TOPICS & REPORT

Teachers' Retirement System of the State of Illinois
Spring 2014

New Pension Benefit Law for Tier I Members Effective on June 1, 2014

Affects all Tier I members who first contributed before Jan. 1, 2011 and all retired members

Despite controversies and court challenges, Illinois' new pension law is set to take effect on June 1, 2014.

In early March, four lawsuits challenging the law as a violation of the Illinois Constitution's pension protection clause were consolidated into one. The initial court arguments over the new law will begin later this year in Springfield.

If the law is upheld, it will affect the future cost-of-living adjustments of all Tier I active and retired members, as well as the initial pensions of Tier I active members.

The new law is designed to eliminate the retirement system's $55.7 billion unfunded liability by 2044. Eliminating the TRS unfunded liability would guarantee continuous pension payment for all generations of TRS members when they retire. With a funded ratio of 40.6 percent, TRS cannot currently make that guarantee for future retirees.

Because of decades of insufficient funding by the General Assembly, TRS has less than 41 cents on hand for every $1 promised to TRS members for future retirement benefits.

The court challenge could delay implementation of the law's provisions. TRS has no indication that the courts will delay the law. If a court does act, we will adhere to the court's decision.

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Director's Message

Executive Director Dick Ingram

If you study the *Annual Financial Report Summary* enclosed within this issue of *Topics & Report*, you'll see that TRS is taking very good care of your retirement fund.

One of the main jobs of the Board of Trustees and TRS staff is to invest your money prudently with the goal of continually increasing the size of the portfolio. In this regard, TRS did well in fiscal year 2013.

TRS investments generated a positive 12.8 percent rate-of-return during fiscal year 2013, net of fees, a result that exceeded the retirement system's 12.51 percent custom benchmark for the fiscal year.

Total TRS assets last June, at the end of fiscal year 2013, were $39.479 billion. That's an 8.7 percent increase in total assets from one year ago at the end of fiscal year 2012 – $36.311 billion. And at the end of December, TRS assets totaled

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$42.75 billion. That's an 8 percent growth in the size of the portfolio in just six months, and a 17 percent increase over the last 18 months.

While we're happy with the 12.8 percent rate-of-return for fiscal year 2013, TRS will continue to stress to you, state officials and the public that the long-term investment performance is more important. Our relationships last with most of you, both as active and retired members, literally for decades.

TRS investments over time are more than right on target. The 30-year investment rate-of-return for TRS at the end of fiscal year 2013 was 9 percent per year on average. Our assumed return rate of 8 percent also is a 30-year expectation.

This is the seventh time in the last 10 years that TRS fiscal year investments have exceeded the long-term investment assumption. It represents the 13th time in the last 20 years that the actual rate of return exceeded the long-term assumption and the 16th time that investment returns were positive.

We will continue to urge the General Assembly to fulfill its commitments to your retirement and to appropriate enough money every year to fully fund your pensions. It is sobering to note that last year's 12.8 percent return and our consistently strong investment performance have done little to improve our funded status, the measure of our long-term fiscal viability.

TRS also is working diligently to make sure that the System is ready to implement the state's new pension law. As the administrator of your pension, TRS must implement the laws enacted by the General Assembly, and that includes the new law approved in December by legislators and Gov. Pat Quinn.

We will be ready to implement the new law on June 1, 2014. The only thing that may delay the effective date is action by an Illinois court. But as I write this, TRS has no indication that the courts will delay the law. If a court does act, we will adhere to the court's decision.

As you may know, TRS is a defendant in the pending lawsuit that challenges the constitutionality of the new pension law. TRS took no position on the law when it was being considered by the legislature and will take no position on it now. TRS is being sued simply for administering state pension laws.

Under the Illinois Constitution and state statute, the state attorney general represents TRS, as well as all the other defendants in this lawsuit. TRS is required to defer to the Office of the Attorney General with respect to the conduct of the case and will not be making any comment on the ongoing litigation.

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With the new law scheduled to take effect in just a few months, TRS is working to help its members understand how the new law will affect them in the future.

Here are brief descriptions of the new law's major provisions:

1% Contribution Decrease July 1, 2014

Active Tier I member contributions will decrease from 9.4 percent to 8.4 percent of salary beginning on July 1, 2014 for the 2014-2015 school year. For a member earning $70,000, the decrease reduces the TRS contribution from $6,580 per year to $5,880, or $700.

Creditable Earnings Cap for Active Tier I Members

The new creditable earnings cap for Tier I members is equal to the existing creditable earnings cap for Tier II members. In fiscal year 2014, the Tier II cap on creditable earnings that can be used to determine final average salary is $110,631. Under state law, this salary cap rises annually by a rate that is equal to one-half of

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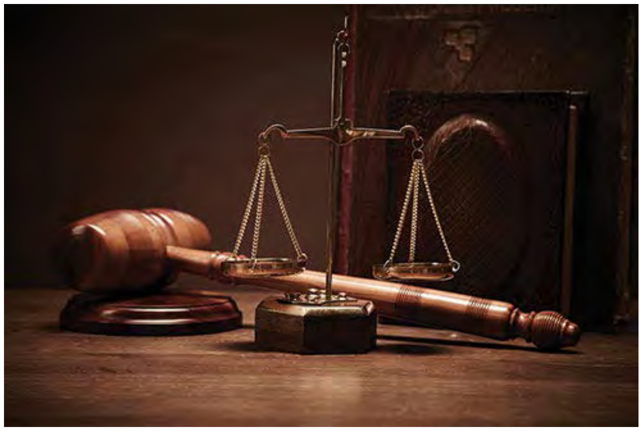
the annual rate of inflation in the previous year.



Exceptions to the salary cap in the law allow a member to establish a cap that is higher than the statutory Tier I and Tier II cap. In general, if a member's salary on June 1, 2014 is higher than the Tier II cap, then the Tier II cap does not apply to that member.

Specifically:

- For any member covered by an individual contract or collective bargaining agreement that is in effect on or prior to June 1, 2014, the cap will be the member's annualized salary on the day that contract expires, even if that salary is higher than the statutory cap. A contract cannot be amended or extended after June 1 to increase the cap.
- For any member not under contract but with a current salary that exceeds the cap, that member's salary cap would be set at his/her salary on June 1. Members with a "grandfathered" salary would each have their own caps.

Tier I Active Members Increased Retirement Age

Over the next 30 years, the law will gradually increase the retirement age for all teachers by five years. The current minimum age of 55 years with 20 years of service will eventually increase to 60 years with 20 years of service.

The retirement age for a member younger than 46 is set on a sliding scale based on his/her age on June 1, 2014. Under this formula, the law essentially adds four months to the old minimum retirement age of 55 for every year that a member is under age 46 at the time the bill takes effect up until a total of five years has been added to the minimum retirement age.

- For members aged 46 and older at the time the bill takes effect, the old retirement ages and eligibility remain in force: A member can retire between the age of 55 and less than 60 years with at least 20 years of service and receive a reduced benefit or at age 60 or more with at least 10 years of service and receive a "full," or non-reduced benefit.

New COLA Formula and Rates for Tier I Active and Retired Members

Two formulas will be used to determine the size of each year's cost-of-living (COLA) adjustment. The COLA formula to be used will be determined each year by the current size of the member's pension.

- Each member, upon retirement, will multiply his/her total service credit by a factor that is initially set at $1,000 when the bill takes effect. This "pension threshold" will be used in the future to determine the annual COLA. For example, a member with 30 years of service upon retirement would have an initial "pension threshold" set at $30,000.
- Beginning in 2016 and in every year thereafter, the $1,000 threshold multiplier will be increased by the rate of inflation, but the rate will never fall below zero percent in case inflation is negative.
- As long as a member's pension is less than his/her current pension threshold, when the member is eligible for a COLA it will be 3 percent compounded, which means calculated from the member's current pension.
- Once a member's pension equals or exceeds his/her threshold, the COLA calculation changes. The COLA in every year then becomes 3 percent of the member's current threshold amount.

First COLAs for Retired Tier I Members

Under state law, a Tier I member who retires after attaining the age of 55 but before turning age 61 will accumulate an annual COLA. But he/she will not collect those accumulated COLAs until the January after he/she turns 61. Under the old pension law, the COLA that accumulated for these members was 3 percent compounded.

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Under the new law, if it is implemented at a time when a member is still accumulating COLAs but has not yet received any of those COLAs, and the member's pension exceeds his/her current pension threshold, the calculation for the accumulated COLAs will be a combination of the old law's 3 percent compounded increase and the new law's increase, which is the current pension threshold multiplied by 3 percent. In these situations, the separation between the old law calculation and the new law calculation will be the implementation date of the law.

Service Credit Used in the New COLA Formula

The service credit used to determine a member's eligibility for a TRS pension is different from the service credit used to calculate a member's "pension threshold" and annual COLA. TRS service credit includes:

- All regular service
- Any service time purchased by the member under an early retirement incentive
- Any optional service purchased by the member, such as leaves of absence, substitute teaching and teaching service in another state
- Unused sick time for anyone who is a TRS member prior to June 1, 2014.

Eligibility: The service credit that will be used to determine a member's eligibility for a pension will include all TRS service plus any service in a pension system that has reciprocal rights with TRS.

Threshold and COLA: The service credit that will be used in calculating a member's new "pension threshold" will be only TRS service credit and will equal the service credit that TRS used or will use to calculate a member's initial TRS pension at retirement.

The COLA Formula and Social Security

TRS members who receive Social Security from a spouse's benefit or from other employment will still use $1,000 as the initial "threshold multiplier" and will still receive their Social Security benefits.

All TRS members will use $1,000 as the starting point for their first "threshold multiplier" because TRS members don't receive Social Security for their service in education and their TRS benefits are not coordinated with Social Security benefits. Since the members of some other state pension systems receive Social Security and have their benefits coordinated with Social Security, their "threshold multiplier" starts at $800.

Staggered COLA Forfeiture

Any TRS member who retires on or before June 30, 2014 will not have to forfeit any COLA increases. Tier I active members who retire on or after July 1, 2014 will forfeit at least one COLA increase, and as many as five increases, based on a sliding scale tied to the member's age on June 1.

	Number of COLAs Forfeited Immediately After Retirement, Starting with 2nd Scheduled COLA
50 years and older	Forfeit the 2nd scheduled COLA
47 to 49	3 forfeited every other year over 6 years
44 to 46	4 forfeited every other year over 8 years
43 and younger	5 forfeited every other year over 10 years

Actuarial Benefit Calculation Change

The law changes the interest rates used in the formula from the mandated 6 percent and 8 percent to a single floating rate: The new floating rate is the interest rate on a 30-year U.S. Treasury bond plus 75 basis points. (0.75 percent) Under current conditions, the new interest rate used in the formula would be 5 percent. The new rate changes annually.

Optional Defined Contribution Retirement Plan

Up to 5 percent or approximately 7,000 Tier I TRS members will be able to freeze their current defined benefit pension plan (DB) benefits and join a new defined contribution benefit plan (DC) in effect until their retirements.

The DC plan is open only to active Tier I members and would begin on July 1, 2015. Members would have one opportunity to elect membership in the new DC plan. After opting in, a member cannot rejoin the DB plan unless the DC plan is ended by the legislature. A member would need to work at least five years in order to be vested in the DC plan.

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On July 1, 2015, all members who have joined the DC plan would have their creditable service frozen on that date for purposes of determining a DB pension. To determine a member's eligibility for a DB pension after the member switches to the DC plan, TRS would use the member's service credit accumulated under both the DB plan and the DC plan at retirement.

Active members in the DC plan pay an 8.4 percent salary contribution. The state's contribution would be determined annually. Upon retirement, members would receive a DB annuity in perpetuity, plus payments from an accumulated DC retirement account until those funds are exhausted.

"The court challenge could delay the implementation date, but not necessarily the June 1 effective date, until a final court ruling is made"

Supplemental Pension Contributions

When the state's pension obligation bonds are paid off in 2019, the state will automatically earmark additional payments to TRS and the other state pension systems until the systems' funding status reaches 100 percent. In fiscal year 2019 the extra payment will be $350 million and $1 billion every year beginning in fiscal year 2020. For TRS, this means a "supplemental" payment of $194 million in fiscal year 2019 and $554 million in fiscal year 2020 and every year after that until the unfunded liability is paid off.

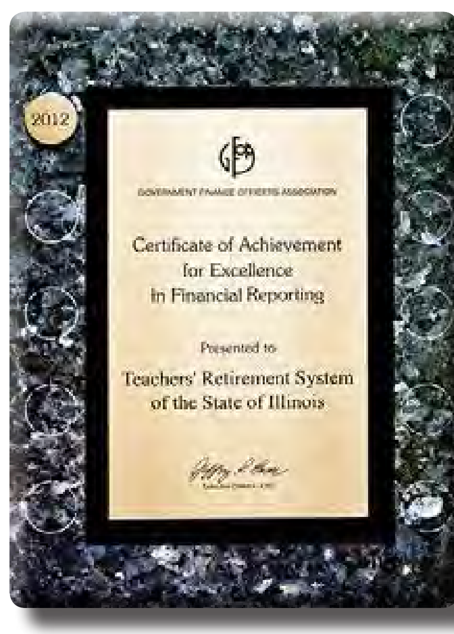
Also, beginning in fiscal year 2016 the state will annually earmark 10 percent of the savings the state will realize from the law's provisions to TRS.

Mandatory State Pension Contributions

If the state does not pay its annual contribution to TRS within a set period of time, TRS could go to court to force the state to pay the contribution in the same way that the Illinois Municipal Retirement Fund can force local governments to pay their contributions. This provision, however, can be altered or repealed by the General Assembly in the future.

Financial Reporting Award for Fiscal Year 2012 Annual Report

TRS's comprehensive annual financial report for the fiscal year ended 2012 was awarded the Certificate of Achievement for Excellence in Financial Reporting by the Government Finance officers Association of the United States and Canada (GFOA). The Certificate of Achievement is the highest form of recognition for excellence in state and local government financial reporting. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.



A Certificate of Achievement is valid for a period of one year only. We believe that our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and we have submitted it to the GFOA to determine its eligibility for another certificate.

Medicare Advantage Enrollment Marked by First Year Challenges

The transfer of Medicare-eligible members of the Teachers Retired Insurance Program to the new Medicare Advantage plans was completed early this year thanks to the diligence of TRS members who were required by state law to make this transition, as well as the hard work and dedication of TRS staff.

More than 35,000 enrollment forms were submitted to TRS between October and December of 2013 authorizing the transfer to one of the four Medicare Advantage insurance plans now offered by the State of Illinois. The switch to Medicare Advantage plans for all eligible TRIP members and state retirees was mandated last spring by the General Assembly with the goal of reducing the state's health insurance costs for retirees. The new coverage for Medicare-eligible members began on Feb. 1.

While the enrollment process was challenging for some, only about 1,000 forms were returned to members for correction – an admirable 97 percent success rate. TRS staff worked long hours and overtime to ensure that the enrollment information was entered into the TRS system before the forms were sent to the Department of Central Management Services and the insurance companies to complete the enrollment process. In addition, TRS staff made proactive telephone calls to many members who were in danger of losing their TRIP health insurance because they did not submit enrollment forms. This effort ensured that these members would continue to receive TRIP insurance.

In 2014, all TRIP members already in a Medicare Advantage plan will see their annual Benefit Choice Period moved from the spring to the fall. This fall selection period for Medicare coincides with the federal government's Benefit Choice Period. TRIP members who will be first eligible for Medicare during 2014 will have to navigate two Benefit Choice Periods this year. The first period will be in the spring, when they select or renew regular TRIP coverage for approximately six months. Then, in the fall, these members will select a Medicare Advantage plan to replace their TRIP insurance. Their Medicare coverage will begin on Jan. 1, 2015.

Medicare Advantage Chart

Your Status	Your Benefit Choice Period(s) in 2014
In TRIP now, not in Medicare	Spring of 2014
In TRIP now and first eligible for Medicare in 2014	Spring of 2014 and Fall of 2014
In Medicare now	Fall of 2014

Early Retirement Option (ERO) Extended to 2016 with Changes

Legislation extending the TRS Early Retirement Option until June 30, 2016 was signed into law last June by Gov. Pat Quinn, but this extension significantly changes the way ERO will operate for the next few years.

For the first time in the program's history, school districts will not be required to let at least 10 percent of eligible teachers retiring between ages 55 and 60 use ERO to offset the required reduction in their initial pensions.

Under the new law, the eligibility criteria for participating in ERO will be negotiated and set by each school district and the union representing a majority of TRS members in that district.

The retirement application will include a section that the member's employer(s) must sign and indicate that ERO is approved. All of a member's employers must agree to the use of ERO.

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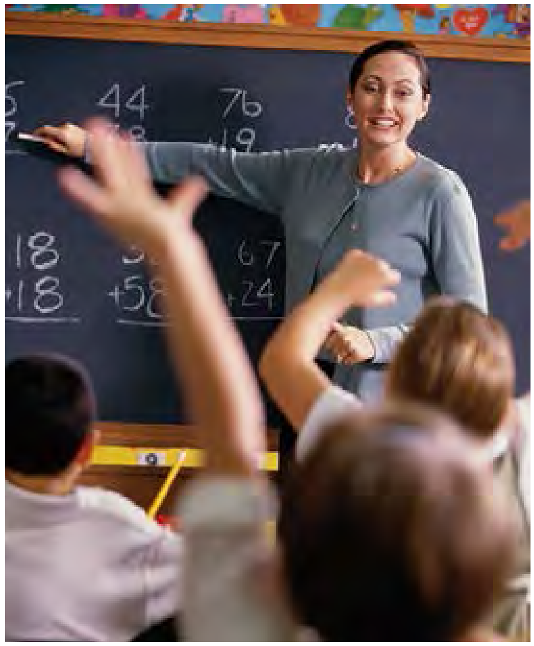
The extension also increases the one-time contributions for ERO that members and school districts must pay in order to participate. The increases were recommended by the General Assembly's Commission on Government Forecasting and Accountability to cover the anticipated future cost of the program.

For TRS members, the one-time contribution to participate in ERO is now 14.4 percent of salary for every year the member is under age 60 or for every year the member's creditable service is less than 35 years, whichever is less. The member contribution rate under the previous law was 11.5 percent.



For school districts, the one-time contribution to have an employee participate in ERO is 29.3 percent of the member's salary for every year the member is under age 60. The employer's contribution rate under the old ERO law was 23.5 percent.

The law also keeps in place the current 0.4 percent payroll contribution paid by all active TRS members to help fund the ERO program.

Benefits Report Emailed to Active and Inactive Members

The TRS Benefits Report was emailed to active members in November. The report summarizes the following information about your TRS account: refundable contributions, beneficiary refund, beneficiaries, estimated benefits, sick leave service, 2.2 upgrade information, reciprocal service, refunded service that may be reinstated, optional service, and active service.

If you have not provided your email address to TRS and you received this newsletter by mail, please visit our site, **http://trs.illinois.gov**. Then, set up an account under "Member Account Access," which can be found on the far left side of the home page. You will need your Member ID, which can be located on the first page on the right side on a past printed TRS Benefits Report or by calling (800) 877-7896. You will be able to view your TRS Benefits Report after signing in.

Additionally, please enter your email address under the contact information in the secure area so you will receive future email alerts.

Recent payments and changes in outstanding balances that have occurred since the 2013 report was sent will be shown online.

If you need to change your beneficiaries, visit the member forms area of our website and complete a Member Information and Beneficiary Designation (MIBD) form, which you can complete online. Please print out and mail the form to us; we will update your file. A new MIBD form replaces any former version on file with TRS.

If you see an error on your reported service record or salaries, contact your employer (school district) without delay to correct the problem. This information is reported by your employer on your behalf to us. It may be more difficult to correct an error if you wait until retirement.

Please call us at (800) 877-7896 if you believe your report has an error (other than salary or service credit), if you need an additional copy, or if you have any questions about the content.

Annuitants do not receive TRS Benefits Reports.

Teachers' Retirement System of the State of Illinois
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Board of Trustee Meetings

All meetings will be held at the TRS office in Springfield. The meetings are tentatively scheduled to begin at 1 p.m. on Wednesday and continue until Friday, if necessary. This schedule is subject to change. Board actions are located on our website, **http://trs.illinois.gov.**

- April 14-15, 2014 (retreat - Mon. & Tues.)
- May 28-30, 2014
- June 24-25, 2014
(tentative - Tues. & Wed.)

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Go Green!

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Web site

http://trs.illinois.gov

Address changes

To ensure that all information about your benefits reaches you, please notify us each time your mailing address changes. You may call us or send us the following information in writing:

- your name and Social Security number
- former street address, city, state, and ZIP
- new street address, city, state, and ZIP
- daytime telephone number.

Topics & Report

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