

COMMISSION ON GOVERNMENT FORECASTING AND ACCOUNTABILITY

PENSION IMPACT NOTE

101ST GENERAL ASSEMBLY

BILL NO: **HB 3013**

March 1, 2019

SPONSOR (S): Martwick

SYSTEM(S): Downstate Fire, General Provisions Article

FISCAL IMPACT: HB 3013 makes sweeping changes to the operation, benefits, and liability accrual of Downstate Fire pension funds; an independent actuarial study is necessary to determine the fiscal impact of the many changes enumerated in the Comment section below. HB 3013 mandates an investment consolidation feasibility study for police and fire pension funds to be performed by CGFA. A supplemental appropriation would be needed to engage the services of an independent investment consultant to perform this study.

SUBJECT MATTER: HB 3013 makes definitive changes to Tier 2 final average salary calculations, maximum salaries, annual cost of living increases, survivor's benefits, and the amortization period and employer contribution calculations. Additionally, HB 3013 proposes to create an opt-in Downstate Firefighters Pension Investment Fund that eligible funds may elect to join. The details of these changes are enumerated in the Comment section below.

COMMENT:

Tier 2 Downstate Fire Salary, Cost of Living Increases, Survivor's Benefits, and Amortization Period Changes

Tier 2 Final Average Salary

- Current statute stipulates that the final average salary for annuity purposes for Tier 2 members is determined by determining the average monthly salary obtained by dividing the total salary of the firefighter during the 96 consecutive months of service within the last 120 months of service in which the total salary was the highest by the number of months of service in that period. HB 3013 would present a second option for determining pensionable salary. Option 2 would allow for the calculation of a retirement annuity based upon the highest salary in a consecutive 36-month period within the last 48 months of service.

Under HB 3013, the firefighter's pension would be based upon the greater of the two final average salary calculations.

Tier 2 Maximum Salary

- P.A. 96-1495, the Police and Fire Tier 2 Pension Act of 2010, set the Tier 2 pensionable salary cap for members of Downstate Fire pension funds at \$106,800. The act increases the cap by the lesser of 3% or half of the consumer price index-u, including all previous adjustments. As of 2018, the cap is up to \$113,645. Beginning in 2020, HB 3013 would set this rate of increase to the lesser of 3% or the annual unadjusted percentage increase in the CPI-U, including all previous adjustments.

Tier 2 Annual Cost of Living Increases

- Current statute determines the Tier 2 annual increase for members of Downstate Fire pension funds by using the lesser of 3% or one half the annual unadjusted percentage increase in the consumer price index-u in the year prior to retirement. This annual cost of living adjustment amount was put into place upon the enactment of P.A. 96-1495 (SB 3538). HB 3013 would increase Tier 2 COLA's to 3% of the originally granted pension (or non-compounded).

Tier 2 Survivor's Pension

- Current statute determines that a survivor's pension equal to two-thirds (66 2/3%) of the firefighter's earned pension at the date of death. HB 3013 would provide another option for calculating the benefits a survivor would receive. Option 2 would allow for the calculation of a survivor's annuity to be the greater of 54% of the firefighter's monthly salary at the date of death, or two-thirds (66 2/3%) of the firefighter's earned pension at the date of death.
- Furthermore, HB 3013 defines benefits for children. If a surviving spouse is the guardian of any minor children, 12% of such monthly salary shall be paid for each child until the attainment of age 18. Should the firefighter's spouse die, or should the firefighter die without a spouse, the guardian of each child shall receive 20% of the monthly salary for the support and maintenance for each child under their care.

Funding Schedule

- Current statute provides that the annual required employer contribution is calculated to equal (1) the normal cost of the pension fund for that year, or 17.5% of the salaries and wages to be paid to firefighters, whichever is greater, and (2) an amount sufficient to bring the total assets of the fund up to 90% of the total actuarial liabilities of the fund by the end of the fiscal year 2040, as annually updated and calculated by an actuary using the projected unit credit actuarial cost method.
- HB 3013 proposes to extend the amortization period to 2050 and increase the funding goal to 100%. Additionally, HB 3013 provides that the actuary would calculate normal cost using the entry age method. Finally, HB 3013 limits the payroll growth assumption an actuary may use to calculate the annual contributions necessary to amortize the unfunded accrued liability as a level percentage of payroll to not be greater than 2.5%.

Consolidation: Creating the Downstate Firefighters Pension Investment Fund*Shifting Investment Authority*

- Eligible Pensions
 - In order to transfer investment authority from an existing Article 4 pension fund to the Board of Trustees of the Downstate Firefighters Pension Investment Fund, a pension fund must reach a “threshold amount” of net assets equal to 3 months of current liabilities.
 - Eligible funds board of trustees must adopt a resolution by an absolute majority of the total number of members entitled to serve on the board. This transfer of authority is irrevocable, and upon the receipt of a certified investment asset list the board shall terminate investment activities.
- The Department of Insurance shall conduct an audit within 6 months of receiving an adopted resolution, the cost of which is paid for by the fund.
- Funds shall transfer assets within 30 days of the end of each quarterly meeting of the funds board of trustees. Each transfer must be accompanied by a written notice to the Downstate Board.
- Within 6 months of the completion of the transfers of investment assets to the Downstate Board, an audit published to the Downstate Board’s website shall be conducted that includes:
 - i. full description of investments acquired and their average costs;
 - ii. full description of the securities sold or exchanged, showing average proceeds or other conditions of an exchange;
 - iii. gains or losses during the transfer;
 - iv. investment income;
 - v. administrative expenses of the board; and
 - vi. the proportion of administrative expenses allocable to each pension fund.

Downstate Fire Investment Board of Trustees

- From the enactment date of this bill to January 1, 2023, an interim Board of Trustees shall be made up of:
 - The State Treasurer (or their designee), who shall serve as the chairperson and vote only in the case of a tie.
 - Three Executive Trustees, comprised of executive officials and appointed by a joint resolution adopted by the General Assembly.
 - Two Firefighter Trustees shall be firefighters participating in an eligible fund, appointed by a joint resolution adopted by the General Assembly.
 - One Annuitant Trustee shall be a retired firefighter participating in an eligible pension fund, appointed by a joint resolution adopted by the General Assembly. Firefighters receiving disability are considered retired.
 - Appointments are to be made within 120 days of the effective date of this bill. If an appointment isn’t made within the 120 day period, the State Treasurer shall make the appointment within 30 days of the expiration date.

- Appointed members serve from November 1, 2020 to December 31, 2022.
- Two vice-chairpersons and a recording secretary shall constitute an executive committee that handles the Board's activities in the interim of meetings.
 - One vice-chairperson is elected by firefighter trustees, the other from executive trustees; the secretary is selected from the membership of the Board.
- Beginning January 1, 2023, the Board shall consist of the following members:
 - Five elected Executive Trustees, each of whom shall be an executive official from participating municipalities.
 - An executive must have a representative from at least 5 municipalities to sign a petition to be nominated. Each governing body of participating municipalities votes to determine Executive Trustees.
 - Five elected Firefighter Trustees, three of whom shall be active firefighters and two of whom shall be retired firefighters, each from participating municipalities.

Active and retired firefighters are selected in separate elections. Active nominees require at least 50 active member signatures, and annuitants require at least 25 annuitant signatures. Actives may vote for active Trustee nominees, and retirees may vote for retiree Trustee nominees.
 - The State Treasurer (or their designee) shall serve as the chairperson and may only vote in the case of a tie.
 - Two vice-chairpersons and a secretary shall be selected to serve on the executive committee that shall handle Board operations in the interim of Board meetings.
 - One vice-chairperson is elected by Firefighter Trustees, the other by the Executive Trustees; the secretary is selected from the membership of the Board.

Downstate Fire Investment Board: Duties & Operations:

- The Downstate Fire Investment Board shall appoint an executive director and investment officers to administer the affairs of the Fund.
 - With approval of the Board, the executive director may enlist the Illinois Municipal Retirement Fund and/or the Illinois State Board of Investment to provide assistance, services, or facilities for the Downstate Fire Pension Investment Fund.
- The Board shall have the authority to arrange for advisory services from national or state banks, authorized trust companies, or other financial institutions organized and /or authorized by Illinois or the federal government.
- The Board may commingle all or part of the invested assets of one or more eligible pension funds under its authority. Assets shall carry the cost or value determined by generally accepted accounting principles.
 - Each investment initially transferred to the Board shall be evaluated; should the realization of an asset in cash be in excess or less than the

credited value, the difference shall be credited or charged to the fund that made the transfer.

- Each eligible fund shall be charged for their respective share of expenses of the Board on a quarterly basis, according to the value of investments held for respective funds.
- At least annually, the Board shall present an audit prepared by a certified public accountant designated by the Auditor general.
 - The audit is published in an annual report of the Board, which includes other fiscal information regarding the investments, policies, audited financial statements, and recommendations for possible changes, among other statutory requirements.
- HB 3013 requires Trustees to complete additional hours of training, with at least 8 hours of training during the first year to cover fiduciary duties and liabilities, as well as trustee ethics.

Local Boards

- Existing Article 4 pension boards are not removed under HB 3013
- HB 3013 mandates that the Downstate Investment Board must make annual reports to local boards concerning investments held, amounts allocable to each fund, comments, and a review of policies, among other financial data.
 - The Board shall provide a full receipt to the local board once the transfer of all assets, securities, and other pension investments to respective Downstate Investment Boards is completed.
- The Downstate Investment Board must also make deposits into local pension funds, from which benefits are paid.
 - Participating municipalities are required to maintain reserves equal to 3 months' current liabilities.
- Any disputes between local boards and the IMRF shall be resolved by the Director of the Department of Insurance.

Commission on Government Forecasting and Accountability Study:

- HB 3013 requires that, by December 31, 2021, the Commission on Government Forecasting and Accountability shall complete an analysis of the merits and feasibility of:
 - (1) Transitioning the investment authority of all downstate boards of trustees of police pension funds organized under Article 3 to a single police pension investment fund; this analysis shall include:
 - i. An examination of the impact of the investment pool;
 - ii. The expected future fund performance of a single police pension investment fund under the prudent investor rule;
 - iii. The expected future total expense ratio and expenses of a single police pension investment fund; and
 - iv. Any other issues of costs and savings of transition unique to a single police pension investment fund-managed pension fund operation
 - v. Additionally, the analysis should evaluate the time period in which the transition could reasonably occur and recommend a reasonable

transition period, while maintaining the present funding requirements of 90% funding by 2040.

- (2) Transitioning the investment authority of all downstate boards of trustees of firefighters pension funds organized under Article 4 to the Downstate Firefighters Pension Investment Fund under Article 4A; this analysis shall include:
 - i. An examination of the impact of the investment pool;
 - ii. The expected future fund performance of the Downstate Firefighters Pension Investment Fund under the prudent person investor rule;
 - iii. The expected future total expense ratio and expenses of the Downstate Firefighters Pension Investment Fund
 - iv. And any other issues of costs and savings of transition unique to a Downstate Firefighters Pension Investment Fund-managed pension fund operation
 - v. Additionally, the analysis should evaluate the time period in which the transition could reasonably occur and recommend a reasonable transition period, while maintaining the present funding requirements of 100% by 2050
- (3) Furthermore, the Commission must also:
 - i. Identify which Article 3 and 4 pension funds receive employer contributions from home rule or non-home rule units of local government
 - ii. Identify funds based on funded ratios: under 20%, 20-30%, 30-40%, 40-50%, and over 50%
 - iii. Identify which funds were most recently investigated by the Public Pension Division of the Department of Insurance, and
 - iv. Identify which Article 3 and 4 pension funds are not in compliance regarding the filing of their annual actuarial statements.

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