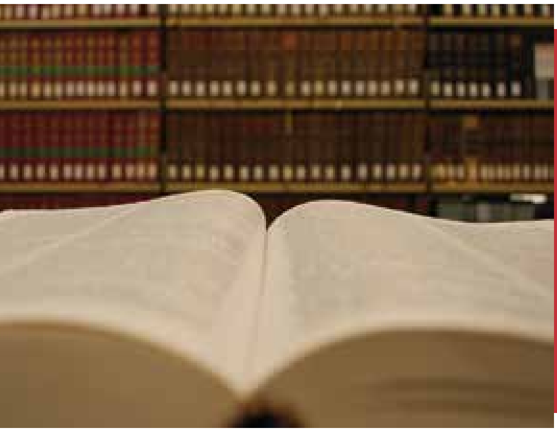
Pension Pointers



Overview of Public Act 101-0610 Firefighter and Police Pension Fund Assets Consolidation

By James G. Wargo
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On December 18, 2019, Governor J.B. Pritzker signed Public Act 101-0610 (the "Act"), which consolidates the State's 649 Article 3 and 4 firefighter and police pension funds and improves the pension benefits for Tier 2 members. The law consolidates the assets into two statewide investment funds: The **Police Officers' Pension Investment Fund** (40 ILCS 5/22B-101) and the **Firefighters' Pension Investment Fund** (40 ILCS 5/22C-101), which is the focus of this article. The Act does not impact or affect the City of Chicago's police and fire pension funds, which will continue to operate independently. Furthermore, local Article 3 and 4 pension funds will continue to exist and administer the benefits of the fund. The effective date of the Act is January 1, 2020.

What is the purpose of the consolidation?

The stated legislative purpose of the new law is "to streamline investments and eliminate unnecessary and redundant administrative costs, thereby ensuring more money is available to fund pension benefits for the beneficiaries" of Article 4 pension funds. (40 ILCS 5/22C-114)

What is the transition period under the Act?

The assets of Article 4 pension funds must be transferred to the Fire Consolidated Fund for management and investment no later than **July 1, 2022,** 30 months after the effective date of the Act. (40 ILCS 5/1A-102; 40 ILCS 5/22C-120)

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How will the Fire Consolidated Fund be governed?

The Fire Consolidated Fund will be governed by a board of trustees. The Governor must appoint a transition board of trustees in January consisting of nine members. The transition board members will serve until the initial permanent board members are elected and qualified. The transition board and the permanent board shall be fiduciaries for the participants and beneficiaries of the Fire Consolidated Fund and shall be required to discharge their duties solely in the interest of the participants and beneficiaries. (40 ILCS 5/22C-114 and 115)

What will be the composition of the transition board of trustees?

The nine members of the transition board will include:

- Three members representing municipalities and fire protection districts who are executive officers or officials of those governmental units, appointed from recommendations by the Illinois Municipal League;
- Three members representing participants, appointed from recommendations by a statewide fire labor organization;
- One member representing beneficiaries, recommended by a statewide fire labor organization;
- One member recommended by the Illinois Municipal League; and
- One member who is a participant, recommended by a statewide fire labor organization. (40 ILCS 5/22C-115)

What will be the composition of the permanent board of trustees?

The permanent board of trustees for the Fire Consolidated Fund will also consist of nine members comprised identically to the transition board. However, the permanent board will be elected, except for the two Governor appointees who are recommended by the Illinois Municipal League and the firefighters' union. (40 ILCS 5/22C-115)

Do the trustees receive any compensation?

Trustees will receive no salary for service on the board but shall be reimbursed for travel expenses incurred while on business for the board. (40 ILCS 5/22C-115)

Are there any ethical constraints on the trustees under the Act?

Trustees are not permitted to have any interest in any brokerage fee, commission, or other profit or gain arising out of any investment directed by the board.

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However, this prohibition does not preclude ownership by any member of any minority interest in any common stock or any corporate obligation in which an investment is directed by the board. (40 ILCS 5/22C-115) The new boards will also be subject to the other ethics statutes set forth in state law, most notably the Public Officer Prohibited Activities Act (50 ILCS 105/1 *et seq.*), the State Officials and Employees Ethics Act (5 ILCS 430/1-1 *et seq.*), and the Illinois Pension Code (40 ILCS 5/1-110).

How are the elections of board members to be administered?

The transition board shall administer the initial elections for the permanent board, which will occur within the first year, and the permanent board shall administer all subsequent elections. Each board shall develop and implement procedures for the conduct of the elections. (40 ILCS 5/22C-116)

All nominations for election shall be by petition:

- For trustees to be elected by the municipalities and fire protection districts that have participating pension funds, by at least 20 such mayors and presidents.
- For trustees to be elected by participants, by at least 400 participants.
- For trustees to be elected by the beneficiaries, by at least 100 beneficiaries.

The board will prepare and send out ballots and ballot envelopes to the participants and beneficiaries eligible to vote in accordance with the rules adopted by the board. In lieu of conducting elections via mail balloting, the board may instead adopt rules to provide for elections to be carried out solely via Internet balloting or phone balloting. The initial election for permanent trustees shall be held, and the permanent board shall be seated, no later than January 1, 2021. (40 ILCS 22C-116)

What is the term of office for the permanent board members?

The elected trustees shall each serve four-year terms, except the initially elected trustees' terms shall be staggered, with some of the trustees serving an initial term of two years. (40 ILCS 22C-116)

What happens if an elected member's status changes?

Any municipal or fire protection district trustee who ceases to serve in their executive role with the municipality or fire protection district shall not be eligible to serve as a member of the board and his or her position shall be deemed vacant. However, any trustee who was elected by the participants who ceases to be a participant may serve the remainder of the elected term. (40 ILCS 22C-116)

What if there is a trustee vacancy?

For a vacancy of an elected trustee occurring with an unexpired term of six months or more, an election will be conducted. Otherwise, the elected vacancy shall be filled by appointment by the board for the unexpired term. Vacancies among the appointed trustees shall be filled by appointment in a manner similar to the original appointments. (40 ILCS 22C-116)

What will be the process for transferring pension fund assets to the Fire Consolidated Fund?

The transfer of pension fund assets will be governed by the rules adopted by the state board of trustees and the statutory requirements set forth below. The board may retain the services of custodians, investment consultants, and other professional services it deems prudent to implement the transition of assets authorized under the Act.

Audit -- As soon as practicable, the board, in cooperation with the Illinois Department of Insurance (DOI), shall audit the investment assets of each transferor pension fund to determine a certified investment asset list for each local fund. The audit shall be performed by a certified accountant.

Certified investment asset list -- Upon completion of the audit, the board and the Department of Insurance shall provide the certified investment asset list to that transferor pension fund. Then, the board shall, within 10 business days or as soon as practicable, initiate the transfer of assets from the local fund. In order to maintain the accuracy of the certified investment list, the transferor pension fund shall not purchase or sell any of its pension fund assets after the asset list has been established.

Notice of intent to assume fiduciary control -- When the Fire Consolidated Fund is prepared to receive the pension fund assets from any transferor pension fund, the executive director shall notify in writing the board of trustees of that transferor pension fund of the Fund's intent to assume fiduciary control of those pension fund assets, and the date that the transferor pension fund will cease to exercise fiduciary responsibility. This letter shall be transmitted no less than 30 days prior to the transfer date. Upon receipt of the letter, the transferor pension fund shall promptly notify its custodian, as well as any and all entities with fiduciary control of any portion of the pension assets. Each transferor pension fund shall have sole fiduciary and statutory responsibility for the management of its pension assets until the start of business on the transfer date.

Transfer of assets -- At the start of business on the transfer date, statutory and fiduciary responsibility for the investment of pension fund assets shall shift exclusively to the Fire Consolidated Fund, and the Fund shall promptly and prudently transfer all such pension fund assets to the board of trustees and terminate the relationship with the local custodian of that transferor pension fund. The Fund shall provide a receipt for the transfer to the transferor pension fund within 30 days of the transfer date.

Post-transition audit -- Within six months after the end of the transition period, the books, records, accounts, and securities of the Fund shall be audited by a certified public accountant. This audit shall include, but not be limited to, the following: (1) a full description of the investments acquired, showing average costs; (2) a full-description of the securities sold or exchanged, showing average proceeds or other conditions of an exchange; (3) gains or losses realized during the period; (4) income from investments; and (5) administrative expenses incurred by the board. The audit report shall be published on the Fund's official website, if applicable, and filed with the DOI. (40 ILCS 5/4-123.2/40 ILCS 5/22C-120)

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What investment authority will individual pension funds have prior to and after the transition period?

The transferor pension funds will retain investment authority over its assets until the transfer of assets to the Fire Consolidated Fund. Upon transfer of its assets, the transferor pension fund shall not manage or control the assets and shall no longer exercise investment authority. However, the local funds may continue to maintain an interest-bearing account with a bank or financial institution for purposes of benefit payments and other reasonable expenses. (40 ILCS 5/22C-120; 40 ILCS 5/4-123 and 123.2; 40 ILCS 5/1A-102)

How will the Fire Consolidated Fund operate and be administered?

The Fire Consolidated Fund will be operated and administered by an executive director appointed by the board. The board may also appoint one or more custodians to facilitate the transfer of the pension assets during the transition period and enter into contracts for such services. The board may also appoint external legal counsel, an independent auditing firm, investment advisors, and other consultants as it determines to be appropriate and enter into contracts for such services. The executive director may also retain the services of other consultants, advisors, fiduciaries, and service providers as may be desirable. With the approval of the board, the executive director may employ professional and clerical personnel.

How are the assets for each local fund accounted for within the Consolidated Fund and how does each local fund obtain moneys to pay benefits?

The board shall separately calculate account balances for each participating pension fund. The operations and financial condition of each participating pension fund account shall not affect the account balance of any other participating fund. Also, investment returns earned by the Fire Consolidated Fund shall be allocated and distributed pro rata among each participating pension fund account in accordance with the value of the pension fund assets attributable to each fund. The board shall from time to time transfer moneys and other assets to the participating pension funds as required to pay expenses, benefits, and other required payments. (40 ILCS 5/22C-118)

What rulemaking authority does the Fire Consolidated Fund have?

The board is required to adopt rules to implement and properly administer the Fire Consolidated Fund. These rules must specifically provide for the transitions processes mentioned above, future transfers with local funds, and compensation and benefits of its employees. (40 ILCS 5/22C-119)

Will the DOI and the Fire Consolidated Fund have the authority to examine and investigate the participating pension funds?

Yes. Prior to the conclusion of the transition period, the DOI shall continue to make periodic examinations and investigations of Article 4 pension funds. After the conclusion of the transition period, the DOI may accept and rely upon a report of audit or examination of such pension fund made by an independent certified public accountant retained by the Fire Consolidated Fund. The Act also empowers the Fire Consolidated Fund to perform periodic examinations and investigations of the pension funds. (45 ILCS/1A-104)

How will the actuarially required employer contribution be determined in the future?

Prior to the conclusion of the transition period, actuarial statements may continue to be prepared using the method of calculating the required contribution for the fund that was in effect prior to the Act. The use of the word "may" in this provision suggests that there will continue to be flexibility to use actuarial assumptions and actuarial methodology that exceeds the "statutory minimum" approach of 90% funding by 2040 using projected unit credit (PUC) prior to the conclusion of the transition period. After the conclusion of the transition period, each actuarial statement shall be prepared by a qualified actuary retained by the Fire Consolidation Fund. In the preparation of such actuarial statements, if a change occurs in an actuarial or investment assumption that increases or decreases the required contribution for the pension fund, the change shall be implemented in equal amounts over a 3-year period. (40 ILCS 5/1A-111)

Will the Fire Consolidated Fund have expanded investment authority?

Once the Fire Consolidated Fund takes custody of transferred pension fund assets, the board shall have the authority to manage the assets for the purpose of obtaining a total return on investments for the long term. The pension fund assets of the Fund shall be maintained in accounts held outside the State treasury. The Act does not prohibit the board from directly investing pension fund assets in public market investments, private investments, real estate investments, or other investments authorized by the Pension Code. (40 ILS 5/22C-121) The Fire Consolidated Fund will have expanded investment authority and is not subject to any of the limitations applicable to the investments of the current firefighter pension funds under Sections 1-113.1 through 1-113.12 or Article 4 of the Pension Code.

Will the Fire Consolidated Fund be required to perform and issue financial reports?

The Fire Consolidated Fund will be on a July 1 to June 30 fiscal year and will be required to perform and issue the following financial reports to the participating pension funds:

Annual audit -- At least annually, the books, records, accounts, and securities of the Fund shall be audited by a certified public accountant in accordance with the rules and procedures promulgated by the Governmental Accounting Standards Board. The audit opinion shall be published as a part of the annual report of the Fund and shall be submitted to the transferor pension funds and the DOI.

Quarterly reports -- For quarterly periods ending September 30, December 31, and March 31, the Fund shall submit to the participating pension funds and the DOI a report providing, among other things, the following information:

- A full description of the investments acquired, showing average costs;
- A full description of securities sold or exchanged, showing average

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proceeds or other conditions of an exchange;

- Gains or losses realized during the period;
- Income from derived investments; and
- Administrative expenses.

Annual Report -- An annual report shall be prepared by the Fund for submission to the participating pension funds and the DOI within six months after the close of each fiscal year. The annual report shall include (besides the items noted above):

- Listing of the investments held by the Fund at the end of the year, showing their book values and market values and their income yields on market values;
- Comments on the pertinent factors affecting such investments;
- A review of the policies maintained by the Fund and any changes that occurred during the year;
- A copy of the audited financial statements for the year;
- Recommendations for possible changes governing the operations of the Fund; and
- A listing of the names of securities brokers and dealers dealt with during the year showing the total amount of commissions received by each on transactions with the Fund. (40 ILCS 5/22C-125)

What are the new training requirements for pension fund trustees?

Initial trustee certification training has been reduced to 16 hours (*formerly 32 hours*), including training in the following areas:

- Duties and liabilities of a fiduciary with respect to the administration and payment of pension benefits;
- Adjudication of pension claims;
- Trustee ethics;
- Illinois Open Meetings Act; and
- Illinois Freedom of Information Act.

Basic accounting and actuarial training are no longer included in the required training. Any trustee who completes the Open Meetings Act training under Section 1.05 of the Open Meetings Act (5 ILCS 120/1.05) is not required to participate in Open Meetings Act training in the initial 16-hour training program.

Pension fund consolidation training of four hours on the changes made by the Act is now required of current pension fund trustees elected or appointed on or before January 1, 2020. For Article 4 pension fund trustees, these training hours may be conducted by a pension fund or the DOI. This training is only required to be completed once by each trustee.

Annual trustee training is now eight hours (*formerly 16 hours*) each year after the first year that the trustee is elected or appointed under Section 1-109.3 of the Pension Code. (40 ILCS 5/1-109.3)

Are there any changes to the annual compliance fee?

After the conclusion of the transition period, the annual compliance fee for each pension fund shall be $8,000 and shall be paid by the Fire Consolidated Fund. Prior to the conclusion of the transition period, the annual compliance fee remains at 0.02% (2 basis points) of the total assets of the pension fund, not to exceed $8,000. (40 ILCS 5/1A-112)

Does the Act impact the ability of individual pension funds to adjudicate benefits?

Each pension fund shall retain the exclusive authority to adjudicate and award disability, retirement, and survivor benefits under the Pension Code. Furthermore, the Fire Consolidated Fund shall not have the authority to control, alter, or modify, or the ability to review or intervene in, the proceedings or decisions of the fund as otherwise provided in this Section. (40 ILCS 5/4-117.2)

What changes does the new law make to Tier 2 benefits?

The Act includes the following improved benefits for Tier 2 members:

"Final average salary" now means the greater of: (i) the average monthly salary obtained by dividing the total salary of the firefighter during the 48 consecutive months (*formerly 96 months*) of service within the last 60 months (*formerly 120 months*) of service in which the total salary was the highest by the number of months of service in that period; or (ii) the previous calculation.

Salary cap for pensionable salary. The salary cap for pensionable salary of $106,800 is now annually increased by the lesser of (i) 3% of that amount, including all previous adjustments, or (ii) the annual unadjusted percentage increase (*previously, one half*)(but not less than zero) in the Consumer Price Index-U for the 12 months ending with the September preceding each November 1, including all previous adjustments. There shall be no retroactive adjustment of any employee contributions. (40 ILCS 5/4-109)

Survivors' pension benefits for Tier 2 members. Survivors of Tier 2 members shall be entitled to a benefit in an amount that is equal to the greater of (*new*) 54% of the firefighter's monthly salary at the date of death (*new*), or (2) 66 2/3% of the firefighter's earned pension at the date of death.

If there is a surviving spouse, 12% of such monthly salary shall be granted to the guardian of any minor child or children until age 18. Upon the death of the surviving spouse leaving one or more minor children, or upon the death of a firefighter leaving one or more minor children but no surviving spouse, a monthly pension of 20% of the monthly salary shall be granted to the guardian of each such child until age 18. The total pension provided shall not exceed 75% of the monthly salary of the deceased firefighter under the following circumstances:

- When paid to the survivor of firefighter who has attained 20 or more years of service credit and who receives or is eligible to receive a retirement pension;
- When paid to the survivor of a firefighter who dies as a result of an illness or accident, or from any cause while in receipt of a disability pension; or
- When paid to the survivor of a deferred pensioner. (*new*)

The Act further provides that any changes made to these survivors' pension benefits apply without regard to whether the deceased firefighter was in service on or after the effective date of the Act. (40 ILCS 5/4-113 and 40 ILCS 5/4-114) ■