Commission on Government Forecasting and Accountability

PENSION IMPACT NOTE
103^{RD} General Assembly

BILL NO: **HB 4873** February 29, 2024

SPONSOR (S): Kifowit

SYSTEM: Five State-funded Retirement Systems (SERS, SURS, TRS, JRS, and GARS), Chicago Teachers' Pension Fund (CTPF), and Illinois Municipal Retirement Fund (IMRF)

FISCAL IMPACT

An actuarial study is being conducted on the major provisions of HB 4873. An updated impact note will be issued when the study is complete.

SUBJECT MATTER: HB 4873 is a pension reform omnibus bill that adjusts various components of the Tier 2 benefit structure of the five State-funded Retirement Systems, the Chicago Teachers' Pension Fund, and the Illinois Municipal Retirement Fund. Each change is summarized below in the Comment Section.

COMMENT:

***All provisions of HB 4873 outlined below would become effective July 1, 2025.**

Increasing the Tier 2 Pensionable Salary Cap to Social Security Wage Base in SERS, SURS, TRS, GARS, JRS, & the Chicago Teachers' Pension Fund (CTPF)

Current Law

- Currently, the Tier 2 pensionable salary cap is equal to $125,773.73.
  - Members do not make contributions on wages above the cap.
- The Tier 2 cap is increased annually by the lesser of:
  - 3%; or
  - ½ the increase in CPI-U for preceding 12 months.
    - If CPI-U = 0, no increase is paid.

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Under HB 4873, the Tier 2 pensionable salary cap for the State Systems and CTPF is brought into line with the Social Security Wage Base, which as of 2024 is $168,600. The bill provides a 3-year "ramp" from the current Tier 2 pensionable salary cap to the Social Security Wage Base, to take place during Calendar Years 2026 – 2029. Beginning on Jan. 1, 2029, the Tier 2 pensionable salary cap will be equal to the Social Security Wage Base.

- The bill specifies that the "wage base adjustment" shall mean the product that results from multiplying the difference between the federal Social Security Wage Base for the coming calendar year and the then-current Tier 2 pensionable salary cap by the "smoothing factor" for that calendar year, as shown below:
    1. For calendar year 2026, 25%;
    2. For calendar year 2027, 50%; and
    3. For calendar year 2028, 75%.

Change to the Tier 2 Automatic Annual Increase for SERS, SURS, TRS, JRS, GARS, & CTPF

Current Law

- SERS, SURS, TRS, & CTPF Tier 2 automatic annual increases are calculated at the lesser of:
    - A simple 3%; or
    - ½ the annual unadjusted percentage increase (not less than zero) in the CPI-U.
    - If the increase in CPI-U is 0, no increase is payable
- JRS & GARS Tier 2 automatic annual increases are calculated at the lesser of:
    - A compounded 3%; or
    - The annual unadjusted percentage increase in the CPI-U.

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- Beginning January 1, 2026, both active and retired Tier 2 members of SERS, TRS, SURS, GARS, JRS and CTPF shall receive their annual increase starting on the January 1 occurring after the first anniversary of the member's annuity start date (GARS members may receive their annuity in July if it occurs first following the first anniversary of retirement).
- The COLA change is prospective only; the bill does not provide for a recalculation of any Tier 2 COLAs already paid.

Accelerated Pension Benefit for GARS, JRS, & CTPF

Current Law

- PA 100-0587 implemented an accelerated pension benefit payment in lieu of any pension benefit for SERS, SURS, & TRS ("Total Buyout"), as follows:
    - Inactive vested Tier 1 & Tier 2 members may elect to receive an accelerated pension payment equal to 60% of the present value of the member's pension benefits in lieu of receiving a traditional retirement annuity.
- PA 100-0587 also established an accelerated pension benefit for a reduction in annual Tier 1 retirement annuity and survivor's annuity increases in SERS, SURS, and TRS ("COLA Buyout"), as follows:
    - A member may elect to receive a lump sum payment equal to 70% of the difference of the present value of the Tier One 3% compounded COLA and the present value of a reduced COLA (simple 1.5%); and
    - Annual increases begin on the January 1 occurring on or after the first anniversary of retirement.
- If an eligible member returns to service, all benefits earned are based solely on service after returning; the accelerated payment may not be repaid and credit cannot be reinstated.
- P.A. 102-0718 extended the sunset date of the two buyout programs to June 30, 2026.

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- HB 4873 establishes both a "Total Buyout" and "COLA Buyout" plan within GARS, JRS, and CTPF;
- The buyout plans mirror the existing plans in SERS, SURS, & TRS, **except** that:
    - Funding for the buyout programs will come from the General Revenue Fund and not from proceeds from the State Pension Obligation Acceleration Bonds, as is the case with the existing buyout programs; and
    - The reduced COLA under the COLA Buyout plan is payable on the first anniversary of retirement or age 67, whichever is later.
- HB 4873 establishes June 30, 2027 as the sunset date for the GARS, JRS, and CTPF buyout programs.

Deferred Retirement Option Plan (DROP) for SERS, SURS, TRS, CTPF, IMRF, and Downstate Fire & Downstate Police

DROP Explanation

- Deferred Retirement Option Plans (DROP) are designed to encourage continued employment past the eligible retirement age for a period of time (usually 3-5 years); below is a summary of the salient features of DROP plans:

  - o Workers continue to draw a salary but are considered retired (for annuity purposes);
  - o The pension annuity amount the worker is entitled to starting at the date they are considered "retired" (DROP date) is credited to the member's individual DROP account; and
  - o Upon completion of the DROP period, the member's DROP account balance is available as lump-sum amount, which can be distributed in any of the following ways:
    - a one-time payment;
    - a payment plan over time;
    - a payment rolled into an IRA.

HB 4873 DROP Provisions

- No later than January 1, 2026, a DROP plan will be made available in SERS, SURS, TRS, CTPF, Downstate Police & Fire, and IMRF for both Tier 1 and Tier 2 members. Eligible participants must meet the following criteria:
  - o The member must be eligible to retire with a full and unreduced pension as determined by the pertinent system;
  - o The member must not be in receipt of a disability or retirement annuity at the time of election;
  - o The member must be actively employed in a position that is covered under a collective bargaining agreement; and
  - o DROP participants must make active member contributions to the pertinent fund for the entirety of the DROP period. DROP participants do not accrue additional service credit during the DROP period.
- Participation in the DROP must be elected by the eligible members no later than January 1, 2029 and is irrevocable, unless:
  - o The DROP participant terminates employment prior to the expiration of the designated DROP period;
  - o The DROP participant becomes eligible for and begins collecting a disability benefit from the pension fund or retirement system;
  - o The death of the DROP participant occurs during the designated DROP period;
- The DROP duration is not to exceed 5 years.
- The State Treasurer will maintain individual DROP accounts for the State Systems plus CTPF. Individual DROP accounts for Downstate Fire & Police and IMRF participants will be maintained by the pertinent fund, unless administrative responsibility of the DROP is transferred to the State Treasurer through an affirmative vote of the board of trustees of the fund.
- Individual DROP accounts shall consist of:
  - o The monthly retirement annuity the participant would have been eligible to receive if the participant had terminated service on the date of participation in the DROP, as well as any benefits from a reciprocal system;
  - o Employee contributions paid by the participant during the DROP period; and

- Any auto-increases the member would have been eligible to receive if the participant had terminated service on the date he or she entered the DROP.
- Upon expiration or termination of the member's participation in the DROP, the member will receive the retirement annuity that they would have received had they retired on the date they entered the DROP with applicable automatic increases accrued during the DROP duration, plus the balance in their individual DROP account.
    - Expiration or termination of a DROP member's participation in the DROP may not occur after January 1, 2034.

Additional Funding to Pension Unfunded Liability Reduction Fund

HB 4873 amends the General Obligation Bond Act, such that every fiscal year after all bonds authorized by PA 93-0002 are retired in FY 2033, the State Comptroller shall order and the State Treasurer shall transfer $500 million from the General Revenue Fund to the newly created Pension Unfunded Liability Reduction Fund for each fiscal year (as of January 31, 2024, $9.92 billion of debt service from the 2003 POB issuance was outstanding). This fund shall be used to make additional contributions to the five State-funded systems plus CPTF based on the pro rata share of the State's annual obligation to each pension fund relative to the total contribution to all 6 pension funds for the ensuing fiscal year.

Pursuant to P.A. 100-0465, which became effective on August 31, 2017, the State currently pays an amount equal to the CTPF employer normal cost on an annual basis. Under the Act, these State contributions to CTPF began in FY 2019.

Closure of GARS & JRS in 2027

HB 4873 closes the window to join GARS & JRS after Jan 13, 2027; active participants in GARS & JRS may elect to terminate participation in the system and transfer up to 10 years of accumulated service credit from GARS or JRS to SERS. The payment amount required for such service credit transfers will be equal to the amount of employee and employer contributions that would have been required had the member participated in SERS, plus interest at the service credit purchase rate of 6.5% from the date of service to the date of payment, and those contributions must be paid no later than 10 years after the election.

HB 4873 also allows active participants in GARS & JRS to elect to terminate **all** participation in the system and transfer all credits and creditable service to SERS upon payment of an amount equal to:

- The difference between the actual funds transferred and the employer & employee contributions that would have been required had they participated in SERS during the period, plus interest at the 6.5% service credit purchase rate; and
- 6.5% interest thereon from the start date of participation in SERS to the date of payment.

Adjustment of Tier 2 Age & Service Requirements in SERS, SURS, TRS, & CTPF

Current Law

- A Tier 2 member or participant is entitled to a retirement annuity upon written application if he or she has attained age 67 and has at least 10 years of service credit. Tier 2 members are eligible to retire at age 62, with annuities reduced by ½ of 1% for each month under age 67.

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- The bill makes changes to the age at which Tier 2 members in SERS, SURS, TRS, and CTPF may retire with an unreduced annuity, as follows:
  - Age 62 with at least 35 years of service credit;
  - Age 64 with at least 20 years of service credit;
  - Age 67 with at least 10 years of service credit.
- The early retirement reduction for Tier 2 members who retire at age 62 under current law would remain in force.
- Beginning July 1, 2025, a Tier 2 member of the SURS system with twenty years of service as a police officer or firefighter is entitled to an unreduced retirement annuity at age 55. This change would bring the retirement age for Tier 2 SURS public safety personnel into line with the retirement age granted to Tier 2 police officers in SERS under P.A. 102-0719, which took effect on May 6, 2022.

Alternative Formula Eligibility for Investigators/Security Employees of the Departments of Lottery and Human Services

Current Law

The chart below details the current SERS Alternative Formula eligibility status of security employees and investigators employed the Department of Human Services and the Illinois State Lottery:

Alternative Formula Participation for Security Employees of the Departments of Human Services and Lottery		
Security Employee / Investigator for:	**Tier 1**	**Tier 2**
Department of Human Services	Yes	No
Department of the Lottery	No	No

The current retirement requirements for the above-mentioned employees are detailed in the chart on the next page:

Retirement Requirements for Employees Currently Ineligible for the Alternative Formula						
Employee	**Tier**	**SS-Coordinated?**	**Contribution Rate**	**Multiplier**	**Full Retirement**	**Reduced Retirement**
DHS Security Employee	2	Yes	4%	1.67%	Age 67 with 10 years service credit	Ages 62-67 with 10 years (Reduced 1/2 of 1% every year under age 67)
Investigator for the Dept. of Lottery	1	No	8%	2.20%	Age 60 with 8 years of service credit OR Rule of 85	Ages 55-60 with 25-30 years (Reduced 1/2 of 1% every year under age 60)
Investigator for the Dept. of Lottery	2	No	8%	2.20%	Age 67 with 10 years service credit	Ages 62-67 with 10 years (Reduced 1/2 of 1% every year under age 67)

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HB 4873 amends the Illinois Pension Code to allow participation in the SERS Alternative Formula for Tier 1 and Tier 2 investigators for the Department of the Lottery, and for Tier 2 DHS security employees

HB 4873 allows affected Department of Human Services (DHS) Tier 2 security employees to convert up to 12 years of regular formula service credit as a Human Services security employee into alternative formula service no later than 2 years after the effective date of the bill. Members must pay an amount equal to the difference between the employee contributions for that period of service and the amounts that would have been contributed had the member been participating in the alternative formula, plus interest at the service credit purchase rate of 6.5%, compounded annually, from the date of service to the date of payment. The bill does not require the payment of the employer's normal cost for the periods of regular formula service that the member wishes to upgrade.

Alternative Formula Participation for Certain Security Employees of the Department of Juvenile Justice

Currently, in order for a security employee of the Department of Juvenile Justice to participate in the SERS alternative formula, the employee must be employed in a position at a DJJ facility and have involvement in areas such as training of delinquent youths, providing rehabilitative and vocational training, and assisting other personnel who perform these duties. Additionally, the employee must:

- Be over the age of 21; and
- Possess a high school diploma or equivalent and either:
    - A bachelor's or advanced degree from an accredited college or university; or
    - 2 or more years of experience providing direct care to youth in the form of residential care, coaching, case management, or mentoring.

HB 4873 stipulates that the bachelor's or advanced degree requirement shall no longer determine eligibility for the alternative formula for the above-mentioned positions at DJJ. Affected employees may convert their prior regular formula service to alternative formula service by paying the difference between the employee contributions for that period of service and the amounts that would have been contributed had the member been participating in the alternative formula from the date of service to the date of payment. The member is not required to pay the employer's normal cost nor interest for the period of service they wish to upgrade.

Placing Downstate Police & Fire Articles Under the Ambit of the Retirement Systems Reciprocal Act

Current Law

Under current law, the Downstate Police and Downstate Firefighters' Articles of the Illinois Pension code are not included under the Retirement Systems Reciprocal Act, although reciprocity exists between the funds within each respective article (e.g., members of Downstate police funds can utilize reciprocity with other Downstate Police Funds). The Retirement Systems Reciprocal Act allows for active employees to combine service credit earned from various participating systems to apply towards the minimum vesting requirements of the fund that they participate in currently or the fund that they last participated in before terminating active service. For example, a Tier 2 member in IMRF could utilize reciprocity and combine 4 years of prior service in SERS and 6 years in IMRF to meet the 10-year Tier 2 vesting requirement in IMRF.

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HB 4873 would place the Downstate Police and Downstate Firefighters' Articles of the Illinois Pension Code under the ambit of the Reciprocal Act. The bill states that participation under the Reciprocal Act would only apply to members who have not yet begun receiving retirement annuities as of the effective date. In other words, retired members would not be entitled to a recalculation of their pensions based upon reciprocal service.

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