COMMISSION ON GOVERNMENT FORECASTING AND ACCOUNTABILITY

PENSION IMPACT NOTE

97TH GENERAL ASSEMBLY

BILL NO: **SB 1673, as amended by HA 5** June 21, 2012

SPONSOR(S): Raoul (Madigan - Nekritz, et al.)

SYSTEM(S): General Assembly Retirement System (GARS), Illinois Municipal Retirement Fund (IMRF), State Employees Retirement System (SERS), State Universities Retirement System (SURS), Teachers Retirement System (TRS)

FISCAL IMPACT: COGFA's actuary has completed a cost study of how the major provisions of SB 1673, as amended by HA 5, will impact the State Universities Retirement System. COGFA's actuary found that between FY 2014 – 2045, the bill will reduce State contributions by $10.9 billion. This savings projection assumes that 50% of Tier 1 members and retirees will accept the reduced COLA. A comparison of State contributions to SURS under this proposal vs. current law can be seen in the charts enclosed under Appendix A.

In a cost study provided by SURS' actuary, the major provisions of SB 1673, as amended by HA 5, were projected to reduce State contributions by $10 billion between FY 2014 – 2045. This study also assumed that 50% of Tier 1 members and retirees would elect to take the reduced COLA. COGFA's actuary notes that his projected savings do not differ significantly from the projections of SURS' actuary; therefore, there is a high probability that the total reduction in State contributions to SURS as a result of this bill will fall between $10 billion and $10.9 billion over the period between FY 2014 and FY 2045, assuming that the State makes its required annual statutory contribution.

Total Reduction in State Contributions State Universities Retirement System FY 2014 - FY 2045	
SURS Actuary	$10.0 Billion
COGFA Actuary	$10.9 Billion

SUBJECT MATTER: SB 1673, as amended by HA 5, amends the Pension Code by creating an irrevocable election for active and retired members of GARS, SERS, SURS, and TRS. This bill outlines consequences for each individual active or retired member and, depending on the elections of active members, establishes a long-term, actuarially-based funding schedule for each retirement system. This bill also establishes and provides rules for the implementation of a Cash-Balance Plan.

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COMMENTS:

Active Members & Retirees: Under current law, Tier I members of GARS, SERS, SURS, and TRS are entitled to a defined-benefit pension plan with a retirement annuity calculated on their respective final average salaries. This Tier 1 retirement annuity includes automatic compounded annual increases (COLA) of 3%. Members who have met the requisite service requirements under the State Employees Group Insurance Act are additionally entitled to a retiree healthcare subsidy.

SB 1673, as amended by HA 5, establishes an irrevocable election for Tier I active and retired members in GARS, SERS, SURS, and TRS. Current members have from January 1, 2013 until May 31, 2013 to choose amongst the following options:

i) Current members, both active and retired, may elect to maintain eligibility for the retiree healthcare subsidy. By selecting this option, the member reduces their COLA to the lesser of 3% or ½ of the CPI-U of the previous year of the originally-granted annuity and may have to make required contributions towards the healthcare subsidy. Additionally, the active member, upon retirement, may not receive any COLA until either the age of 67 or the January after the fifth anniversary of first receiving the retirement annuity, whichever occurs sooner.
    a. A retired member making this election may not receive a COLA until the earlier of either the age of 67 or the January after the fifth anniversary of first receiving the *original* retirement annuity. Additionally, the revised Tier 1 COLA will be calculated upon the member's original pension; however, any applicable prior years' COLA's remain in force.

ii) Current members, both active and retired, may elect to maintain the 3% compounded COLA. By selecting this option, the member forfeits the retiree healthcare subsidy. Additionally, the member's final average salary will not take into account any future increases in income received after July 1, 2013.

Employer Contributions: SB 1673, as amended by HA 5, stipulates that, in concordance with Central Management Services, GARS, SERS, SURS, and TRS will each evaluate the election results within each system.

If more than 50% of active members retain their healthcare subsidy and reduce their COLA, then each system will adopt a new, 30-year actuarially-required contribution (ARC) funding schedule starting in FY 2014 and going through FY 2043. Such a contribution shall be calculated as a level percentage of payroll and shall be deteremined under the Projected Unit Credit (PUC) actuarial cost method.

If less than 50% of the active members of GARS or SERS individually elect to take the lesser COLA and secure their retiree healthcare subsidy, then that retirement system will maintain its current funding schedule of reaching 90% funded by FY 2045. If less than 50% of the active members of SURS and TRS individually elect to take the lesser COLA and secure their retiree healthcare subsidy, then that retirement system will still adopt a new actuarially-based long-term funding schedule with the goal of being 100% funded by FY 2045 (for more details, see below).

Regardless of the election results, each system will make the following changes:

GARS and SERS: The state contribution into the pension fund will be equal to the sum of 1) the State's portion of the projected normal cost for that fiscal year, plus 2) an amount sufficient to bring total assets of the system up to the designated funded ratio by the end of the funding schedule.

SURS and TRS: Each individual employer, university, community college, school district, etc, will begin to provide SURS or TRS, respectively, with the employer contribution, while the State makes supplemental contributions on behalf of the employers. Each *employer* will make an employer contribution to their appropriate system of an amount equal to the sum of 1) the normal cost for that fiscal year for employees hired before July 1, 2013 on a ramped-up, percentage of payroll basis, plus 2) the normal cost for employees hired *after* July 1, 2013, plus 3) an amount sufficient to amortize any unfunded liabilities accrued after July 1, 2013 on a 30-year rolling amortization schedule. The portion of the employer contribution accounting for employees hired *before* July 1, 2013 will start at 1% of payroll in FY 2014, increasing at 1% of payroll each year through FY 2019, and then only increasing at .5% of payroll each following fiscal year until the employer contributes 100% of the normal cost for these employees. From FY 2014 through the end of the funding schedule, the State shall make a contribution equal to the sum of 1) an amount sufficient to amortize all liabilities accrued before July 1, 2013, plus 2) the normal cost for any employees whom the State directly employs, plus 3) an amount to complement the employer contribution of the normal cost of employees hired before July 1, 2013, such that, between the State and the employer, 100% of the normal cost is paid. Once the State has has amortized 100% of the total liabilities accrued by July 1, 2013, the State will no longer contribute on behalf of the employers.

Cash-Balance Plan: SB 1673, as amended by HA 5, also creates a Cash-Balance Plan and an Optional Cash Balance Plan. Within SURS and TRS, members joining on or after July, 1st, 2013 will be enrolled in the Cash-Balance Plan, while any Tier II members have the exclusive option to opt in as well. This Cash-Balance pension benefit will replace the Tier II pension the members would normally receive upon retirement. These participants will make the same employee contribution as they would under their original retirement system, and the employer will match 4.4% of salary for SURS participants and 3.4% of salary for TRS participants. Interest on all accounts will be referred to as the "assumed treasury rate," a rate equal to the average annual yield of the 30-year U.S. Treasury Bond of the previous year, and will be charged at a credit of between 4% and 10%. For any given year, an account may earn no less than 4% interest; however, it will only make 2/3 of the investment returns over 4% *on the condition* that the last 5 year average assumed treasury rate is not less than 4% as well. The retirement annuity, including any subsequent 3% COLA's calculated on the originally-granted pension, will be calculated under the assumption that the retiree's notional account will reach $0 by their actuarially assumed date of death or by the death of their eligible survivor.

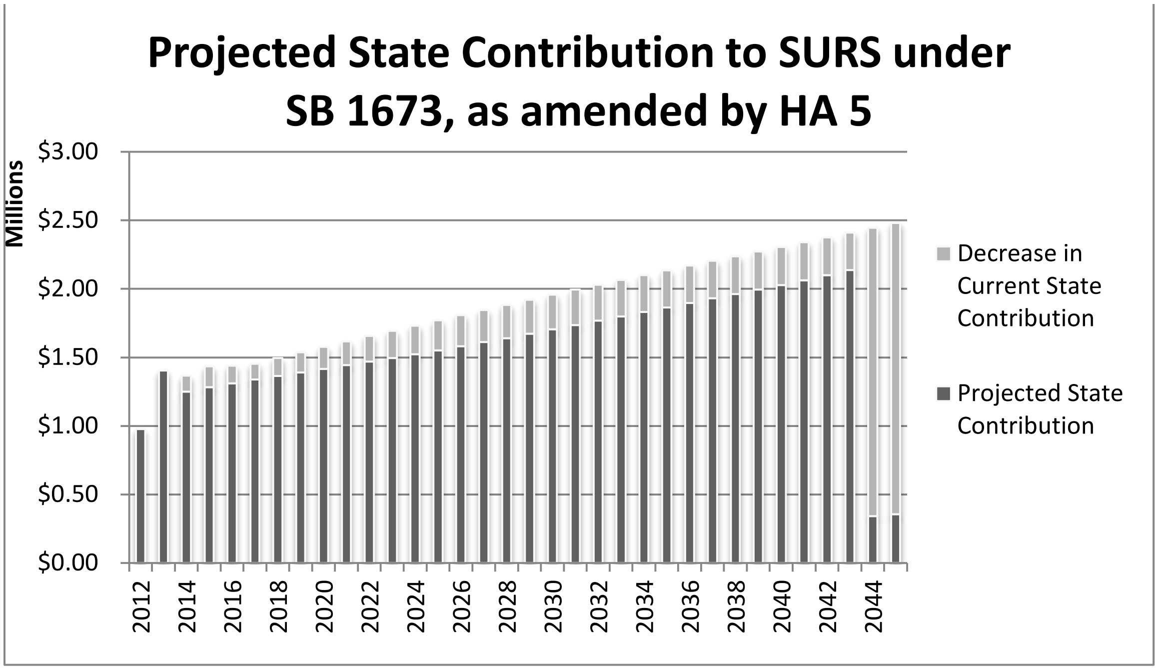
The Optional Cash-Balance Plan, as proposed by this bill, is available to all SERS members who opted for the revised COLA as well as all participants of the Cash-Balance Plan. Participation in the Optional Cash-Balance Plan is in addition to, not in lieu of, any other pension benefit. Participation consists of employee contributions of an additional 2% of salary. These employee contributions, along with any interest credited in the same fashion as the Cash-Balance Plan, are the sole source of income for notional account holders. No employer contribution to the Optional Cash-Balance Plan is required. Annuities will be paid out in the same fashion as annuities under the Cash-Balance Plan.

Miscellaneous: SB1673, as amended by HA 5, also provides more narrow definitions of an employee under IMRF, SURS, and TRS by excluding certain employers who operate outside the auspices of school districts, universities, and municipalities. These provisions only apply to new hires and not to any existing employees of these employers.

This bill disallows any member of SURS from receiving service credit for a leave of absence for service with a teacher organization occurring after the effective date of this bill.

This bill also disallows members of SERS hired after the effective date of this bill to earn service credit for payment or reimbursement from travel vouchers. Nor does this bill allow for members of TRS hired after the effective date of this bill to claim credit for unused sick time.

Appendix A: COGFA's actuary found that between FY 2014 – 2045, SB 1673, as amended by HA 5, will reduce State contributions to SURS by $10.9 billion.



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