

General Memorandum 652

To: All Authorized Agents

November 17, 2014

Re: Voluntary Payments to Reduce the Unfunded Actuarial Accrued Liability

We encourage each Authorized Agent to share this memorandum with their unit of government's financial administrators.

Executive Summary

Some IMRF employers carry Unfunded Actuarial Accrued Liability (UAAL). While part of an employer's annual contribution rate goes toward paying down UAAL, IMRF employers may choose to make additional payments to pay down the liability more quickly. An employer who makes additional payments to reduce its UAAL faces unique rewards and risks.

If you are interested in discussing the rewards and risks of voluntary payments, please contact IMRF's Chief Financial Officer Mark Nannini at 630-368-5345. To maximize potential benefits, it is important to make additional contributions before year-end.

Your employer contribution rate and your UAAL

Your employer annually pays a contribution rate set by IMRF. The rate your employer pays is broken down in your Contribution Rate Notice in the Document Archive of [Employer Access](#).

Each employer's contribution rate includes a portion to pay the Normal Cost of an IMRF pension. The Normal Cost is the cost to the employer of the members' pension benefits earned in a given year. For employers who carry UAAL, the contribution rate includes a portion called a Funding Adjustment. The Funding Adjustment goes toward paying interest and principal on UAAL. The UAAL carries a 7.5% interest charge.

For 2015 employer contribution rates:

- The UAAL is amortized over 28 years for employers with the ability to levy property taxes. The amortization period will reduce each year until it reaches 15 years, at which time it will become a rolling 15-year amortization period.
- The UAAL is amortized over a rolling 10-year period for employers without the ability to levy property taxes.

When an amortization period becomes a rolling period, the remaining UAAL is effectively refinanced each year. That means, theoretically, that the remaining UAAL will never be paid off.

Voluntary payments and your UAAL

Some IMRF employers opt to make voluntary payments specifically designated to pay down the UAAL. An employer who makes voluntary payments to reduce its UAAL faces unique rewards and risks.

Rewards:

- **The employer will reduce its employer contribution rate.**
For example, an employer with an \$8 million UAAL and an IMRF payroll of \$12.7 million would reduce the Funding Adjustment portion of its employer contribution rate from 3.48% to 3.43% with a \$100,000 payment. This would result in a reduction in employer contributions of \$6,350 on an annual basis.

- **If IMRF investments earn in excess of the 7.5% assumed rate of return in a given year, the employer will receive additional credit to its employer reserve account.**

The reason for this credit is that employers—as sponsors of a defined benefit plan—bear the rewards of investment returns. The amount of the credit is enhanced by the magnitude of the additional employer contribution to pay down its UAAL. (A smaller UAAL results in a larger employer reserve balance; a larger employer reserve balance results in a larger credit.)

Risks:

- **If IMRF investments earn less than the 7.5% assumed rate of return in a given year, the employer will receive an additional charge to its employer reserve account.**

The reason for this charge is that employers—as sponsors of a defined benefit plan—bear the risks of investment returns. The amount of the charge is enhanced by the magnitude of the additional employer contribution to pay down its UAAL. (A smaller UAAL results in a larger employer reserve balance; a larger employer reserve balance results in a larger charge.)

Contact IMRF

If you are interested in discussing the rewards and risks of voluntary payments, please contact IMRF's Chief Financial Officer Mark Nannini at 630-368-5345. To maximize potential benefits, it is important to make additional contributions before year-end.