

COMMISSION ON GOVERNMENT FORECASTING AND ACCOUNTABILITY

PENSION IMPACT NOTE

102nd GENERAL ASSEMBLY

BILL NO: **HB 3305**

March 23, 2021

SPONSOR (S): Durkin - Spain

SYSTEM(S): GARS, SERS, SURS, TRS, and Chicago Teachers

FISCAL IMPACT: HB 3305 introduces the "consideration model" for Tier 1 employees as enumerated below. Based upon a study conducted by COGFA's actuary in 2018, the proposal was expected to result in State pension contribution savings of \$7.8 billion through FY 2045 (\$3.9 billion in "present value" dollars in the year 2018). Please see page 3 for a summary of the actuarial analysis.

SUBJECT MATTER: HB 3305 proposes the "consideration model" which gives Tier 1 employees under Articles 2, 14, 15, 16, and 17 the option to choose to receive delayed and reduced annual increases in exchange for a "consideration payment" of 10% of contributions already made and a reduction in annual contributions going forward (see the chart under "Tier 1 contribution changes" on Page 3 for more information on Tier 1 employee contribution rate reductions). Future pay increases would be considered pensionable. Those who do not choose this option will retain the 3% compounded COLA but will have their pensionable salary frozen. The "consideration model" is explained in more detail below in the Comment section.

COMMENT: Under HB 3305, employees may either make the election enumerated below to receive pay raises that will count as "pensionable salary," or agree to receive a raise on the condition that the increase cannot be included in the calculation of pensionable salary.

Consideration model: Tier 1

- Each Tier 1 employee participating in the General Assembly, State Employees, State Universities, Downstate Teachers, and Chicago Teachers Pensions shall make an election to either:
 - a. agree to delay automatic annual increases until the earlier of the attainment of age 67 or the fifth anniversary of retirement, and to have the amount of automatic annual increases in their annuity be calculated at the rate of 3%

or one-half (but not less than zero) the consumer price index-u of their originally granted annuity. If the consumer price index-u is zero or negative, no increase is granted. If a Tier 1 employee makes the foregoing election, they shall receive a “consideration payment” equal to 10% of the contributions made by or on behalf of the employee before the effective date of that election; or

- b. elect not to agree to the above terms. Each future increase offered to a Tier 1 employee shall be offered expressly on the condition of not counting towards the employee’s salary in regard to pension calculations.
- The foregoing election would then apply to all salary increases granted on or after June 30, 2022 (June 30, 2023 for SERS).
- The “consideration choice’ election must be made by Tier 1 employees between January 1st and March 31st, 2022 (between January 1st and March 31st 2023 for SERS).
- If no election is made for any reason, the employee will be deemed to have refused the delayed and reduced cola, i.e., rejected the "consideration model."

Recertification of FY 2023 Contributions (FY 2024 for SERS)

- HB 3305 requires the systems to recertify the FY 2023 State pension contributions on two separate occasions. The first recertification would occur on or before May 1, 2022, and would reflect the effect on the pertinent system’s liabilities as a result of the Consideration Model elections. The second recertification would occur on or before October 1, 2022, and would require a reduction in State contributions to each system equal to the amount of the 10% “consideration payments” for those Tier 1 members who have agreed to a delayed and reduced COLA. (For SERS, the first recertification would occur on or before May 1, 2023, and the second certification would occur on or before October 1, 2023.)

Tier 1 Contribution Changes

The chart below outlines the changes in employee contributions for Tier 1 members who accept the "consideration model." Those who refuse will see no change to the employee contribution rates currently enshrined in statute.

Note – under SERS, “covered” refers to those employees who are coordinated with and pay into Social Security. Those who are “non-covered” do not pay into Social Security.

HB 3305 Potential Changes to Contributions			Employee Election	Retirement Annuity	Cost-of-Living-Increase (COLA)	Survivor's & Children Benefits	Total
General Assembly:			Accepted	8.50%	0.00%	1.85%	10.35%
			Refused	8.50%	1.00%	2.00%	11.50%
State Employees:	Regular Formula	Covered	Accepted	3.15%	0.00%	0.45%	3.60%
			Refused	3.50%	0.00%	0.50%	4.00%
		Noncovered	Accepted	6.30%	0.00%	0.90%	7.20%
			Refused	7.00%	0.00%	1.00%	8.00%
	Alternative Formula	Covered	Accepted	7.20%	0.00%	0.45%	7.65%
			Refused	8.00%	0.00%	0.50%	8.50%
		Noncovered	Accepted	10.35%	0.00%	0.90%	11.25%
			Refused	11.50%	0.00%	1.00%	12.50%
	Security Employees	Covered	Accepted	10.80%	0.00%	0.45%	11.25%
			Refused	8.00%	0.00%	0.50%	8.50%
		Noncovered	Accepted	10.35%	0.00%	0.90%	11.25%
			Refused	11.50%	0.00%	1.00%	12.50%
State Universities:		Non-Police	Accepted	6.50%	0.00%	0.70%	7.20%
			Refused	6.50%	0.50%	1.00%	8.00%
		Police & Fire	Accepted	8.00%	0.00%	0.55%	8.55%
			Refused	8.00%	0.50%	1.00%	9.50%
Downstate Teachers:			Accepted	7.50%	0.00%	0.60%	8.10%
			Refused	7.50%	0.50%	1.00%	9.00%
Chicago Teachers:			Accepted	7.50%	0.00%	0.60%	8.10%
			Refused	7.50%	0.50%	1.00%	9.00%

Actuarial Analysis: The Commission's actuary, Segal Consulting, conducted an actuarial impact study on the Consideration Model in May of 2018. The analysis concluded that younger members with fewer years of service and many years until retirement would be most likely to accept the proposal, while older members with a long service record who are close to retirement would be most likely to refuse the consideration offer. Segal assumed that all Tier 1 members would make the choice that would maximize their individual wealth.

Under the "wealth maximization" approach, 32% of TRS Tier 1 members are expected to accept, and 68% to decline. 44% of SERS Tier 1 members are expected to accept, and 56% to decline. 39% of SURS Tier 1 members are expected to accept, and 61% to decline. Based on these assumptions, the 10% consideration payments for each fund are estimated to be \$144,000,000 for TRS, \$80,000,000 for SERS, and \$125,000,000 for SURS. Finally, each fund is expected to see a reduction in State contributions through FY 2045. ***Segal notes that inasmuch as the foregoing rates of acceptance and refusal of the consideration model were calculated in 2018, it can be assumed that fewer Tier 1 members would accept the Consideration Offer and more would refuse it, inasmuch as the Tier 1 population has aged by 3 years since the 2018 study. An updated actuarial study would be needed to assess the effect of the “wealth maximization” choice based on FY 2020 actuarial data.***

Under the 2018 study, TRS was expected to see a nominal reduction in State pension contributions through 2045 of \$5.32 billion, or \$2.62 billion based on present value. SERS was expected to see a nominal reduction of \$1.76 billion, or \$0.82 billion based on present value, and SURS was expected to see a nominal reduction of \$0.70 billion or \$0.46B based on present value.

Below are charts outlining the actuarial assumptions used to calculate the savings using the "wealth maximizing" choice, and estimates of long-term State contribution savings that correspond with the rates of acceptance and refusal of the Consideration Model as shown below.

Please note – this actuarial study of the “Consideration Model” was conducted in May of 2018, and was based upon the systems’ annual actuarial valuations as of June 30, 2017. An updated actuarial study would be required to assess the fiscal impact of HB 3305 using FY 2020 actuarial data.

Assumed Election Rates		
	Choice 1 (Accept)	Choice 2 (Refuse)
TRS	32%	68%
SERS	44%	56%
SURS	39%	61%

Consideration Choice Characteristics		
Characteristics	Choice 1	Choice 2
Age	Younger	Older
Years of Service	Lower service	Higher service
Proximity to Retirement	Many years in the future	Near retirement

Reduction in State Contribution		
System	Nominal Increase/(Reduction) in State Contribution Through FY 2045	Present Value of Increase/(Reduction) in State Contribution Through FY 2045
TRS	(\$ 5.32B)	(\$ 2.62B)
SURS	(\$ 0.70B)	(\$ 0.46B)
SERS	(\$ 1.76B)	(\$ 0.82B)

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