TOPICS & REPORT

Teachers' Retirement System of the State of Illinois
Winter 2015

Executive Director's Message

Executive Director Dick Ingram

If you have ever heard one of my public presentations about the long-term financial problems we face at Teachers' Retirement System, you would have heard me say that because I joined TRS early in 2011, I am one of the first members of Tier II within TRS.

While I'm very happy leading a great organization like TRS and interacting with our members, I'm not too happy to be a Tier II employee. Tier II has some big problems that could cost the state and local school districts a lot of money in the future unless it's fixed.

That's one of the reasons why a special state task force was convened this fall by legislators to look into the potential trouble created by Tier II and how these future problems could affect the recruitment and retention of teachers in Illinois. I'm a member of that committee.

Contents

Tier II is the pension benefit structure created by the General Assembly in 2010 for anyone who had not contributed to TRS or another Illinois public pension system before January 1, 2011. Tier II is designed to help solve the financial problems faced by TRS and the other systems by reducing pension benefits for these new members. Lower pensions means reduced long-term costs for the state.

If Tier II is left alone, it will accomplish its mission. The $61.6 billion TRS unfunded liability will shrink over several decades and eventually be eliminated because the state will pay less to the ever-growing number of Tier II members. In fact, at some point in the future, we estimate that Tier II members actually will help create a surplus of funds for TRS that effectively could eliminate the need for any state government contribution to the System.

But the core of Tier II – the reduced benefits structure – is a problem the Teacher Recruiting and Retention Task Force will review. The benefit structure is unfair to all Tier II members.

Right now, a Tier I member's pension costs roughly 20 percent of an active member's salary. Because of the benefit reductions in Tier II, a Tier II member's pension is worth just 7 percent of an active member's salary. However, by law, active Tier II members of TRS, like me, pay the same 9.4 percent salary contribution to the System that active Tier I members pay.

What all this means is that Tier II members are paying the entire cost of their pensions plus an extra 2.4 percent to TRS. That extra 2.4 percent subsidizes the pensions of Tier I members.

Like other Tier II members, I'm happy to help out, but I'm not really too thrilled with paying for my entire pension and paying extra to subsidize somebody who is paying less than half the cost of their pension. I like all of you very much, but this is a matter of equity for Tier II members.

And someday this subsidy may be declared unconstitutional, which threatens the revenue stream that is designed to eliminate the System's unfunded liability. We may see a scenario where Tier II members argue in court that the subsidy we pay is really an extra income tax – a tax that only we have to pay. That would be unconstitutional.

The Task Force will investigate whether this problem will erode the ability of public schools in Illinois to attract the best and brightest teachers. But that's only one of the problems with Tier II that the new Task Force will discuss.

TRS ILLINOIS

Director's message
continued on page 2

Director's Message *continued from page 1*

The second major problem we see down the road is that some Tier II members will be forced into Social Security and those members and their employing school districts will each have to start paying the 6.2 percent federal Social Security tax.

As you know, TRS members' service in public education is not part of Social Security, so neither members nor employing school districts have to pay that federal payroll tax. But for TRS members to stay out of Social Security, the System's minimum benefits must be at least as good as the minimal benefit provided by Social Security. It's called the "safe harbor" provision.

The TRS actuaries project that because the Tier II law limits the growth of Tier II benefits to a rate that is slower than the growth of Social Security benefits, in the future a Tier II benefit will be smaller than the minimum Social Security "safe harbor" benefit.

As we understand the law right now, Tier II members will become Social Security members one at a time as soon as their estimated retirement benefit falls below the "safe harbor." At that point that member must start paying the appropriate federal taxes. That's 6.2 percent of salary for a member – on top of the current 9.4 percent contribution for TRS. School districts would have to pay 6.2 percent to the federal government, along with the 0.58 percent that they currently pay to TRS. Because Tier II members will be added to Social Security one at a time, we anticipate it could be an administrative nightmare for school districts, create unexpected strain on local school budgets and impact efforts to hire and retain the best teachers.

Tier II, indeed, has issues.

I will keep you posted on further developments from the new Task Force. But already with this Task Force Illinois lawmakers have taken a huge positive step by not burying their heads in the sand. They're recognizing that the anticipated rewards of Tier II may be more than negated by unforeseen consequences created by the law. The goal of this effort is to fix Tier II so it does not hurt TRS members and Illinois, and with billions of dollars and the future retirements of Illinois teachers at stake, the earlier we get started, the better.

Best Wishes,

Dick Ingram

New Pension Law Declared Unconstitutional; Court Challenge Continues

Despite a recent court judgment that declared the state's new pension law (Public Act 98-0599, formerly Senate Bill 1) to be unconstitutional, the legal challenge to the new law will continue.

On November 21, 2014, Sangamon County Circuit Court **Judge John Belz** ruled that the new pension law violates the Pension Protection Clause of the Illinois Constitution. Less than a week later, **Attorney General Lisa Madigan** appealed Judge Belz's decision directly to the Illinois Supreme Court.

Judge Belz's decision said that the new law violated the state constitution because it "diminished" retirement benefits promised to the members of the state's public pension systems. The judge also said that the state had no authority to bypass the Pension Protection Clause as part of its efforts to correct state government's mounting financial problems.

For now, Judge Belz's ruling keeps in place the current law governing the calculation of TRS pensions and cost-of-living adjustments, as well as the administration of TRS benefits.

TRS cannot comment further about this lawsuit and will offer no opinion on how the challenge to the new pension law may be treated by the Supreme Court. TRS is a defendant in the lawsuit simply because the System administers the Illinois Pension Code.

Gov. Pat Quinn signed Senate Bill 1 into law in December of 2013. The goal of the new law is to stabilize TRS finances long-term and eliminate the System's unfunded liability by 2044, primarily by reducing benefits for retired and active members and creating funding guarantees and contribution levels that will gradually, over 32 years, fully fund TRS.

Five lawsuits challenging the law as a violation of the Pension Protection Clause were filed after the bill was signed into law. These cases were consolidated in Sangamon County Circuit Court. As part of the court challenge, in May of 2014 the court issued a temporary injunction that delayed the

New Law Unconstitutional *continued on page 3*

New Law Unconstitutional *continued from page 2*

implementation of the new law beyond its initial effective date of June 1.

In July, the state Supreme Court ruled that the Constitution's Pension Protection Clause is unambiguous and prevents the General Assembly from "diminishing or impairing" any of the benefits promised to members of a state retirement system.

This ruling came in response to a separate lawsuit that challenged a two-year-old state law which required all retired state employees to pay a premium for their state-subsidized health insurance benefits. Until the enactment of that law, retired state employees with at least 20 years of service paid no premiums for their health insurance in retirement. However, the court's decision said that the state could not charge those employees a premium based on the size of their annual pensions. That, the court said, was a "diminishment" of the retirees' benefits. TRIP members were not included in this legislation because retired TRIP members always have paid premiums in retirement.

Priority to Enhance Helpful Services to You

Members always will be the first priority at Teachers' Retirement System. We are continually working to enhance the way we interact with you, answer your questions, solve your problems and provide you with the help you need to navigate an increasingly complex world.

Usually, the first point of contact most members have with TRS is a telephone call or email to our Call Center or an in-person visit with a benefits counselor in either Springfield or Lisle. With a total staff of 28 dedicated to member services, the TRS Call Center is available to help members understand their benefits Monday, Wednesday and Friday from 7:30 a.m. to 4:30 p.m., and on Tuesday and Thursday from 7:30 a.m. to 5 p.m. Counselors are available between 9 a.m. and 3:30 p.m., Monday through Friday.

Call Center Supervisor Robert Powers and **Benefits Counseling Supervisor Renē Troppa** report that during the last fiscal year, which ended on June 30, 2014, member services staff fielded or returned more than 180,000 telephone calls and almost 15,000 emails and completed one-on-one counseling with more than 7,000 members.

"We're continually working to improve response times and limit the amount of time that members have to wait in order to speak to someone who can help them," Powers said. "Every member's experience is different, but our goal is to be as helpful as we can as quickly as we can."

Powers added that enhanced Call Center procedures put in place during 2014 are lowering the number of calls in which a member "abandons" the connection because they have been on hold too long. During September of 2014, for example, the number of abandoned calls fell by 72 percent as opposed to September of 2013. The number of members who left voicemails in September of 2014 dropped by 59 percent compared with September in 2013 because they were able to reach TRS staff. All the while, the total number of calls during September 2014 increased 13 percent from September of 2013. The average length of a phone call with a member, though, remained approximately four minutes.

Troppa said it is always preferable that TRS members seeking a one-on-one counseling session first make an appointment in either Springfield or Lisle. TRS does not turn down any "walk-in" counseling requests and accommodated more than 2,300 walk-ins in fiscal year 2014. However, all walk-in members must wait until all members in the office with an appointment have seen a counselor.

"By scheduling an appointment, we can touch base before we look at your situation and remind you to bring all of the records and information you will need to get your questions answered and to make your session as successful as possible," Troppa said.

"For example, if you are an active member, our information on you is only updated annually after the last school year ends," he added. "We advise active members to bring with them information that they can get only from their employers: current and projected salary information, including what will be reported to TRS as their creditable earnings and projected unused sick leave with their current employers. If you have questions about what your employer will report to TRS as creditable earnings for the current school year, you must contact your employer."

To make a counseling appointment, email TRS at **members@trs.illinois.gov** or call (800) 877-7896.

Investments Improve Unfunded Liability During Fiscal Year 2014

Strong investment returns in fiscal year 2014 led to a slight improvement in the funded ratio of Teachers' Retirement System for the first time in several years, to 44.2 percent from 42.5 percent, as measured by a calculation that uses the fair market value of the System's assets.

Investment Rate of Return

The rate of return on TRS assets in fiscal year 2014 was 17.4 percent, net of fees, a total that exceeded the System's custom investment rate benchmark for fiscal year 2014 – 16.4 percent. In fiscal year 2013, the System's rate of return, net of fees, was 12.8 percent.

TRS assets on June 30, at the end of fiscal year 2014, were $45.8 billion. That total is 15.0 percent higher from one year ago at the end of fiscal year 2013, when assets totaled $39.9 billion.

The 30-year rate of return for TRS at the end of fiscal year 2014 was 9.72 percent. The System's assumed return of 8 percent in fiscal year 2014 is also a long-term expectation. This means that over time TRS investments are performing better than expected.

June 30, 2014, assets were $45.8 billion, 15.0 percent higher than the previous year's assets of $39.9 billion.

The 17.4 percent rate of return, net of fees, is the ninth time since 2000 that TRS investments have exceeded the long-term investment assumption. It's also the 11th time in the last 15 years that investment returns were positive.

TRS Funded Ratio

Under the pension funding formula required by state law, for the first time in years the TRS funded ratio at the end of fiscal year 2014 did not decrease from the previous year, but remained level at 40.6 percent. The formula in state law requires the System's investment gains and losses to be averaged – or "smoothed" – over a rolling five-year period. Current market values are not used.

While an improved funded ratio is always good news, it doesn't mean by any means that the financial problems at TRS have been solved. TRS cannot invest its way out of its unfunded liability. TRS members still face a fiscal day of reckoning in the future unless a dramatic improvement is seen over time in the funded status.

TRS is still among the worst-funded major public pension system in the country. The System's funded status should be 100 percent, not 40 percent. Under any formula, TRS currently has about 40 cents for every dollar owed to the System's 395,000 members for their retirements. The last time the System's funded ratio improved in a year was in 2005 - 2006.

During fiscal year 2014, which ended in June, the TRS unfunded liability grew by 10.51 percent from $55.73 billion at the end of fiscal year 2013 to $61.59 billion. However, the System's funded ratio remained stable because strong investment returns helped assets grow at a pace similar to liabilities. Liabilities increased in part due to changes in actuarial assumptions.

State Contribution to TRS for Fiscal Year 2016

Based on the funding formula in state law, the TRS Board of Trustees in December gave approval to a $3.74 billion state government contribution for fiscal year 2016. This contribution covers the expected cost of TRS pensions to be earned in 2016, as well as funds to pay down the System's unfunded liability. By law, this contribution is reviewed by the Illinois State Actuary before final approval is given by the TRS Board of Trustees.

The fiscal year 2016 state contribution to TRS will be 9.7 percent greater than the contribution to be paid during the current fiscal year of $3.41 billion. More than 70 percent of current annual contributions goes toward paying off the System's growing unfunded liability, which is the result of 75 years of insufficient funding by state government.

When computing the state contribution each year, the TRS Board requires its actuaries, Buck Consultants of Chicago, to calculate the payment in three ways:

- The $3.74 billion is the state contribution required under the funding formula in current state law, which does not follow generally accepted actuarial standards.
- If generally used actuarial standards are applied to calculate the payment, the state contribution would be $4.37 billion in fiscal year 2016, a difference of 16.6 percent from the statutory requirement.
- If the state contribution is calculated with the goal of preventing any growth in the unfunded liability, the state payment would be $5.34 billion, or 42.6 percent higher than the contribution dictated by law.

TRS Trustee Candidate Petitions Available on TRS Website

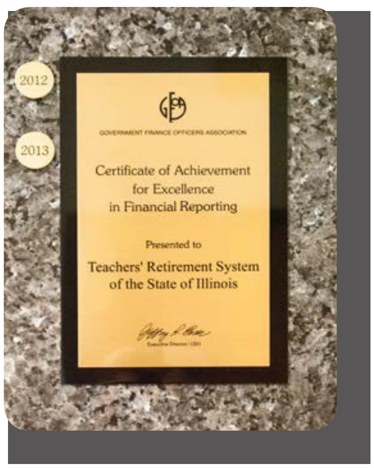
The election of two teacher trustees and one annuitant trustee to the TRS Board is set by law for Friday, May 1, 2015.

To be nominated and placed on the ballot, prospective candidates must collect and deliver to TRS a minimum of 500 eligible signatures as defined by state law.

Instructions for gathering signatures on the petitions, blank petitions and the Board election rules are available as PDF files on this page **http://trs.illinois.gov/trustees/election.htm** within the TRS website. Before circulating petitions, please carefully read the instructions. Completed and notarized petitions must be returned to TRS no sooner than Jan. 1, 2015 and no later than 4:30 p.m. on Jan. 30, 2015.

If you have any questions, please contact **TRS Administrative Services Manager Alice Kern** at **akern@trs.illinois.gov**.

TRS Receives Awards for Financial Reporting and Plan Administration



Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to TRS for its *Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2013. This was the 25th consecutive year that the System has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government or government entity 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 are submitting it to the GFOA to determine its eligibility for another certificate.

Public Pension Coordinating Council (PPCC) Recognition Award for Administration

TRS received the Recognition Award for Administration in 2014 in recognition of meeting professional standards for plan administration as set forth in the Public Pension Standards of the PPCC. The award is presented by the PPCC, a confederation of the National Association of State Retirement Administrators (NASRA), the National Conference on Public Employee Retirement Systems (NCPERS), and the National Council on Teacher Retirement (NCTR).

Board Information

Below is the calendar of upcoming Board meetings. Unless otherwise indicated, meetings will be held at the TRS Springfield Office, 2815 West Washington Street, Springfield, Illinois. The meetings generally begin Wednesday and continue until Friday, if necessary. This schedule is subject to change.

- Feb. 18-20, 2015
- March 30-31, 2015
  Hyatt Lodge
  Hamburger University
  Oakbrook, IL
- May 20-22, 2015
- June 25-26, 2015
  (tentative)

Important Annuitant Tax and Payment Reminders for 2015

Expect arrival of 1099-R

If you received a TRS benefit in 2014, the Office of the Comptroller will mail an IRS Form 1099-R to you by Jan. 31, 2015. This form will report your income received from TRS during 2014.

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 2014 was the first year that you received a benefit from TRS.

If you do not receive a 1099-R form by February 1, 2015 or you need a duplicate copy sent to you, please log in to the Member Account Access area. Annually after Feb. 1, you may request a duplicate 1099-R online for a prior year.

If you have not yet set up your online member account, please watch this video to learn how: **http://trs.illinois.gov/members/videos/acctAccess.htm**. Your member ID is required to set up an account. All annuitants received their member cards with their member IDs in July via email or mail.

Increase reflected on Feb. 1 check

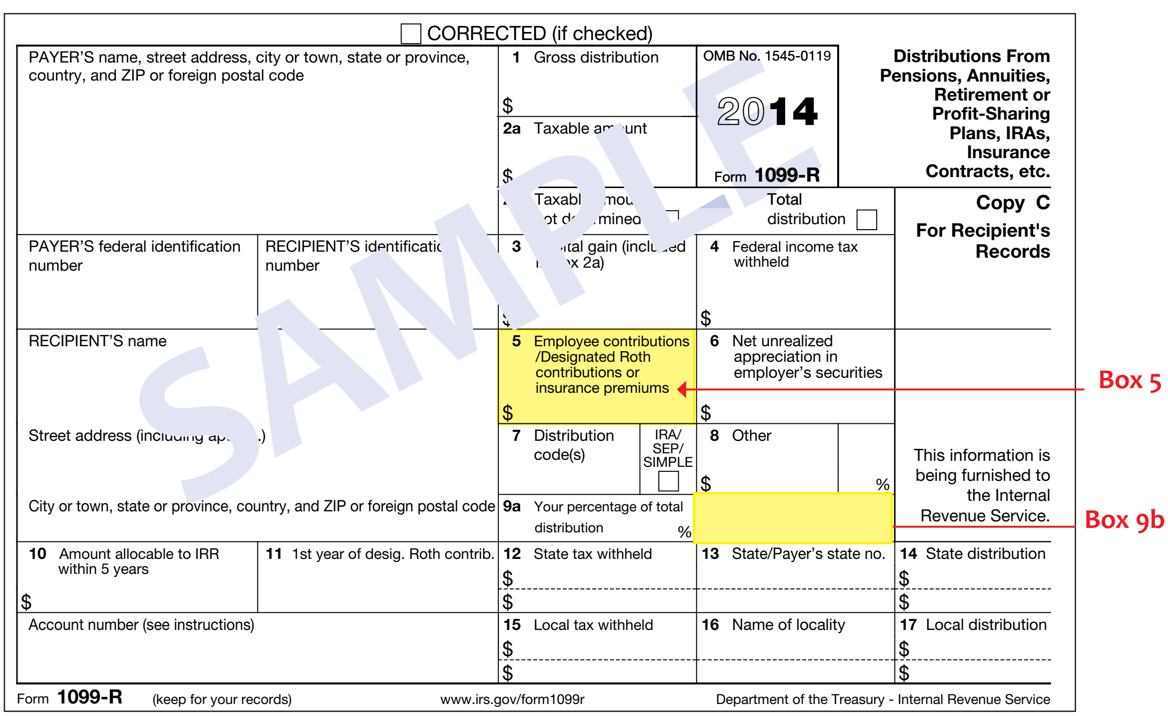
TRS pays your monthly annuity in arrears. The check issued Jan. 1, 2015 is your payment for the month of December. Cost-of-living adjustment (COLA) increases, certain insurance premiums and federal tax withholding changes will be reflected on the check issued Feb. 1, 2015, which is your monthly annuity for January 2015.

The checks you receive in January and February may be for different amounts if the January 2015 benefit payment received in February reflects your annual 3 percent post-retirement increase. With some exceptions, recipients of monthly survivor benefits will also see a 3 percent increase. The COLA increase is first effective on Jan. 1 following either your first retirement anniversary or your 61st birthday, whichever is later. TRS only sends a notification letter before your first COLA occurs. If you are not a new retiree, you may log in to the secure Member Account Access area to view your annual benefit amount changes. You may also view your monthly statements online in Member Account Access.

Tax withholding tables change

Revised federal income tax withholding tables will go into effect on Jan. 1, 2015. As a result, the federal taxes withheld from your Jan. 1, 2015 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 2015 tax year. If you are under-withholding, 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 may print a personalized Form W4-P online within the secure Member Account Access area after you have signed in. Additionally, you can obtain a new blank form by calling us at (800) 877-7896 and pressing "2" for our 24-hour Forms Order Line and selecting #600, by visiting **http://www.irs.gov/pub/irs-pdf/fw4p.pdf** for a blank Form W4-P or by calling your local Internal Revenue Service office. A new Form W4-P replaces any former version on file with TRS.



TRS Benefits Report Emailed to Active and Inactive Members in November

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, 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 was mailed to you in a letter this year or it can be located on the first page on the right side on a past printed TRS Benefits Report. You may also call us for your member ID, (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 2014 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.

No Leave of Absence Service Credit Purchases for Teacher Strikes

Am I eligible to purchase leave of absence optional service credit if I went on strike?

No. If you go on strike and receive less than 170 days paid in a fiscal year, you are not eligible to purchase those days as leave of absence service credit.

A strike is a voluntary work stoppage initiated by teachers and their respective representatives. A leave of absence is creditable as an approved leave if:

- the member did not resign,
- the employer promised renewed employment at the end of the leave,
- and the employer took official action to approve the request for the leave,
- or the leave qualifies as a leave under the Family Medical Leave Act, as certified by the employer.

In order to receive the maximum 1.000 year of service credit in a given fiscal year, you must be paid for at least 170 work days. A strike day is not considered a paid work day. Depending on the employment agreement and the number of unpaid strike days, you may or may not satisfy the paid 170-days worked requirement.

If the paid work days in a given fiscal year equaled 170 days or greater, you would receive 1.000 year of service credit. For example, an employment agreement was for 185 days and you went on strike for 13 days. You would be credited with 172 days paid (185 days – 13 days = 172 days paid) resulting in 172/170 = 1.000 year of service credit. The maximum of 1.000 year was attained.

If the paid work days in a given fiscal year were less than 170 days, you would receive less than 1.000 year of service credit. For example, an employment agreement was for 185 days and you went on strike for 20 days. You would be credited with 165 days paid (185 days – 20 days = 165 days paid) resulting in 165/170 = 0.971 of a year of service credit. Less than the 1.000 maximum was attained.

Teachers' Retirement System of the State of Illinois
2815 West Washington Street, P.O. Box 19253
Springfield, Illinois 62794-9253

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.

Office Information

2815 West Washington
P.O. Box 19253
Springfield, IL 62794-9253

4200 Commerce Court,
Suite 101
Lisle, IL 60532-3611

Phone

Toll Free: (800) 877-7896
TDD: (866) 326-0087

Forms Order Line

Toll Free : (800) 877-7896,
press "2" when prompted

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.

Find us on the Internet:

TRS website:
http://trs.illinois.gov

Facebook:
https://www.facebook.com/TRSIllinois

Twitter: **@ILLTRS**

Google+:
https://plus.google.com/+trsillinois/

YouTube+:
https://plus.google.com/+trsillinois/videos/

Topics & Report

Published by the Teachers' Retirement System of the State of Illinois

Editor: Kathy Boehme
kboehme@trs.illinois.gov

Layout: Jael Dunn

Printed by the authority of the State of Illinois.
online — Pub04 — 1/15