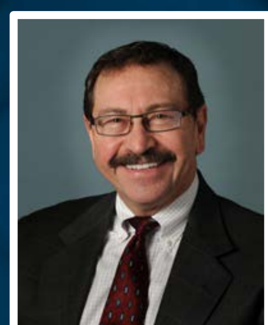
PENSION SPIKING AND THE ACCELERATED PAYMENT

Facts and Good Practice

Presented by



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PROUD LEGACY BRIGHT FUTURE

1941 - 2016

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Agenda

- **What is Pension Spiking?**
- **Legislative Mandates:**
  - The 125% Rule
  - The Pension Impact Statement
  - The Accelerated Payment

What is
Pension Spiking?

Pension Spiking, sometimes referred to as "salary spiking:"

A unit of government increases a public employee's pay just prior to retirement in order to provide a pension larger than he or she would normally have been entitled to based upon a normal salary progression.

Example:

- **Government Employee**
  - Age 60 married
  - 20 years of service
  - $40,000 annual salary
  - **Receives $20,000 increase (+50%)**

$60,000 ANNUALLY

12 months later…

- **Government Employee**
  - **Receives <u>ANOTHER</u> $20,000 increase (+50%)**

$80,000 ANNUALLY

- **Retires 1 year later (age 62)**

Pension Spiking

- **Present Value *without* the spiking:**

  $206,716.63

- **Present Value *with* the spiking:**

  $298,149.88

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Pension Spiking

After taking into account
the member contributions plus interest,
the total cost to the employer for the spiking is:

$82,754.97

This is Pension Spiking

Pension Spiking

- IMRF employers make monthly contributions to prefund employees’ future pensions.
- Actuaries assume average pattern of salary increases when setting rates.
- At retirement, a pension is fully funded by the employer reserve, barring unusual salary increases.

IF

an employee's salary increases past typical range before retirement,

THEN

the amount needed to fund the employee's future pension increases.

THE SHORTFALL = AN UNFUNDED LIABILITY

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Who is responsible for paying the unfunded liability?

The Employee?	**NO**
The Local Unit of Government?	**YES**
The Taxpayers?	**YES**

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To fund increased liability:

- IMRF removes funds from the employer's reserve account.

- Because there is less money in the reserve for other employees, IMRF must increase the employer's future contribution rate.

As a result…

Future generations
of taxpayers
are paying the costs of a
spiked pension.

Legislative Mandates

The 125% Rule

- Effective January 1, 1964
- Applies to ***all*** IMRF active members
- Caps the amount of reported earnings used for calculating pension benefits

The 125% Rule – Tier 1

Limits earnings used in the pension calculation in the final 3 months of a member's FRE period, to no more than 125% of the highest earnings in any single month during the first 45 months of the FRE period.

The 125% Rule – Tier 2

Limits earnings used in the pension calculation in the final 24 months of a member's FRE period to no more than 125% of the highest earnings in any single month during the first 72 months of the FRE period.

The 125% Rule – Tier 1

Highest month of earnings in the first 45 mos. of member's FRE is **$3,000**

Earned **$4,500 / mo.** in the last 3 months

125% Rule:
125% of $3,000 is $3,750

IMRF will use **$3,750 / mo.** for the last 3 months for calculating FRE

Because **$4,500 exceeds $3,750**, IMRF uses $3,750 per month for the last three months for calculating the member's FRE.

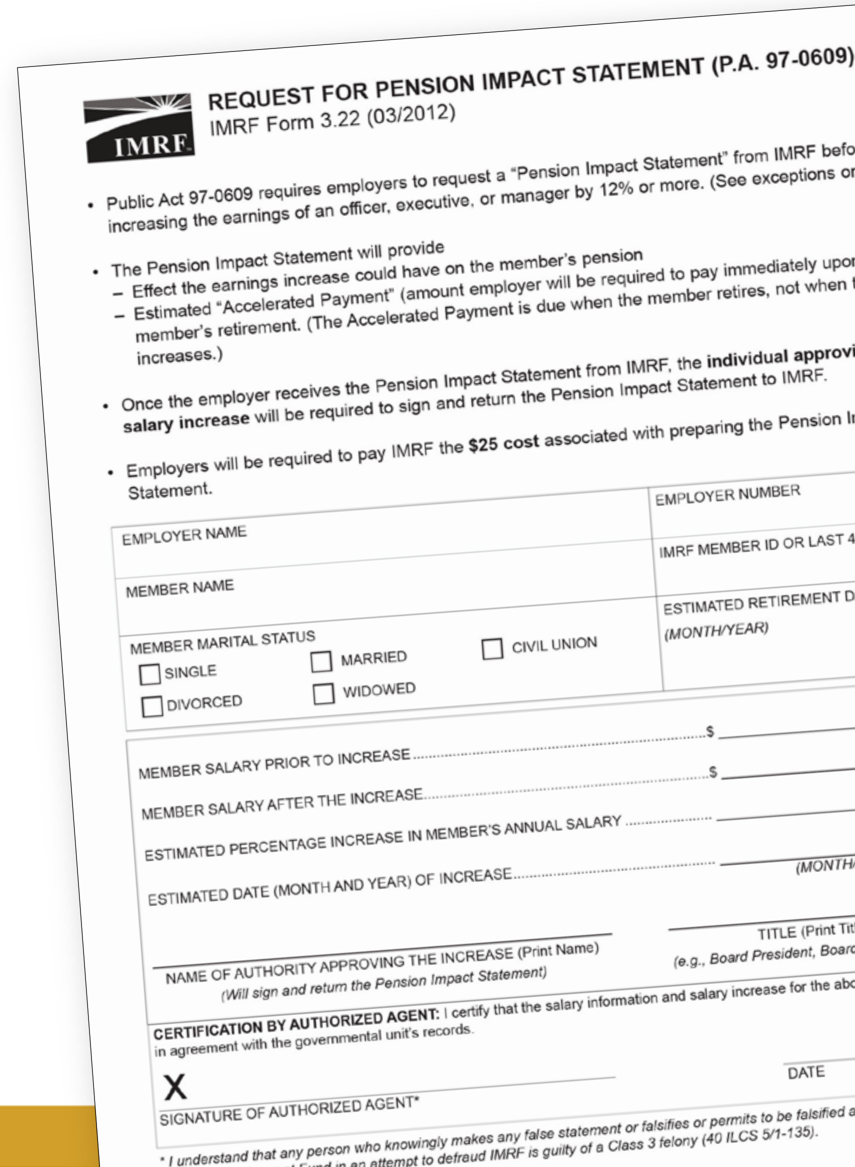
Pension Impact Statement

- Public Act 97-0609 effective January 1, 2012

- Employers must request a Pension Impact Statement ***before*** increasing the earnings of an officer, executive, or manager by 12% or more.

Pension Impact Statement

- **IMRF Form 3.22, “Request for Pension Impact Statement”**
- IMRF will provide the resulting effect the salary increase could have:
  - On the employee’s pension
  - On the estimated Accelerated Payment due from the employer at the employee’s retirement



REQUEST FOR PENSION IMPACT STATEMENT (P.A. 97-0609)
IMRF Form 3.22 (03/2012)

- Public Act 97-0609 requires employers to request a “Pension Impact Statement” from IMRF befo[…] increasing the earnings of an officer, executive, or manager by 12% or more. (See exceptions o[…]
- The Pension Impact Statement will provide
  - Effect the earnings increase could have on the member’s pension
  - Estimated “Accelerated Payment” (amount employer will be required to pay immediately upo[…] member’s retirement. (The Accelerated Payment is due when the member retires, not when […] increases.)
- Once the employer receives the Pension Impact Statement from IMRF, the **individual approv[…] salary increase** will be required to sign and return the Pension Impact Statement to IMRF.
- Employers will be required to pay IMRF the **$25 cost** associated with preparing the Pension I[…] Statement.

EMPLOYER NAME | EMPLOYER NUMBER

MEMBER NAME | IMRF MEMBER ID OR LAST 4[…]

MEMBER MARITAL STATUS
☐ SINGLE ☐ MARRIED ☐ CIVIL UNION
☐ DIVORCED ☐ WIDOWED

ESTIMATED RETIREMENT D[…] *(MONTH/YEAR)*

MEMBER SALARY PRIOR TO INCREASE .... $

MEMBER SALARY AFTER THE INCREASE .... $

ESTIMATED PERCENTAGE INCREASE IN MEMBER’S ANNUAL SALARY ....

ESTIMATED DATE (MONTH AND YEAR) OF INCREASE .... *(MONTH[…]*

NAME OF AUTHORITY APPROVING THE INCREASE (Print Name)
(Will sign and return the Pension Impact Statement)

TITLE (Print Tit[…]
(e.g., Board President, Boar[…]

CERTIFICATION BY AUTHORIZED AGENT: I certify that the salary information and salary increase for the abo[…] in agreement with the governmental unit’s records.

X
SIGNATURE OF AUTHORIZED AGENT* | DATE

** I understand that any person who knowingly makes any false statement or falsifies or permits to be falsified a[…] Fund in an attempt to defraud IMRF is guilty of a Class 3 felony (40 ILCS 5/1-135).*

Pension Impact Statement

- Upon receipt, the employer must consider the Pension Impact Statement and determine whether to move forward with the increase.

- The individual approving the increase is required by law to sign the statement and return it to IMRF.

Pension Impact Exemptions

- Increases for members who are more than 10 years from retirement.
- Increases from standard employment promotions that result in increased responsibility and workload.
- Increases due to (or because of) an increase in the number of hours to be worked.
- Increases from contracts or collective bargaining agreements entered, amended, or renewed before January 1, 2012.

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The Accelerated Payment

- Public Act 97-0609 effective January 1, 2012

- Many employers may not be aware of the resulting effect of compensation decisions on long-term pension costs.

The Accelerated Payment

- Under Public Act 97-0609, employers are required to immediately pay the total additional cost of a pension resulting from end-of-career salary increases of 6% or more.

- The statement must be paid immediately.

The Accelerated Payment

The present value of the member's pension

MINUS

The present value of the member's pension, without wages in excess of 6%, during the FRE period

THE PENSION COST DUE TO SPIKING

LESS

Contributions on the excess wages

EQUALS

ACCELERATED PAYMENT INVOICE AMOUNT

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The
Accelerated Payment
IS NOT a penalty.

Between January 1, 2012, and December 31, 2015, IMRF issued:

3,258

ACCELERATED PAYMENT INVOICES

776

SEPARATE EMPLOYERS

TOTAL: $28,640,500

The Accelerated Payment

- Accelerated Payment invoice is due within 90 days
- 7.5% interest assessed after 90 days
- Total amount, plus interest, must be paid within 3 years

The Accelerated Payment

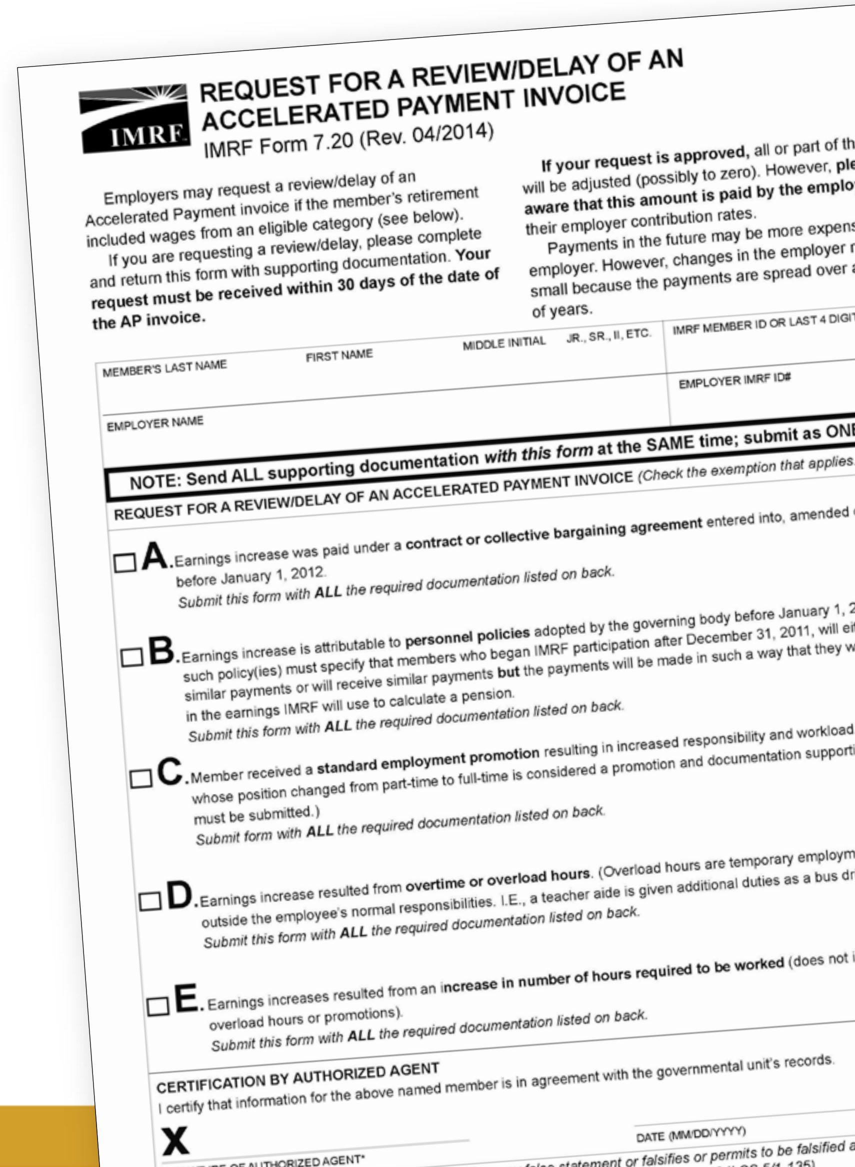
- IMRF recommends …
  PAY THE ACCELERATED PAYMENT INVOICE RIGHT AWAY

- Delays will cost much more to pay off the balance

Accelerated Payment Exemptions

- **IMRF Form 7.20,**

  “Request for a Review/Delay of an Accelerated Payment Invoice”



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REQUEST FOR A REVIEW/DELAY OF AN ACCELERATED PAYMENT INVOICE

IMRF Form 7.20 (Rev. 04/2014)

Employers may request a review/delay of an Accelerated Payment invoice if the member's retirement included wages from an eligible category (see below).

If you are requesting a review/delay, please complete and return this form with supporting documentation. **Your request must be received within 30 days of the date of the AP invoice.**

If your request is approved, all or part of th will be adjusted (possibly to zero). However, **ple aware that this amount is paid by the emplo** their employer contribution rates.

Payments in the future may be more expens employer. However, changes in the employer r small because the payments are spread over a of years.

MEMBER'S LAST NAME	FIRST NAME	MIDDLE INITIAL	JR., SR., II, ETC.	IMRF MEMBER ID OR LAST 4 DIGIT
EMPLOYER NAME				EMPLOYER IMRF ID#

NOTE: Send ALL supporting documentation *with this form* at the SAME time; submit as ONE

REQUEST FOR A REVIEW/DELAY OF AN ACCELERATED PAYMENT INVOICE *(Check the exemption that applies*

☐ **A.** Earnings increase was paid under a **contract or collective bargaining agreement** entered into, amended before January 1, 2012.
*Submit this form with **ALL** the required documentation listed on back.*

☐ **B.** Earnings increase is attributable to **personnel policies** adopted by the governing body before January 1, 2 such policy(ies) must specify that members who began IMRF participation after December 31, 2011, will ei similar payments or will receive similar payments **but** the payments will be made in such a way that they w in the earnings IMRF will use to calculate a pension.
*Submit this form with **ALL** the required documentation listed on back.*

☐ **C.** Member received a **standard employment promotion** resulting in increased responsibility and workload whose position changed from part-time to full-time is considered a promotion and documentation supporti must be submitted.)
*Submit form with **ALL** the required documentation listed on back.*

☐ **D.** Earnings increase resulted from **overtime or overload hours**. (Overload hours are temporary employm outside the employee's normal responsibilities. I.E., a teacher aide is given additional duties as a bus dr
*Submit this form with **ALL** the required documentation listed on back.*

☐ **E.** Earnings increases resulted from an **increase in number of hours required to be worked** (does not i overload hours or promotions).
*Submit this form with **ALL** the required documentation listed on back.*

CERTIFICATION BY AUTHORIZED AGENT

I certify that information for the above named member is in agreement with the governmental unit's records.

X

DATE (MM/DD/YYYY)

Accelerated Payment Exemptions

Earnings increases:

- Due to promotion
- Resulting from overtime hours
- Resulting from an increase in the number of hours required to be worked
- Paid under a collective bargaining agreement entered into, amended, or renewed before January 1, 2012
- Attributable to certain personnel policies adopted before January 1, 2012. *<u>The earnings increases must be limited to those employed before January 1, 2012.</u>*

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The Accelerated Payment

Example of a personnel policy that would exempt earnings increases from the Accelerated Payment:

Personnel policy adopted **May 13, 2006**, providing for cash-outs of accrued sick leave at termination.

Policy is amended **October 1, 2011**

***BEFORE**
January 1, 2012

The amended policy provides that employees hired **on or after October 1, 2011** are not eligible for cash payments for accrued sick leave.

THIS AMENDED PERSONNEL POLICY WILL EXEMPT SICK LEAVE CASH-OUTS PAID TO EMPLOYEES HIRED BEFORE OCTOBER 1, 2011, FROM THE ACCELERATED PAYMENT.

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The Accelerated Payment

An example of a personnel policy that will not exempt the earnings increases from the Accelerated Payment:

Personnel policy adopted **May 13, 2006**, providing for cash-outs of accrued sick leave at termination.

Policy is amended to limit cash-outs to employees hired before **January 1, 2012**, but the date of the amendment is later than **December 31, 2011**.

THIS AMENDED PERSONNEL POLICY <u>WILL NOT</u> EXEMPT THE CASH-OUTS PAID FROM THE ACCELERATED PAYMENT.

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The Accelerated Payment

An example of a personnel policy that will not exempt the earnings increases from the Accelerated Payment:

Personnel policy adopted **May 13, 2006**, providing for cash-outs of accrued sick leave at termination.

Policy is amended **October 1, 2011**, to provide that the employer will not report to IMRF the payments for accrued sick leave for employees hired on or after **October 1, 2011***.

Employer has no authority to determine what payments are reportable to IMRF.

THIS AMENDED PERSONNEL POLICY <u>WILL NOT</u> EXEMPT THE CASH-OUTS PAID FROM THE ACCELERATED PAYMENT.

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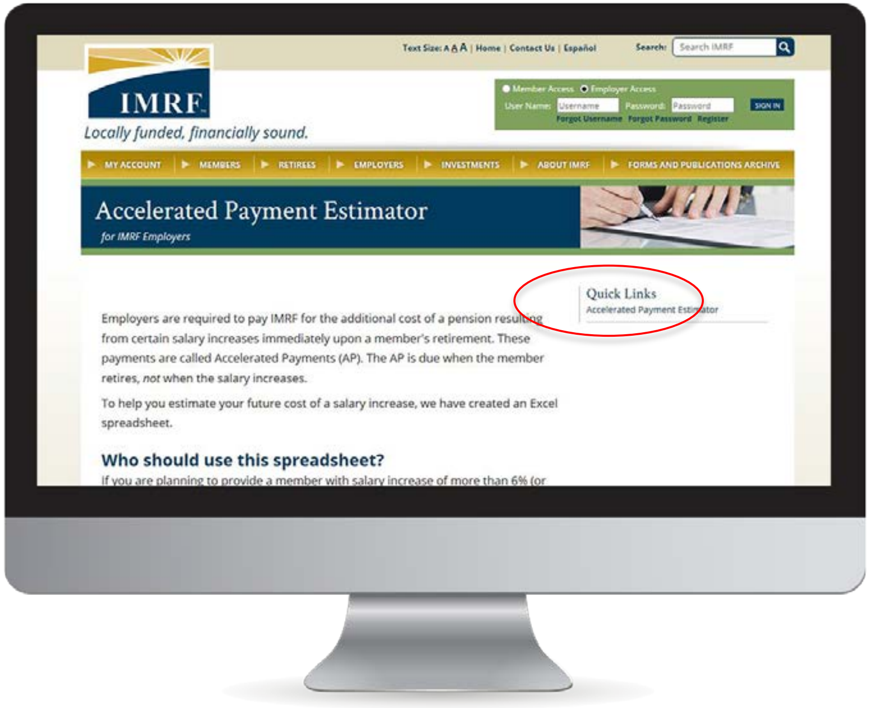
Accelerated Payment Estimator



Located online:

www.imrf.org

Remember…

Ultimately, your unit of government's taxpayers will be responsible for the impact of your employer's compensation decisions on long-term pension liabilities.

Resources

1) Contact your **Field Representative**

2) Accelerated Payment Estimator, **www.imrf.org**

3) Section 7.20E of the ***Manual for Authorized Agents***

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Do you have any questions?

Thank you!

Employer-Only Phone Number: 1-800-728-7971

Online Resources: www.imrf.org

***Employer Digest* electronic newsletter**