

COMMISSION ON GOVERNMENT FORECASTING AND ACCOUNTABILITY

PENSION IMPACT NOTE

101ST GENERAL ASSEMBLY

BILL NO: **SB 1300, as amended by HA 5, 6 and 7** November 18, 2019
SPONSOR (S): Castro – Holmes (Hoffman – Batinick)
SYSTEM(S): Downstate Police, Downstate Fire, TRS, SURS, IMRF, SERS

FISCAL IMPACT: In creating two unified investment entities for Article 3 and Article 4 pension funds (Downstate Police and Fire), SB 1300, as amended by HA 5-7, creates the opportunity for enhanced investment returns via expanded investment opportunities and savings in investment management fees. Also, some degree of administrative savings can be expected from streamlining actuarial services under the auspices of the consolidated funds. The amount of long-term savings from investment consolidation are highly dependent upon future market performance and the asset allocation of the consolidated funds. The costs of changing the final average salary calculation for Tier 2 members of Article 3 and Article 4 pension funds has not been determined, and is unknown at this time. The potential impact of changing the rate of growth in the final average salary cap for Tier 2 police officers and firefighters has also not been calculated.

SUBJECT MATTER: SB 1300, as amended by HA 5-7, amends various articles of the Illinois Pension Code. Primarily, the bill establishes two consolidated entities for Downstate Police and Fire pension funds (Article 3 and Article 4). These consolidated entities will be concerned with managing pension fund assets. Existing Article 3 and Article 4 pension funds will remain in operation for the purposes of administering benefits and adjudicating disability claims, but will have no investment authority after the conclusion of a 30-month “transition period.” The bill changes the final average salary period for Tier 2 police officers and firefighters, and also the rate of growth in the final average salary “cap” for Tier 2 police officers and firefighters. The changes are described in detail below in the Comment section. The bill also makes unrelated changes in the SURS, TRS, SERS, and IMRF articles of the pension code, which are also detailed below.

COMMENT:

Consolidated Police and Fire Pension Investment Funds

Under SB 1300, as amended by HA 5-7, as soon as practicable after the effective date of this Act, but no later than 30 months afterwards, each Article 3 and Article 4 fund shall transfer all of its securities, funds, assets, and moneys to the newly created Police Officers’ and Firefighters Pension Investment Funds (this period of time is referred to in the amendment as “the transition period”). Upon transferal, the two consolidated Funds will

assume management and investment authority, and the Article 3 and Article 4 funds shall no longer exercise control over such securities, funds, assets, and moneys.

The Transition Boards for the Consolidated Funds

- For each consolidated fund, the Governor will appoint a 9 member, temporary transition board within 1 month of the bill's effective date.
- Each transition board will select a chairperson from among the trustees and will consist of the following members:
 - 3 members representing municipalities who are mayors, presidents, chief executive officers, chief financial officers, or other officers or executives of municipalities. They will be appointed from among candidates recommended by the Illinois Municipal League.
 - 3 selected from participant members, as detailed below:
 - For the Police Fund transition board, 2 will be appointed from among candidates recommended by an organization representing more than 20,000 active and retired police officers in the State of Illinois, and one will be appointed from among candidates recommended by a benevolent association representing police officers in the State of Illinois.
 - For the Firefighter Fund transition board, all 3 will be recommended by a statewide labor organization representing at least 85 municipalities and which is affiliated with the Illinois State Federation of Labor.
 - 2 employee/annuitant members, as detailed below:
 - For the Police Fund, 2 members selected from beneficiary members. One will be appointed from among candidates recommended by an organization representing more than 20,000 active and retired police officers in the State of Illinois, and one will be appointed from among candidates recommended by a benevolent association representing police officers in the State of Illinois.
 - For the Firefighter Fund transition board, one member will be selected from beneficiary members. They will be recommended by a statewide labor organization representing at least 85 municipalities and which is affiliated with the Illinois State Federation of Labor. One participant member recommended by a statewide labor organization representing at least 85 municipalities and which is affiliated with the Illinois State Federation of Labor
 - 1 representative of the Illinois Municipal League
- The “transition period” begins on the effective date of the Act and will end when so determined by the transition board. The transition boards cannot function for a period longer than 30 months.

- The transition board members will serve until the end of the transition period and until the permanent board members are elected.
- This initial election for the permanent board will be administered and conducted by the transition board, with the permanent board determining the procedure for all future elections.

The permanent Boards of Trustees for the Consolidated Funds

- The permanent Boards of Trustees will consist of 9 members, as follows:
 - 3 employer members who are mayors, presidents, chief executive officers, chief financial officers, or other officers or executives of municipalities. They will be elected by the mayors and presidents of municipalities with participating pension funds.
 - 3 members elected by and from active participant members
 - For the Police Board, 2 members elected by and from beneficiary members.
 - For the Firefighter Board, 1 member elected by and from beneficiary members. Also, for the Firefighter Board, 1 member appointed by the Governor with the advice of the Senate following recommendation by a statewide labor organization representing at least 85 municipalities and which is affiliated with the Illinois State Federation of Labor.
 - 1 member recommended by the Illinois Municipal League and appointed by the Governor, subject to Senate confirmation
- The Chairperson of the permanent boards will serve 2 year terms and will be selected from among the trustees.

Consolidation Timeline of Events:

- The transition board will audit the investment assets of each current Article 3 and Article 4 fund as soon as practicable after the effective date of the bill.
- Once the audit is certified by both the newly created board(s) and the existing Article 3 and Article 4 funds, the transfer of assets will begin within 10 business days.
- The interim executive directors of each newly created board, appointed by the Governor until the permanent boards appoint their own, will notify the board of trustees of existing Article 3 and Article 4 funds no less than 30 days before the consolidated Fund takes control of their assets.
- Within 90 days after the end of the transition period, all remaining assets in any Article 3 and Article 4 fund must be transferred into the consolidated Fund.
- Within 6 months after the end of the transition period, a public accountant selected by the consolidated boards will audit the consolidated funds. The report will be published on the Funds' website and filed with the Department of Insurance.
- Quarterly reports will be issued by the consolidated Funds to Article 3 and Article 4 funds detailing the status of investments.

- A yearly, more comprehensive report will be published by the consolidated funds describing their investment operations, yearly performance, and other related information. Included in this report will also be the results of an audit undertaken by an accounting firm selected by the board of the consolidated fund.

Relinquishment of investment authority for Article 3 and Article 4 funds

- The General Provisions article is amended so that Article 3 and Article 4 funds shall, upon transferal of assets, no longer exercise any investment authority over such investments.

Illinois Finance Authority loan authorization

The Illinois Finance Authority is authorized to loan up to \$7,500,000 to each consolidated Fund to assist with the costs associated with the transition process. The loan shall be repaid by the Fund with an interest rate tied to the Federal Funds Rate or an equivalent market established variable rate. Such agreement will be made public record and the terms of the loan will be posted on the Fund's official website.

Department of Insurance examinations and investigations

Current law allows the Department of Insurance to accept, in lieu of conducting their own investigation, an audit or examination performed by an independent certified public accountant on behalf of any pension system. HA 5-7 to SB 1300 amends the Pension Code so that:

- After the end of the transition period, the Department of Insurance may accept and rely upon an audit or examination performed by an independent certified public accountant retained by the consolidated funds.

Current law states that such audits and examinations shall be conducted once every three years. HA 5-7 to SB 1300 grants the consolidated funds the same powers to conduct audits and/or investigations that the Department of Insurance currently exercises.

Annual Financial and Actuarial Statements

Under current law, each Article 3 and Article 4 fund files yearly financial and actuarial statements with the Department of Insurance and can do so utilizing the services of independent actuaries. HA 5-7 to SB 1300 amends Pension Code so that:

- After the conclusion of the transition period, each actuarial statement will be prepared by or under the supervision of an actuary retained by the consolidated funds.
- The bill implements 3-year "actuarial assumption smoothing" for the consolidated funds, whereby the net impact of any changes in actuarial or investment assumptions will be implemented in equal annual amounts over a 3-year period, beginning in the fiscal year in which the change first occurs. ("Actuarial assumption smoothing" was implemented for the five State systems in 2017 via P.A. 100-0023).

Article 3 and Article 4 pension funds, Tier 2 Final Average Salary

Current law dictates that Tier 2 employees of Article 3 and Article 4 funds have their pensions based on their final average salaries using the 96 consecutive months of service

during which their total salary is highest within their last 120 months of service. HA 5-7 to SB 1300 amends the Downstate Police and Fire Pension Code so that:

- Tier 2 employees' final average salaries are calculated using the greater of (i) the method dictated by current law, previously summarized or (ii) the 48 consecutive months of service when their total salary is highest within their last 60 months of service.

Article 3 and Article 4 pension funds, Computation of Final Average Salary Cap

Under current law, the highest salary that can be used for calculation of a final average salary for Tier 2 employees in an Article 3 or Article 4 fund is \$106,800. However, that amount has been increased annually since 2011 by the lesser of (i) 3% of that amount, or (ii) 50% of the annual unadjusted percentage increase in the consumer price index-u. HA 5-7 to SB 1300 amends Pension Code so that:

- The final average salary cap increases by the lesser of (i) 3% of that amount, or (ii) 100% of the annual unadjusted percentage increase in the consumer price index-u.
- The bill does not permit retroactive changes in employee contributions.
- COLA's will still be computed at simple interest.

Article 3 and Article 4 pension funds, Tier 2 Survivor pensions

For Article 3 and Article 4 fund employees in the Tier 2 system, current law entitles spouses, children, or parents of a police officer or firefighter to survivor pensions equal to 66 2/3% of the police officer or firefighter's earned pension at the date of death. HA 5-7 to SB 1300 amends Pension Code so that:

- The survivors are entitled to the greater of (i) the current survivor benefit, previously described, or (ii) 54% of the police officer or firefighter's monthly salary at the date of death.
- If a survivor is a spouse, then the guardian of any minor children, including children not yet born, is entitled to 12% of such monthly salary for each child until they reach 18.
- A monthly pension of 20% of such monthly salary is granted upon the death of the surviving spouse, or upon the death of a police officer or firefighter leaving one or more minor children but no surviving spouse, to an appointed guardian until the children reach 18.
- The total survivor's pension provided shall not exceed 75% of the monthly salary of the deceased officer or firefighter when paid to the survivor of an officer or firefighter who:
 - Has attained 20 or more years of service credit and receives or is eligible to receive a pension.
 - Dies as a result of illness or accident.
 - Dies from any cause while in receipt of a disability pension.
 - Is a deferred pensioner.

Changes in Training Requirement for Article 3 and 4 Pension Trustees

Currently, all elected and appointed trustees for Downstate Police and Fire pension funds must undergo 32 hours of initial trustee training certification in a variety of areas, including fiduciary fundamentals, adjudication of pension claims, and trustee ethics, among others. This bill reduces the initial hourly commitment to 16 hours of training, and deletes the requirement that trustees undergo “basic accounting and actuarial training.” The bill requires all trustees elected or appointed before the effective date of this Act to undergo 4 hours of training on the changes made by this bill. In addition, the bill reduces the annual continuing education requirement for trustees from 16 hours to 8 hours.

Alternative (State Police) Formula Eligibility for Certain Police Officers

HA 5-7 to SB 1300 amends the General Provisions and State Employees articles of the Illinois Pension Code to allow Conservation police officers, Secretary of State investigators, Commerce Commission police officers, arson investigators, and investigators for the Department of Revenue or the Illinois Gaming Board to qualify for the alternative (state police) formula in SERS as of the effective date of the bill. HA 5-7 also allows these officers the opportunity to convert up to eight years of prior regular formula service credit into alternative formula service. In order to convert these years of service, the officer must apply within one year of the effective date of this bill, and pay to SERS an amount equal to the difference between what was actually paid for the regular formula service and what would have been paid had the service been accrued under the alternative formula, plus interest at the actuarially assumed rate, compounded annually, from the date of service to the date of payment.

Reinstatement of Eligibility for Certain Survivor Annuities in IMRF

P.A. 99-682 was enacted to allow those IMRF members who had retired prior to the passage of the Illinois Religious Freedom Protection and Civil Union Act (P.A. 96-1513) to reinstate a survivor benefit after retirement. HA 5-7 to SB 1300 would extend this right to the surviving spouse of an annuitant, provided the annuitant (1) retired prior to June 1, 2011, (2) was not married on the date the retirement annuity began, (3) received a refund of survivor credits; and (4) died prior to the implementation of P.A. 99-682. Eligible surviving spouses may re-establish survivor benefit rights by paying to IMRF the total amount of the refund received for survivor credits, including interest, within one year beginning 5 months after the effective date of the bill. The surviving spouse would be required to provide documentation proving that he or she was married to the annuitant at the time of death and has not since remarried.

Optional Service Credit for certain State Police Officers

HA 5-7 to SB 1300 allows State Police officers to establish up to 5 years of service credit for law enforcement service with the federal government, or by a state or local government located outside Illinois, provided credit for such service is not held in another public pension fund. In order to establish this service credit, the officer must pay to SERS the following amounts: 1) employee contributions based on the applicant’s salary on the first day of service in Illinois following the out-of-state employment, plus 2) the employer’s normal cost of the benefit for the service credit being established, plus 3) interest at the actuarial rate of return on the foregoing amounts. The officer must apply for this optional service within 3 years of the effective date of this bill.

Change in Retirement Eligibilities for Certain SURS Tier 2 members

SURS provides different formula rate structures to calculate retirement annuities. Among the several formula rate structures, “Rule 4” applies to police officers and firefighters. It provides a higher formula than the flat 2.2% rate under “Rule 1.” Under current statutes, the Tier 2 eligibility for the Rule 4 formula is age 67 with at least 20 years of service as a police officer or a firefighter for the full retirement annuity, as opposed to age 50 with 25 years or age 55 with 20 years for Tier 1 members.

Graduated formula rates for Rule 4 are as follows:

- For each of the first 10 years: 2.25%
- For each of the next 10 years: 2.50%
- For each in excess of 20 years: 2.75%

Under SB 1300, as amended by HA 5-7, the eligibility for the Rule 4 formula rates would be lowered to age 60 with 20 years for Tier 2 public safety members. This change applies retroactively to January 1, 2011.

SURS Board of Trustees

Currently, the Chairperson of the Board of Higher Education shall become the Chairperson of the SURS board of trustees board by statutes. Under this legislation, the Governor would appoint the Chairperson of the Board from among the trustees.

Change in the Structure of the TRS Board of Trustees

Currently, the TRS Board consists of 13 members, as follows:

- the Superintendent of Education, ex officio, who shall be the president of the board by law;
- 6 non-members of TRS, appointed by the Governor and not to hold elected State office;
- 4 teachers elected by the TRS members; and
- 2 annuitant members elected by TRS annuitants.

Under this legislation, the number of the TRS Board members would increase to 15, with one more non-member appointed by the Governor and one more teacher elected by TRS members. In other words, the board would have 7 non-members instead of 6, and 5 teachers instead of 4. In addition, the president of the board would be appointed by the Governor, rather than the Superintendent of Education automatically serving as the president of the board.

Summary of HA 6

HA 5 to SB 1300, which contained the main body of the legislation heretofore described, had a provision prohibiting a third party from controlling, altering, or modifying, or having the ability to review or intervene in the proceedings or decisions of the existing Article 3 and Article 4 funds. HA 6 is a technical amendment which clarifies that only the consolidated funds shall not have the aforementioned “intervention authority” in the operations of existing Article 3 and Article 4 pension funds. So, for example, the board or staff of the consolidated funds would not be able to present evidence during a disability review hearing of an existing Article 3 or Article 4 pension fund, but an employing municipality could present such evidence.

Summary of HA 7

HA 7 to SB 1300 added investigators for the Department of Revenue or the Illinois Gaming Board to the list of police officers now eligible for the SERS alternative (State Police) formula, and to convert up to 8 years of previous regular formula service credit into alternative formula service, as described in the pertinent section above.

DH:bj
LRB101 07899 RPS 64703 a