

Pension Consolidation Act Illinois Legislative Update

On December 18th, 2019, Governor Pritzker officially signed [Public Act 101-0610](#) into law, which then took effect January 1st, 2020. A large portion of this new law (the “Pension Consolidation Act”) requires all 649 Illinois suburban and downstate police and firefighters pension funds — previously established as prescribed by Articles 3 and 4, respectively, of the Illinois Pension Code — to consolidate their assets into two new statewide funds: one for all police pension funds and one for all firefighter pension funds.

The Pension Consolidation Act was largely based on the recommendations of the Illinois Pension Consolidation Feasibility Task Force established by Governor Pritzker last February, which issued its [findings](#) in October 2019. After evaluating the expenses and returns of the investment portfolios of the Article 3 and 4 pension funds, the task force reported that on average, the relatively small size of most of these funds resulted in lower investment returns as well as higher investment expenses than their larger statewide counterparts. The task force concluded that by consolidating the investment portfolios of these funds, the new statewide funds would gain access not only to a broader range of investment opportunities that can provide higher returns, but also to more competitive investment fees, and that the expenses associated with managing their assets and administering benefits would be lowered.

The Pension Consolidation Act addresses several of the task force’s recommendations:

- Establishes the Police Officers’ Pension Investment Fund, which will oversee approximately \$8.7B in combined assets;
- Establishes the Firefighters’ Pension Investment Fund, which will oversee approximately \$6.3B in combined assets;
- Creates both a transition and permanent Board of Trustees for each consolidated fund;
- Establishes a timeline for the consolidation process;
- Provides some benefit enhancement for “Tier 2” employees.

The Pension Consolidation Act also stipulates that all assets and liabilities of all existing Article 3 and 4 pension funds will stay under the ownership of each local pension board in order to ensure that the financial condition — including, but not limited to, pension benefit funding levels and ratios — of one participating pension fund will not affect the financial condition of any other participating pension fund.

TIMELINE OF CONSOLIDATION PROCESS

The Pension Consolidation Act establishes the following timeline for the consolidation process:

| By no later than February 1, 2020: | By no later than January 1, 2021: | By no later than July 1, 2022: |
|---|--|--|
| The Governor is responsible for appointing Trustees to the transition boards for the consolidated Police Officers' Pension Investment Fund and the Firefighters' Pension Investment Fund that will serve until a permanent board is in place. | The consolidated investment funds must hold elections for the Trustees of the permanent board for each fund. | All assets of existing local Article 3 and 4 pension funds must be transferred to the respective consolidated investment fund. |

ONGOING RESPONSIBILITIES AND REQUIREMENTS OF LOCAL BOARDS

Under the Pension Consolidation Act, all existing Article 3 and 4 pension boards will relinquish investment authority for the management of their pension assets and will cease to exercise fiduciary responsibility once their assets are transferred into the respective consolidated fund. However, all local boards will continue to maintain sole authority to determine and award disability benefits, retirement benefits, and survivor benefits.

Additionally, the Pension Consolidation Act reduces the training requirements for Trustees of local boards, lowering the requirement for new Trustees from 32 hours to 16 hours and lowering the requirement for annual renewal of existing Trustees from 16 hours to eight hours. The law also requires four hours of specialized training related to the changes being implemented by the whole of Public Act 101-0610.

TRANSITION BOARDS AND PERMANENT BOARDS OF CONSOLIDATED FUNDS

Both the transition board and permanent board for each consolidated fund will be composed of nine trustees, with five trustees representing active employees and retiree beneficiaries and four trustees representing municipalities. Each board will be required to meet at least quarterly.

Each Transition Board of Trustees shall select its chairperson from among its board's trustees for the duration of the transition board's tenure.

Permanent Board Trustees will serve terms of either two or four years based on representation, as defined in the Act. The chairperson of each Permanent Board will also be selected by the board from among the trustees. The chairperson will serve a term of two years and each two-year term must alternate between employee and employer trustees.

The trustees will be instated under various stipulations, with each fund's Transition and Permanent Board of Trustees comprised as follows on the next two pages.

Police Officers' Pension Investment Fund

| TRANSITION BOARD | | | |
|--|--|---|---|
| Appointed by the Governor by 2/1/20 | | | |
| 3 members representing active employees | 2 members representing retiree beneficiaries | 3 members representing municipalities | 1 member representing the IL Municipal League |
| <i>with</i> | <i>with</i> | <i>appointed from</i> | |
| 2 candidates recommended by the IL Fraternal Order of Police | 1 candidate recommended by the IL Fraternal Order of Police | candidates recommended by the IL Municipal League | |
| 1 candidate recommended by the IL Police Benevolent and Protective Association | 1 candidate recommended by the IL Police Benevolent and Protective Association | + are mayors, CEOs, CFOs, other officers, executives, or department heads of municipalities | |

| PERMANENT BOARD | | | |
|--|---|---|---|
| Seated by no later than 1/1/21 | | | |
| 3 members who are active participating employees | 2 members who are retiree beneficiaries | 3 members that are mayors, presidents, CEOs, CFOs, or other officers, executives, or department heads of municipalities that have participating pension funds | 1 member recommended by the IL Municipal League |
| <i>elected by</i> | <i>elected by</i> | <i>elected by</i> | <i>appointed by</i> |
| active participants | beneficiaries | the mayors and presidents of municipalities that have participating pension funds | the Governor with the advice and consent of the IL Senate |

Firefighters' Pension Investment Fund

| TRANSITION BOARD | | |
|---|---|---|
| Appointed by the Governor by 2/1/20 | | |
| 3 members representing active employees | 1 member representing retiree beneficiaries | 1 member representing the Associated Fire Fighters of IL |
| <i>recommended by</i> | <i>recommended by</i> | <i>who is</i> |
| the Associated Fire Fighters of IL | the Associated Fire Fighters of IL | a participant |
| 3 members that are mayors, presidents, CEOs, CFOs, or other officers, executives or department heads of municipalities or fire protection districts | | 1 member representing the IL Municipal League |
| <i>appointed from</i> | | |
| candidates recommended by the IL Municipal League | | |

| PERMANENT BOARD | | |
|--|---------------------------------------|--|
| Seated by no later than 1/1/21 | | |
| 3 members who are active participating employees | 1 member who is a retiree beneficiary | 1 member recommended by the Associated Fire Fighters of IL |
| <i>elected by</i> | <i>elected by</i> | <i>appointed by</i> |
| active participants | beneficiaries | the Governor with the advice and consent of the IL Senate |
| 3 members that are mayors, presidents, CEOs, CFOs, or other officers, executives, or department heads of municipalities or fire protection districts that have participating pension funds | | 1 member representing the IL Municipal League |
| <i>elected by</i> | | |
| mayors and presidents of municipalities or fire protection districts that have participating pension funds | | |

TRANSITION OF ASSETS

The transition board will be responsible for coordinating the transition of assets of all existing local Article 3 and 4 pension funds (“transferor pension funds”) into the respective consolidated investment funds as soon as practical and by no later than July 1st, 2022. As part of the transition process, the transition board is authorized to retain the services of custodians, investment consultants, and other professional services it deems prudent to implement the transition of assets. The permanent board will not be bound by any contracts or agreements for services entered into by the transition board.

In order to transition the assets of a transferor pension fund, the transition board will be required to notify the board of trustees of each transferor pension fund of its intent to assume fiduciary control of the pension fund’s assets and the date on which it will assume control (“transfer date”). This must be delivered in writing at least 30 days in advance of the transfer date. Upon receipt of the letter, the transferor pension fund is required to promptly notify its custodian, as well as any and all entities with fiduciary control of any portion of the pension assets.

Prior to transitioning any assets of transferor pension funds, the transition boards will be required to audit the investment assets of each transferor pension fund in order to obtain a certified asset list. Once obtained, the certified asset list must be provided to the transferor pension fund and the transfer of assets must be initiated within 10 business days. In order to maintain accuracy of the certified investment list, transferor pension funds will be prohibited from purchasing or selling any securities once the asset list has been obtained.

Transferor pension funds retain sole fiduciary and statutory responsibility for the management of their pension assets until the start of business on the transfer date, at which point all statutory and fiduciary responsibility for the assets will be shifted to the consolidated fund. Within 30 days of the transfer date, the consolidated fund shall provide a receipt for the transfer of assets.

NEXT STEPS

There is still some uncertainty regarding the implementation and timing of the transition. It will likely take several months for service providers (i.e., custodians, investment consultants, transition managers, auditors, etc.) to be retained by the transition board. Once that process begins, there should be some additional clarity on the expected timeline.

As the transition boards begin the implementation of the Illinois Pension Consolidation Act, a well thought out transition plan will be paramount to ensure success of the consolidation process. At this early stage, we believe the following points to be of utmost importance:

- **Governance:** Key documents should be thought out and drafted. These include a framework for the development and adoption of an investment policy statement as well as the implementation, management, and oversight of this policy.
- **Infrastructure:** Proper structure is significantly important when creating a new fund. The transition boards should take the initiative and time to create well thought out and appropriate infrastructure and governance models up front, which will avoid duplicate work down the road.
- **Internal Personnel:** The transition of individual pension funds into one plan will require both significant internal and external resources. Key internal positions include the Executive Director as well as a staff of investment professionals. Consideration should be given to individuals who have institutional investment experience and/or who have previously managed/worked for large public pension retirement systems.

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- **External Personnel:** The request for proposal process should be initiated as soon as possible for fund counsel, independent investment consultant, third-party custodian, auditor, transition manager(s), and ultimately investment managers. Experienced external hires who have experience with both Illinois Article 3 and 4 public pension funds as well as larger state retirement systems will be extremely valuable resources to both the transition and permanent boards.
 - **Transition Plan:** A clear plan outlining the timeline and objectives, including the order in which each individual pension fund will be transitioned needs to be developed. Priority should be given to the pension funds who may benefit most immediately from consolidating assets, particularly those with less than \$10 million that are subject to the most investment restrictions by current state statute and that often have higher investment expenses. A well thought out plan will ensure that all parties are on the same page throughout the process.
 - **Implementation:** The transition will be massively complex. A best practices document with clear, specific, and consistent instructions should be given to all individual pension funds prior to their transition date. When the transition date arrives, existing boards should focus on making sure best practices are utilized throughout the transition to ensure as minimal market impact and cost as possible.

Marquette will continue to monitor new announcements closely and will provide regular updates to our Article 3 and 4 pension fund clients as details emerge. Once transfer dates have been communicated, we will work with the consolidated funds, auditors, and any other necessary service providers to ensure our clients experience a transition that is as seamless as possible. As always, your consultant can answer any questions directly. ■

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