

IPPFA Regional Seminar

February 10, 2016



MJ ADKINS
DEPUTY DIRECTOR
PUBLIC PENSION DIVISION
ILLINOIS DEPARTMENT OF INSURANCE



Contacting the Public Pension Division



Internet:

<https://insurance.illinois.gov/Applications/Pension>

Mailing Address: Illinois Department of Insurance
Public Pension Division
320 West Washington Street, Room 575
Springfield, IL 62767

Phone: (217) 782-7542 or (800) 207-6958

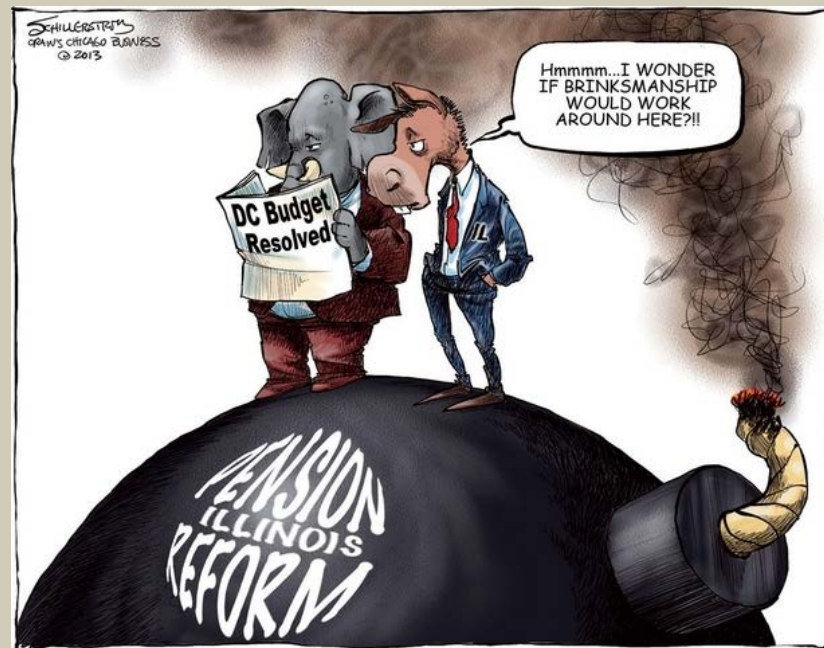
Fax: (217) 524-5978

Email: **doi.pension@illinois.gov**

Agenda



- ***DOI Public Pension Update - FOIA Portal, Audits***
- ***Financials Overview - State, Article 3 and 4***
- ***Municipal Underfunding and Enforcement Overview***



Public Pension FOIA Portal



- ***In September 2015, launched Freedom of Information Act (FOIA) Portal***
- ***Annual Statements, Complete Profile Reports and Actuarial Valuations currently available***
- ***Will be adding: Notices of Noncompliance, Director's Orders, Advisory Opinions, Reports of Examination, Financial Reports***
- ***Able to download in PDF/Excel format***
- ***www.insurance.illinois.gov***
- ***Questions? DOI.Pension@illinois.gov***



Compliance Audit Examinations



- **Updated Audit Procedure**
 - **Perform Audit (Desk or Field)**
 - **Issue DRAFT Audit Report**
 - **Fund may file written response within 2 weeks**
 - ✦ **No automatic extensions!**
 - ✦ **We may agree to additional time...+/- 30 days**
 - **Division issues Final Report (Report of Examination)**
 - **Fund has 30 days to request hearing**
 - ✦ **On facts contained in the Final Report (not Compliance)**
 - **Director's Order issued if no hearing requested**
 - **If hearing requested, will receive Notice of Hearing**
 - **Fund has 30 days to comply with Director's Order**
 - ***Even if no longer an issue, Finding stays in if found during Audit period.**

What is checked in an Audit?



- **Financial transactions, investment policies, and procedures;**
- **Books, records, documents, files, regarding financial, statistical, and administrative operations;**
- **Policies and procedures**
- **A determination of whether or not full effect is being given to the statutory provisions governing the operation of the pension fund;**
- **Determination if administrative policies effectively protect and preserve the rights of the participants;**
- **Financial and statistical records**
- **Benefit Calculations**

Common Findings



- ❑ **Calculation errors on retirement and disability pensions.**
 - Incorrect salary used as the basis for the calculation (Spikes, inclusion of non-pensionable salary).
 - Incorrect percentage used based upon pensioner's years of creditable service.
 - Errors in the calculation of cost of living increases.
- **Incomplete membership records** (birth certificates, application for retirement, marriage licenses, benefit calculations).
- **Failure to collect proper employee contributions.**
 - 9.455% of 'salary for pension purposes' for regular firefighter contributions, 9.91% of 'salary for pension purposes' for regular police officer contributions.
- **Incomplete meeting minutes** (Voting records not recorded, expenses or pensions not approved, minutes not signed).
- **Investments** in certain categories **exceed allowable limits.**

Financials and Funding Overview – 2014 Data



THE WALL STREET JOURNAL



"We're in good shape.
Nobody understands our financial statement."



State of Illinois Public Pension Statistics - 2014



- **Total Funds Regulated:** **672**
- **Total Participants:** **1.064 Million**
(Actives/Annuitants/Disabled/Survivors)
- **Aggregate Pension System Assets:** **\$158 Billion**
- **Total Yearly Benefits Paid:** **\$15 Billion**
- **Accrued Actuarial Reserve Liabilities:** **\$316 Billion**
- **Average Funding Condition:** **50% funded**

Article 3 and 4 Statistics - 2014



- **Total Funds Regulated:** **657**
- **Total Participants:** **40,412**
(Actives/Annuitants/Disabled/Survivors)
- **Aggregate Article 3 & 4 Assets:** **\$11.4 Billion**
- **Total Yearly Benefits Paid:** **\$880 Million**
- **Total Actuarial Liabilities:** **\$21.4 Billion**
- **Average Funding Condition:** **56.3% (Fire)**
57.2% (Police)

Suburban and Downstate Assets - 2014



- **Article 3:**

- **Net Present Assets (MV):** **\$7.1 Billion**
- **Investments:** **\$6.7 Billion**

- **Article 4:**

- **Net Present Assets (MV):** **\$5.1 Billion**
- **Investments:** **\$4.9 Billion**

Suburban and Downstate Liabilities - 2014



- **Article 3:**

- **Service Pension:** **\$5.9 Billion**
- **AL for Active Employees:** **\$5.1 Billion**
- **Total Actuarial Liability:** **\$12.3 Billion**

- **Article 4:**

- **Service Pension:** **\$4.0 Billion**
- **AL for Active Employees:** **\$3.9 Billion**
- **Total Actuarial Liability:** **\$9.1 Billion**

Suburban and Downstate Expenses - 2014



- **Article 3:**

- **Pension Payouts:** **\$500 Million**
- **Total Administrative Expenses:** **\$29 Million**
- **Total Expenses:** **\$530 Million**

- **Article 4:**

- **Pension Payouts:** **\$380 Million**
- **Total Administrative Expenses:** **\$22 Million**
- **Total Expenses:** **\$402 Million**

Article 3 & 4 Financials – What Does it Mean?



- ***Net Present Assets:*** ***\$12.2 Billion***
- ***Accrued Actuarial Reserve Liability:*** ***\$21.4 Billion***
- ***Expenses (including pension payments):*** ***\$932 Million***
- ***Contributions from Municipalities:*** ***\$659 Million***
- ***Unfunded Liability:*** ***57%***

Pension Funding



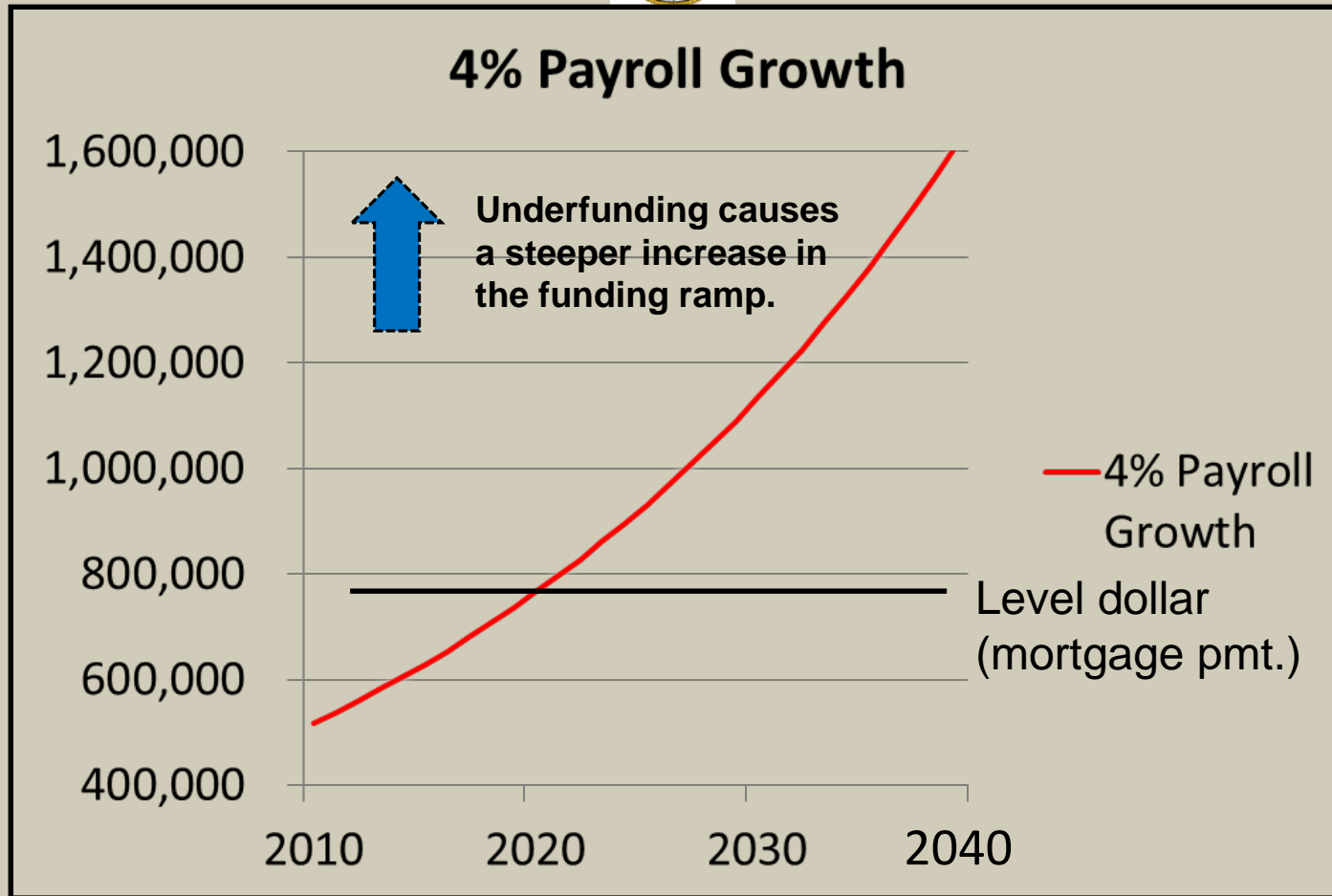
- ***Pension Funds are Funded by Municipal / Employee Contributions and Investment Income***
- ***Pension Funds spend money by paying pension benefits and expenses***
- ***Therefore...***
 - ***Municipal / Employee Contributions + Investment Income = Pension Benefits + Expenses***
 - ✦ ***This is the ideal equation***
 - ✦ ***When this equation is not balanced, that is when a fund experiences underfunding***

Basics: Municipal Funding



- ***Sections 3-125 and 4-118 of the Pension Code outline the municipal funding requirement:***
 - ***The City Council or the Board of Trustees ... shall annually levy a tax..., which when added to employee contributions and revenue available from other sources, will equal ...the annual actuarial requirements of the pension fund...***
- ***Annual Actuarial Requirements of the Fund:***
 - ***The normal cost of the pension fund for the year involved; and***
 - ***An amount sufficient to bring the total assets of the pension fund to 90% by 2040***
- ***Determined by an Enrolled Actuary employed by DOI, or by an Independent Enrolled Actuary employed by the Municipality or the Pension Fund***
 - ***Statute requires that DOI used Projected Unit Credit method (PUC) but many independent enrolled actuaries use the Entry Age Normal method. (EAN)***

Basics: Municipal Funding



Causes of Underfunding



Four Common Causes of Underfunding

- **Enhanced Benefits**
- **Low Return on Investments**
- **Common Pension Errors**
- **Municipal Underfunding**

Enhanced Benefits



- **Board awards benefits based on pensionable salary that includes non-pensionable salary items**
 - Retirement Incentives
 - Longevity not pro-rated
 - Holiday pay
 - Re-Entry into Active Service
- **Board Duty:**
 - Fiduciary Duty to the FUND (past, present, future)
 - Correction of Payments
- **Public Pension Division Limitations:**
 - Audit Findings
 - Advisory Opinions

Common Pension Errors



- **Mistake Language in Code**
 - 35 – day Administrative Review Law deadline
- **Board Duty:**
 - Fiduciary Duty to the FUND (past, present, future)
 - Encourage you to let DOI know of pending awards
- **Public Pension Division Limitations:**
 - Audit Findings
 - Advisory Opinions

Low Return on Investments



- **Investment Income is one half of the Fund's funding source**
- **Historical Rate of Return for Article 3 and 4 Funds is 4.95% for 10 years, 6.95% for 5 years**
- **Total \$12 Billion Investment Assets for 3 & 4 Funds**
- **Consolidation of Investment Assets**
 - **Increase in investment income**
 - ✦ **Economies of Scale**
 - ✦ **Increase Access to Asset Classes**
 - ✦ **Diversification**
 - **Decrease in cost of investments**

Municipal Underfunding – Funding Basics



- ***Sections 3-125 and 4-118 of the Pension Code outline the municipal funding requirement:***
 - ***The City Council or the Board of Trustees ... shall annually levy a tax..., which when added to employee contributions and revenue available from other sources, will equal ...the annual actuarial requirements of the pension fund...***
- ***Annual Actuarial Requirements of the Fund:***
 - ***The normal cost of the pension fund for the year involved; and***
 - ***An amount sufficient to bring the total assets of the pension fund to 90% by 2040***
- ***Determined by an Enrolled Actuary employed by DOI, or by an Independent Enrolled Actuary employed by the Municipality or the Pension Fund***
 - ***Statute requires that DOI used Projected Unit Credit method (PUC)** but many independent enrolled actuaries use the Entry Age Normal method. (EAN)***

Municipal Underfunding: What To Do About It



- ***Civil Enforcement – Section 1-115 of the Pension Code***
- ***Board of Trustees of the Riverdale Police Pension Fund v. Village of Riverdale***
 - ✦ ***Constitution pension protection clause extends to protecting pension benefits but do not extend to any expectation of a particular level of funding (reaffirming McNamee and Sklodowski decisions).***
 - ✦ ***No contractual right to funding unless can show that benefits are in immediate danger of being diminished (bankruptcy or default)***
- ***Section 3-124 – Insufficient Funds***
 - ***If at any time there is insufficient money in the fund to pay benefits, the city council or board of trustees shall make every legal effort to replenish the fund so that all beneficiaries may receives the benefits to which they are entitled***

Municipal Underfunding: What To Do About It



- ***Tax Levy Report***
 - ***Trustees Duty to the Municipality***
 - ***Annual Report on the Condition of the Pension Fund Each Fiscal Year***
 - ***Shall Include:***
 - ✦ ***Total Assets***
 - ✦ ***Estimated Employee Contribution***
 - ✦ ***Estimated Amount Required During Next Fiscal Year***
 - ***To Pay All Pensions***
 - ***Meet Annual Requirement Under Sections 3-125 and 4-118***
 - ***Funded Ratio***
 - ***Fund's Unfunded Liability***

DOI Enforcement of Municipal Funding



- ***Notices of Noncompliance – Section 1A-113(d)***
- ***Applies to Municipalities and Government Bodies***
- ***Process:***
 - ***Step 1: Written Notice***
 - ***Step 2: Immediate Steps Toward Compliance***
 - ***Step 3: If No Compliance, Hearing for Good and Sufficient Cause***
 - ***Step 4: If No Good Cause Shown, Order Compliance***
 - ***Step 5: If Still No Compliance, Civil Penalty***
 - ***Step 6: If Penalty Not Paid, Refer to Attorney General***

Notices of Noncompliance



- ***Written Notice of Noncompliance***
- ***Outline years of underfunding and amounts***
- ***Orders compliance be submitted to the Division***
- ***Municipalities have 30 days to comply***
 - ***Payment of last year's minimum statutory requirement; AND***
 - ***Plan for making future payments***



Noncompliance Hearings



- ***Hearing for Good and Sufficient Cause***
 - ***Evidence that, through no fault of the municipality, there was an unforeseeable delay or occurrence***
 - ***Evidence of an uncontrollable circumstance; and***
 - ***Evidence pertaining to Acts of God***
- ***Director will consider:***
 - ***Evidence or claims of ignorance of the Code and/or Regulations; and***
 - ***Evidence of irresponsibility and/or mismanagement on the part of the municipality***



Division Efforts



- ***Continuing communication with municipalities***
- ***Successes: \$3.2 Million into Funds***
- ***Weaknesses:***
 - ***Long Process***
 - ***Enforce most recent contribution requirement***
 - ***\$2,000 find per violation of a Director's Order***
 - ***If the penalty is paid, no referral to the Attorney General's office***

**JUST SOLVE THE
PROBLEM**

Intercept



- ***Starting in 2016, Municipalities and FPD subject to additional enforcement for failure to make full annual employer contributions***
- ***If payment is 90 days late, the Fund can certify the amount owed to the Illinois State Comptroller***
- ***Pension Fund must give notice to the municipality of this***
- ***Intercept***
 - ***2016: 1/3 of Amount Delinquent***
 - ***2017: 2/3 of Amount Delinquent***
 - ***2018: Full Amount Delinquent***



Future of Public Pensions



1919 Pension Laws Commission Report



“The commission has made a very exhaustive study of the subject...Among other things, however, that commission has found that nearly all, if not all, of the several pension funds are hopelessly insolvent. These funds were established with wholly inadequate provisions for their future...I recommend that your Honorable Body give its fullest consideration to this entire subject.”

Governor Frank O. Lowden, Message to the General Assembly, January 8, 1919

Questions?

