

TOPICS & REPORT

Teachers' Retirement System of the State of Illinois
Winter 2012-13



State Officials Eye Pension Code Overhaul

TRS is preparing contingency plans designed to help members understand and comply with any overhaul of the state's pension code that may affect benefits, contributions and health insurance plans.

As this issue of *Topics & Report* is being finalized, the General Assembly has yet to act on pending proposals that have generated intense debate among TRS members, state officials and the general public.

Although it is likely that any change in the pension code approved by lawmakers will be delayed due to promised court challenges, TRS nonetheless has outlined plans to help explain the impact of any changes in the law and what members' responsibilities may be going forward.

A new comprehensive pension reform proposal, **House Bill 6258**, was introduced in the General Assembly on December 5 by Rep. Elaine Nekritz (D-Northbrook) and Rep. Daniel Biss (D-Evanston). It seeks to stabilize TRS finances and eliminate the System's unfunded liability in 30 years.

That bill would reduce the annual cost of living adjustment; raise the retirement age for all members under age 46; increase active member contributions by 2 percentage points over time; cap the amount of salary that can be used to determine a final average salary; create a new law that prevents the state from skipping its annual pension contribution; and shift the annual cost of TRS pensions from the state to local school districts.

Still pending in the General Assembly at the turn of the new year was **Senate Bill 1673**, legislation that would overhaul the benefit structure and funding mechanism for TRS pensions by forcing all members to choose between two benefit options

involving the cost of living adjustment (COLA) and state health insurance eligibility.

If any overhaul of the state's pension code is approved by legislators and signed into law by the governor, it will face a court challenge. The main argument will be that the bill reduces pension benefits that are contractually guaranteed to TRS members and therefore violates the

pension protection clause of the state constitution. That clause prevents existing pension benefits from being "diminished or impaired."

Here is a menu of major pension proposals lawmakers are considering:

A benefit choice for the future: COLA and health insurance – This proposal calls on all active, inactive and retired TRS members to choose between two options in the make-up of their retirement benefits.



- **Option 1:** Accept a COLA pension change – from 3 percent calculated from a retired member's current pension amount to one that is capped at 3 percent or one-half of the increase in the consumer price index, whichever is less. This reduced COLA would be calculated each year from a member's original pension amount. In return, the TRS member retains "access" to state-supported health insurance through the Teachers' Retirement Insurance Program. For active members, future salary increases will be used to calculate the member's future pension.
- **Option 2:** Reject the change in the COLA and it remains at 3 percent compounded annually. The TRS member loses "access" to state-supported health insurance through the Teachers'



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Retirement Insurance Program. For active members, all future salary increases would not count when the member's future pension is calculated.

COLA limits – A 3 percent COLA would be added annually to a retired member's pension, but the COLA rate would apply only to the first \$25,000 of a pension. Currently, the average TRS pension is \$48,216. Under the current COLA, that pension grows to \$49,662 in the second year and \$51,152 in the third year. Under **House Bill 6258**, with a capped COLA the same pension would grow to \$48,966 in the second year and \$49,716 in the third year.

New start date for a TRS COLA – TRS members agreeing to Option 1 would first see the new COLA on the Jan. 1 in the year after turning age 67 or in the year after the fifth anniversary of the member's retirement, whichever is earlier. If a retired Tier I member now eligible for the current COLA accepts Option 1, the current COLA would be suspended until the member is eligible for the new COLA.

Increase in active member contributions – Active member contributions would increase from 9.4 percent to 10.4 percent in 2014 and increase to 11.4 percent in 2015.

Increase in the retirement age – The retirement age would be set on a sliding scale based on the member's age at the time the law takes effect:

- 46 and older: Retire at 55 with 20 years of service and receive a reduced benefit, or at 60 and receive a full benefit
- 40 to 45 years old: Retire at 56 for a reduced benefit and 61 for full benefits.
- 35 to 39 years old: Retire at 58 for a reduced benefit and 63 for full benefits.
- 34 and younger: Retire at 60 for a reduced benefit and 65 for full benefits.

Salary caps for calculating a pension –

The salary used to determine an active member's final average salary would be capped at the maximum Social Security wage base, which is \$113,700 in 2013. However for a TRS member employed under an individual or union contract, the cap would be set at the member's salary at the end of the contract if the salary exceeds the Social Security wage base. Contractual salaries that are below the Social

Security wage base when the bill takes effect would be allowed to rise to the Social Security wage base.

Cash balance plan – This proposal creates a new "Tier III" benefit structure that is commonly referred to as a "cash balance plan." All new TRS members hired after the law takes effect would automatically be in Tier III. Existing Tier II members could elect to join Tier III.

Under the plan, TRS members, school districts and the state would contribute toward member pensions. TRS would annually credit interest of between 4 percent and 10 percent, depending on investment earnings.

While the contributions of all Tier III members would be commingled for investment purposes, each Tier III member would have an individual notional account on file with TRS that would be comprised of his/her individual contributions, school district contributions and investment income.

Upon retirement, TRS would calculate a guaranteed life-time annuity based solely on the money credited to each member's account and adjusted for estimated future investment earnings and the member's anticipated lifespan in retirement. The annuity continues even after money in the member's account is exhausted

Forcing the State to Pay Its Annual Contribution to TRS

– Under this proposal, if the state fails to pay any monthly share of its legally-required contribution to TRS within 90 days, the TRS Board would have the right to go to the Illinois Supreme Court for an order commanding the comptroller to pay TRS out of the state budget's General Revenue Fund.

School districts pay the annual cost of TRS pensions –

School districts would be responsible, beginning in 2014, for paying an increased share of the annual costs of TRS pensions and the state would pay less toward these

costs. Eventually, school districts would be responsible for paying the entire annual cost of benefits being earned every year. In fiscal year 2013, the annual cost of TRS pensions is approximately \$800 million. Starting in 2014, the share of the annual cost paid by local school districts would

increase by 0.5 percent each year until the total annual pension cost is paid by the districts.

If you haven't yet, email us, members@trs.illinois.gov, using your "home" email address (not work) and include your full name/ address/last 4-digits of SSN so we may quickly contact you regarding any pension changes.

TRS Rides an Uncertain Economy; Faces Another Year of State “Underfunding”

The long-term fiscal health of TRS continues to be a source of concern for the System and its members due to a highly volatile economy that depressed investment earnings last year. State funding also continues to fall short of what is needed to secure the future.

TRS will be able to meet its obligations to retired teachers in the near future, but it cannot guarantee retirement security for future generations of teachers unless the state meets its total obligations in the coming years.

In October the TRS Board set state government’s fiscal year 2014 funding contribution for the System at \$3.438 billion, a 27.2 percent increase over last year’s contribution. However, that contribution once again falls short of the amount needed to fully fund TRS over the next 30 years. TRS faces the real risk of future insolvency because of insufficient funding.

The fiscal year 2014 state contribution is hundreds of millions of dollars below the amount of money that would be required to fully fund the System if standard actuarial calculations were used to determine the contribution.

The System’s funded ratio declined from 46.5 percent in fiscal year 2011 to 42.1 percent at the end of June 2012. This reduction is due to years of insufficient state funding coupled with an uncertain economy in the last year that depressed the System’s investment earnings, as well as regular changes in actuarial assumptions. TRS earned 0.8 percent on its investments during fiscal year 2012, compared with 23.6 percent in fiscal year 2011.

State contributions to TRS are artificially low

Over the last several years state government has fulfilled its statutory responsibilities to TRS and paid

Fiscal Year	TRS Rate of Return
2012	0.8%
2011	23.6
2010	12.9
2009	(22.7)
2008	(5.0)
2007	19.2
2006	11.8
2005	10.8
2004	16.5
2003	4.9



exactly what state law calls for the state to contribute. But for decades those legal contributions have not been enough to improve the System’s long-term finances. The contribution is set artificially by state law.

Under standard actuarial practices, the state’s annual contribution for the coming year should be about \$4 billion.

The calculations set in state law are different from normal actuarial practices in a few key areas. State law:

- Requires pension costs to be calculated on a 50-year timetable instead of the standard 30 years
- Establishes a 90 percent funding target instead of the standard 100 percent goal
- Requires the debt payments on state pension bonds to be deducted from the total contribution.

To TRS, long-term results are more important

In determining the fiscal health of TRS, the System does not focus on a single year’s worth of investment returns and always takes a long-term view of investment earnings. TRS strives to be viable not only for our members who are currently retired, but for all of our active members in the decades to come.

Over the last 30 years, the System’s investments have exceeded previous predictions – the TRS investment rate of return is 9.6 percent for that period. In the last decade, total TRS assets available to pay pensions grew by 62 percent. In the last three fiscal years – 2012, 2011 and 2010 – the TRS return was 12 percent. TRS ended fiscal year 2012 on June 30 with \$36.3 billion in assets.

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This sharp swing does underscore the continued uncertainty and volatility in the world economy, especially in Europe. The 0.8 percent return was for a 12-month period that ended in June. But the TRS investment return for the 12-month period that ended in September was 16.4 percent.

The 0.8 percent rate of return for TRS falls in line with the investment returns for fiscal year 2012 being reported by other large public pension systems across the country. Many saw their investment returns at the end of a 12-month period in June drop from more than 20 percent to less than 4 percent.

Economic volatility forces a reduction in predicted long-term TRS investment income

In September the Trustees approved revisions to a number of assumptions contained in the current TRS actuarial model, including a reduction in the System's long-term assumed rate of return on its investment portfolio from 8.5 percent to 8 percent.

The trustees also voted to undertake the next study of the System's actuarial assumptions, including the assumed rate of return, in three years instead of the

five years called for in state law because of the continued volatility of the world economy.

Reducing the rate from 8.5 percent to 8 percent is a prudent move that balances reality with the needs of TRS members. The decision takes into consideration many things: the volatility of the world economy, the fiduciary duty the trustees have to keep the System strong and state government's long-term responsibility to teacher pensions.

The former 8.5 percent rate of return, first adopted by the TRS Board in 1997, proved to be appropriate over time. The actual TRS investment rate of return between 1981 and 2012 was 9.6 percent.

The National Association of State Retirement Administrators (NASRA) reported earlier this year that of 126 major state and municipal pension systems across the country, including TRS, 47 had set an assumed rate of investment return at 8 percent. The NASRA study also found that over the last 25 years, the 126 pension systems recorded a median actual investment return of 8.3 percent.

Early Retirement Option (ERO) Update

On June 1, 2005, legislation increased ERO contribution rates and mandated a study for future rates to ensure that the ERO contribution paid by the member and employer adequately funded the program.

The recently completed actuarial experience analysis included the System's experience under the early retirement without a discount option, including consideration of the sufficiency of the member and employer ERO lump-sum contributions and the active member contribution of 0.4 percent to adequately fund early retirement without a discount option. The study found that the rates would need to be higher to cover the cost of the ERO program.

The TRS Board recently communicated the results of the actuarial investigation to the Commission on Government Forecasting and Accountability (COGFA).



Based on this information, COGFA must recommend to the General Assembly by Feb. 1, 2013 any proportional adjustment in the amounts of the member and employer lump-sum ERO contribution rates. If the General Assembly fails to accept the member and employer contribution rates in response to COGFA's recommendations, the ERO plan will be terminated and shall cease for retirements commencing July 1, 2013 or later.

ERO continues to be available for members who will retire on or before June 30, 2013. (This means your last day of work must be June 29 or prior, and you must meet all of the other eligibility requirements.) Members should ensure that they will be eligible based on their district's ability to limit the number of those retiring to 10 percent of those eligible.

Important Annuitant Tax and Payment Reminders for 2013

Expect arrival of 1099-R

If you received a TRS benefit in 2012, the Office of the Comptroller will mail an IRS Form 1099-R to you by Jan. 31, 2013. This form will report your income received from TRS during 2012.

The amount shown in Box 5 on the 1099-R form represents the non-taxable portion of TRS retirement benefits paid to you for the year and is the difference between Boxes 1 and 2a. Box 9B will only have a value if 2012 was the first year that you received a benefit from TRS.

If you do not receive a 1099-R form or you need a duplicate copy sent to you, please call us at (800) 877-7896 or email us at members@trs.illinois.gov.

Increase reflected on Feb. 1 check

The checks you receive in January and February may be for different amounts if the January 2013 benefit payment received in February reflects your annual 3 percent post-retirement increase. The increase is first effective on Jan. 1 following either your first retirement anniversary or your 61st birthday, whichever is later. Following

the first increase, your benefit increases 3 percent each Jan. 1. With some exceptions, recipients of monthly survivor benefits will also see a 3 percent increase.

Withholding tables usually change

Revised federal withholding tables may go into effect on Jan. 1, 2013. As a result, the federal taxes withheld from your Jan. 1, 2013 annuity payment may increase or decrease based on your filing status.

TRS cannot give tax advice due to federal and state restrictions. You may wish to contact a qualified tax advisor or the Internal Revenue Service at (800) 829-1040 to ensure that you have adequate federal withholding for the 2013 tax year. If you are underwithholding, there could be a negative consequence at tax time.

If you would like to change your withholding election, you must complete a new Form W4-P. You can obtain a new form by calling us at (800) 877-7896 and pressing "2" for our 24-hour Forms Order Line, by visiting our forms page at <http://trs.illinois.gov>, or by calling your local Internal Revenue Service office. A new Form W4-P replaces any former version on file with TRS.

PAYER'S name, street address, city, state, and ZIP code		1 Gross distribution \$		OMB No. 1545-0119 2012 Form 1099-R		Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.	
		2a Taxable amount \$					
		2b Taxable amount not determined <input type="checkbox"/>		Total distribution <input type="checkbox"/>			
PAYER'S federal identification number	RECIPIENT'S identification number	3 Capital gain (included in box 2a) \$		4 Federal income tax withheld \$			
RECIPIENT'S name		5 Employee contributions / Designated Roth contributions or insurance premiums \$		6 Net unrealized appreciation in employer's securities \$			
Street address (including apt. no.)		7 Distribution code(s)		8 Other \$			
City, state, and ZIP code		9a Your percentage of total distribution %		9b Total employee contributions \$		This information is being furnished to the Internal Revenue Service.	
10 Amount allocable to IRR within 5 years \$		11 1st year of desig. Roth contrib.		12 State tax withheld \$		13 State/Payer's state no.	
Account number (see instructions)				15 Local tax withheld \$		16 Name of locality	
				17 Local distribution \$			

Form 1099-R (keep for your records) www.irs.gov/form1099r Department of the Treasury - Internal Revenue Service

Box 5

Box 9b

Constitutional Amendment Regarding Pension Benefit Increases Rejected

A proposed amendment to the Illinois Constitution making it tougher to approve increases in public pension benefits was legally rejected during the Nov. 6 election and will not take effect.

The proposal fell short in both of the requirements needed to become part of the Constitution. Any proposed addition to the Constitution needs approval from at least 60 percent of voters on that particular question or 51 percent of all voters in the election. The proposal received the support of 48 percent of all voters and 58 percent of voters on that question.

The amendment would have governed the actions of the General Assembly, county, township and city governments, school districts and special districts throughout the state. It would have required a three-fifths majority to increase any pension benefit or expand the eligibility for any benefit. For instance, a TRS benefit increase would have needed 71 votes in the Illinois House and 36 votes in the Illinois Senate to pass, as opposed to a simple majority of 60 votes and 30 votes, respectively.



Enrique M. Vasquez Appointed to TRS Board

Enrique M. Vasquez, the president of a Schaumburg-based financial investment firm, was named in September by Gov. Pat Quinn to the TRS Board of Trustees.

Trustee Vasquez, of Cary, is president and CEO of Genworth Financial Investment Services. His term will expire in 2014 because he is completing the term of a former trustee who resigned in 2011.



Trustee Vasquez holds a bachelor's degree in accounting from Kean University in Union, New Jersey and a master's degree in business administration, international finance, from Fordham University in New York.

In August, Gov. Quinn reappointed trustees Mike Busby of Kenilworth, Janice Reedus of Indian Head Park and Sonia Walwyn

of Naperville to new four-year terms. All three were appointed to the Board in 2009.

Genworth Financial partners with 1,800 independent financial advisors on the integration of wealth management practices into the services they provide clients. Prior to joining Genworth in 2004, he served in various leadership capacities with GE Capital for close to a decade, including vice president of business development for GE Commercial Finance, GE Financial Assurance and GE Capital, as well as vice president, manager of finance, for GE Asset Management.

The other members of the TRS Board are State School Superintendent Christopher Koch, who serves as president; Molly Phalen of Rockford; who serves as vice president; Marcia Campbell of O'Fallon; Jan Cleveland of Carmi; Cinda Klickna of Rochester; Sharon Leggett of Evanston; Bob Lyons of Hoffman Estates; and Cynthia O'Neill of Carlyle.

Trustee Candidate Petitions Available Online



The Board of Trustees election for two active member trustees and one annuitant trustee is scheduled for May 1, 2013. To be nominated, prospective candidates must receive a minimum of 500 eligible signatures. Petition instructions, petitions, and the board election rules are available as PDFs from <http://trs.illinois.gov>. Before circulating petitions, please carefully read the instructions. Certified petitions must be returned to TRS no sooner than Jan. 2, 2013 and no later than 4:30 p.m. on Jan. 31, 2013. If you have any questions, please contact Administrative Services Manager Alice Kern at akern@trs.illinois.gov.



Optional Service Purchases

Optional service, such as military, pregnancy or adoption leave, may be purchased to increase your service credit for retirement purposes. **Once optional service has been added to your record and purchased, refunds are permitted only if it is duplicated service or in excess of what is allowed under the Illinois Pension Code.** Purchases of most service credit must be completed before you retire. The only exception is credit for pregnancies and adoptions. For more information, please read either the *Tier I Member Guide* or *Tier II Member Guide* online.

Benefits Report Mailed to Active and Inactive Members

Last time reports mailed – electronic delivery only next year

The TRS Benefits Report was emailed to half of our active membership in November and mailed to the other half without email addresses on file in early December. 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.

To save on printing and mailing costs, the report will be available for members to view **online only** next year. Social Security statements are also only provided online now for the same reason.

This new delivery change and required member ID for sign in to the secure Member Account Access area was printed at the top right of the mailed member statements. **If you received this Topics & Report by mail, you must provide your email address to us to ensure you receive notification your statement is ready for viewing next year.** Either send your email address and full name and mailing address to members@trs.illinois.gov or call us at (800) 877-7896.

Recent payments and changes in outstanding balances that have occurred since the 2012 report was sent will be shown online. You may also view prior statements from 2004 to 2012.

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 is fillable 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 and 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>.

- February 20-22, 2013
- April 17-19, 2013 (Retreat - T.B.D.)
- May 22-24, 2013
- June 20-21, 2013

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Go Green!

To receive this newsletter electronically, send an email to members@trs.illinois.gov. Include your full name, zip code, the last four digits of your Social Security number, and your email address.

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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
- new street address, city, state, and ZIP
- former street address, city, state, and ZIP
- daytime telephone number.

Topics & Report

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