ROBBINS SCHWARTZ
NICHOLAS LIFTON & TAYLOR, LTD.

In Brief

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PENSION CHANGES TO AFFECT ARTICLE 3 AND ARTICLE 4 PENSION FUNDS

On December 30, 2010, Governor Quinn signed Senate Bill 3538 into law (P.A. 96-1495, the "Act"), completing Illinois' pension reform for 2010, which has effected changes in all of the pensions provided for under Illinois' Pension Code beginning January 1, 2011.[1]

CHANGES TO PENSION BENEFITS

The Act, which also affects Chicago Police and Fire pensions, makes the following changes affecting new Article 3 and Article 4 fund members (those joining a fund after January 1, 2011):

- Minimum Retirement Age increased to 55 with a minimum of 10 years of service.
- Retirement pension calculated by multiplying 2.5% for each year of service by the "Final Average Salary," capped at 75%.
- Early Retirement Option at age 50 with a minimum of 10 years of service, but a reduction in annuity of 1/2 of 1% for each month under age 55 (6% per year).
- "Final Average Salary" (used to determine pension annuity) is based on an average salary based on the best 8 out of the last 10 years of service.
- Final Average Salary is capped at $106,800, increased annually by the lesser of 3% (of the salary amount) or 1/2 of the annual increase in the CPI-U.[2]
- Survivor benefits reduced to 66-2/3% of deceased employee's salary at time of death (subject to cost of living adjustments).
- Cost of living adjustments beginning the year after the retiree or survivor turns age 60 with annual increases of the lesser of 3% or 1/2 of the annual increase in the CPI-U.

The measures set forth in P.A. 96-1495 do not affect pension benefits for those already participating in an Article 3 or Article 4 fund. However, the changes will be effective for any member who joins a fund after January 1, 2011.

EXPANDED INVESTMENT OPPORTUNITIES FOR CERTAIN FUNDS

P.A. 96-1495 also provides expanded investment opportunities into corporate bonds and equity holdings. All funds are now permitted to invest in:

- Pooled interest-bearing accounts or funds of the Illinois Metropolitan Investment Funds; and
- Investment grade corporate bonds managed through an investment advisor.[3]

In addition, Article 3 and Article 4 funds with net assets of $10,000,000 or more are now permitted to invest an additional portion of assets in common

[1] P.A. 96-0889, signed into law in April 2010, made similar changes to all other Articles of the Pension Code.

[2] Measuring the change in prices for goods/services purchased by urban consumers.

[3] If corporate bonds are downgraded below investment grade, they must be liquidated within 90 days.

and preferred stocks and mutual funds. Previously, larger pension funds were limited to investing only 45% of the fund assets in equity holdings. Under the Act, for funds with at least $10,000,000 in net assets, the limit is initially extended to 50% and then to 55% on July 1, 2012.

- The stocks must be:
  - Listed on a national exchange or board of trade, and
  - Of a corporation in existence for at least 5 years.
- The mutual funds must have net assets of at least $250,000,000 and must be:
  - Managed by an investment company,
  - In operation for at least 5 years, and
  - Comprised of a diversified portfolio of common or preferred stocks, bonds, or money market instruments.

The additional investments, when combined with the other equity holdings of the fund, must not exceed 50% of the fund's net present assets as of July 1, 2011, and must not exceed 55% as of July 1, 2012.

CHANGES IN MUNICIPAL FINANCING

Certain provisions of the Act also provide needed relief to municipalities that struggle to meet annual police and fire pension funding obligations. Article 3 and Article 4 funds must now be 90% funded by 2040. Previously funds were required to be 100% funded by 2033. This adjustment should reduce the actuarially determined annual cost to be levied by the municipality.

Most notably, municipalities are now required to establish the annual pension levy based on an actuarial determination of the fund liabilities, as determined by the Department of Insurance actuarial report or another actuarial report obtained by either the fund or the municipality. The municipality must levy an amount that (when added to participant contributions) will equal a sum sufficient to meet the annual requirements of the fund, as determined by one of the actuarial reports.

In addition, P.A. 96-1495 includes provisions that will allow Article 3 and Article 4 funds to enforce municipal funding obligations beginning in 2016. The Act provides that if a municipality fails to transmit the required fund contributions for more than 90 days after payment of the contributions are due, the fund may, after giving notice, certify to the State Comptroller the amounts of delinquent payments. Upon receipt, the Comptroller must, beginning in FY 2016, deduct the delinquent amount from State grant funds allocated to the municipality and deposit those amounts in the fund. The portion of State grant funds available for this purpose is limited in 2016 and 2017 as follows:

- In FY 2016, the amount of the delinquent payment up to 1/3 of the total amount of any grants of State Funds to the municipality, and
- In FY 2017, the amount of the delinquent payment up to 2/3 of the total amount of any grants of State Funds to the municipality.

However, in FY 2018 and each year thereafter, all of the State grant funds may be diverted to the pension fund, up to the amount of the delinquent pension fund contributions.

COMMISSION ON GOVERNMENT FORECASTING AND ACCOUNTABILITY STUDIES TO BE REPORTED TO GENERAL ASSEMBLY BY DECEMBER 31, 2011

The new legislation also outlines a number of studies to be completed by the Commission on Government Forecasting and Accountability ("COGFA"). By December 31, 2011, COGFA must report on:

- Feasibility of an investment pool to supplement and enhance investment opportunities for Article 3 and Article 4 funds, and
- Enhancing cost-share components between the fund and the municipality.

In addition, for each Article 3 and Article 4 pension fund COGFA shall report by January 1, 2013 on the following:

- Fund balances,
- Historical employer contribution rates for each fund,
- The actuarial formulas used to determine employer contribution, including the rate of return,
- Available contribution funding sources,
- The impact of any revenue limitations caused by the Property Tax Extension Limitation Law ("PTELL") and employer home rule or non-home rule status, and
- Existing statutory funding compliance procedures and enforcement mechanisms for all municipal pension funds.

If you require additional information, please do not hesitate to contact any RSNLT employee benefits or municipal attorney.

Camille Cribaro-Mello, of the firm's Chicago office, prepared this *In Brief*.

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Robbins Schwartz Nicholas Lifton & Taylor, Ltd.
55 West Monroe Street | Suite 800 | Chicago, Illinois 60603 | 312-332-7760 | questions@rsnlt.com.