. Those individuals who are receiving extended short-term disability benefit payments cannot be separated from the number of members currently eligible to receive disability benefits as an other postemployment benefit.

Benefit and contribution provisions are established by Chapter 135, Article 6, of the General Statutes and may be amended only by the North Carolina General Assembly. By statute, the DIPNC is administered by the Department of State Treasurer and the Board of Trustees of the Teachers' and State Employees' Retirement System.

The plan does not provide for automatic post-retirement benefit increases.

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The following table presents the three year trend of the annual required contributions (ARC) the State and its component units made to the plans required by GASB 45. GASB 45 was implemented this fiscal year, 2008. Fiscal years 2006 and 2007 data represent required and contributed amounts to the plans. The ARC equals the State's OPEB cost.

State of North Carolina's Annual Required Contributions (ARC)  
and Annual OPEB Cost as an Employer  
For the Years Ended June 30, 2006 through June 30, 2008  
(dollars in thousands)

	Retiree Health Benefit	Disability Income
Primary Government:		
2008	\$ 135,051	\$ 17,128
2007	117,930	16,138
2006	108,597	14,861
Component units:		
Universities:		
2008	\$ 120,871	\$ 15,330
2007	104,297	14,272
2006	94,523	12,935
Community Colleges:		
2008	\$ 30,015	\$ 3,807
2007	26,642	3,646
2006	24,342	3,331
Proprietary Funds:		
2008	\$ 870	\$ 110
2007	815	112
2006	781	107
Total Primary Government and Component Units:		
2008	\$ 286,807	\$ 36,375
2007	249,684	34,168
2006	228,243	31,234
Percentage of ARC Contributed:		
2008	100%	100%
2007	100%	100%
2006	100%	100%

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

	<u>Retiree Health Benefit</u>	<u>Disability Income</u>
<b>Employee Groups</b>		
Retirees and beneficiaries currently receiving benefits .....	149,331	n/a
Disabled members receiving long term disability benefits .....	n/a	5,983
Terminated employees entitled to benefits but not yet receiving them .....	23,724	-
Active plan members .....	351,829	352,131
Total .....	<u>524,884</u>	<u>358,114</u>
Date of valuation .....	12/31/07	12/31/07

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The funded status of each plan as of the most recent actuarial valuation date is as follows (dollars in thousands):

	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c) (3)	UAAL as a Percentage of Covered Payroll ([b-a]/c)
Retiree Health (1)	12/31/07	\$ 296,500	\$ 28,890,120	\$ 28,593,620	1.0%	\$ 14,810,279	193.1%
Disability Income (2)	12/31/07	\$ 326,674	\$ 474,614	\$ 147,940	68.8%	\$ 13,849,158	1.1%

(1) The AAL has been prepared using the projected unit credit cost method.

(2) The AAL has been prepared using the entry age actuarial cost method. The information presented is intended to approximate the funding progress of the plan as required by GASB Statements 43 and 45.

(3) Buck Consulting reported the unadjusted covered payroll for the DIPNC long-term disability benefits.

Aon Consulting reported the adjusted, annualized payroll for postemployment health benefits.

### C. Actuarial Methods and Assumptions

Actuarial valuations of the plans involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The latest actuarial valuation for Retiree Health is dated December 31, 2007. The latest actuarial valuation for DIPNC is dated December 31, 2007. The schedules of funding progress, presented as required supplementary information following the notes to the financial statements, present multiyear trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

The actuarial assumptions used for the Retiree Health Benefit are consistent with those used to value the pension benefits of the TSERS where appropriate. These assumptions

are based on the most recent experience study prepared as of December 31, 2004 and adopted beginning with the December 31, 2005 pension valuation. The discount rate used for Retiree Health reflects a pay-as-you-go approach.

Projections of benefits for financial reporting purposes of the plans are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. Historically, the benefits funded solely by employer contributions applied equally to all retirees. Currently, as described earlier in the note, benefits are dependent on membership requirements.

The actuarial methods and assumptions used for DIPNC include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

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Below are listed the actuarial methods and significant assumptions for these valuations that will be used to determine future annual required contributions.

	<u>Retiree Health Benefit</u>	<u>Disability Income</u>
<b>Valuation Date</b>	12/31/07	12/31/07
<b>Actuarial Cost Method</b>	Projected Unit Credit	Aggregate
<b>Amortization Method</b>	Level percent of pay	Level percent of pay
<b>Remaining Amortization Period</b>	30 years	(1)
<b>Period Open/Closed</b>	Open	(1)
<b>Asset Valuation Method</b>	Market Value of Assets	5 year smoothed
<b>Actuarial Assumptions:</b>		
<b>Investment Rate of Return (2)</b>	4.25%	7.25%
<b>Healthcare Cost Trend Rate (2) (3)</b>	9% initial 5% ultimate	N/A
<b>Projected Salary Increases (4)</b>	N/A	4.5-16.1%

(1) The aggregate cost method does not identify or separately amortize unfunded liabilities, thus information about the plan's funded status and funding progress has been prepared using the entry age actuarial cost method. The information presented is intended to approximate the funding progress of the plan.

(2) Includes inflation at 3.75%.

(3) Trend rates apply to both Medicare eligible and pre-Medicare-eligible members.

(4) Aon Consulting used the projected unit credit method which does not include salaries, thus salary increases are not applicable for FY2008.

N/A Not Applicable