PENSION NEWSLETTER – MAY 2019

At the May 2019 Pension Board meeting there was a spirited debate amongst the trustees concerning the publication of the Secretary's April letter. Traditionally, the Secretary's letter is published to communicate issues that the Board is facing or discussing. Many years ago, the Secretary would occasionally politic on an item that the Board did not feel was relevant and was a distraction to the administration of the pension fund. Due to the Secretary's politicking, the Board adopted a policy requiring the Secretary to submit his letter to the Board for approval. Last month, Secretary Tony Martin submitted a letter addressing a policy I had proposed and the Board had been discussing. The policy proposal recommends that the Board would monitor the total amount of active member payroll contributions and compare it to assets on hand. My view, is that the active members' contributions should not be used to subsidize retired members' benefits; active members' contributions and statutory interest should always remain in the fund.

The Board had a productive discussion on the policy, most notably around what the Board would do if the assets fell below the active members' contributions, which would effectively be taking active members payroll deductions to fund retiree benefits. I suggested a policy that if the active members' contributions were ever to exceed a certain percentage of the Fund's assets that we would send a written correspondence to the fund sponsor, the City of Chicago. The communication would state that the Board has a policy of keeping the plan sponsor aware of any potential substantive actions it may take. Additionally, the communication would state that an identified financial threshold has been breached that requires the Board to consider, on principal, the partial suspension of benefits. And finally, a stated expectation that the City will provide the funds required to 'un-breach' the threshold, at a specific date, determined by the Fund. The impetus for the policy that I proposed was on moral and prudent grounds; the concern active members are subsidizing retiree members benefits; and the trustee's shared fiduciary responsibility to speak up, in particular when funding reaches critically low levels.

The Board's focus then turned to the legality of the Board having the authority to withhold payments. Members may recall that the Board dealt with a similar issue back in 2017 when trustees voted to withhold a portion of members' benefits because the City had failed to submit the funding earmarked specifically for that benefit. I am opposed to diminishing any member's benefits that are clearly supported by the pension code. But unfortunately, because the City has been negligent, we now have our collective backs up against the wall and the plan sponsor needs to be put on notice.

During the Board's initial discussion of the policy, the Board's legal counsel brought up the recent Illinois Appellate Court decision concerning the City of Harvey pension crisis [*Board of Trustees of the City of Harvey Firefighters' Pension Fund v. City of Harvey*, 2017 IL App (1^{st}) 153074]. I was critical of Tony Martin's letter for not including this most relevant and recent case. In the *Harvey* case, the Appellate Court addresses the important question of when a pension fund is near the verge of default or imminent bankruptcy. This is a critical definition because that is the threshold, established by the Illinois Supreme Court, when a participant or pension board can sue the plan sponsor for adequate funding. In our case this would be the City of Chicago. Prior to the Appellate Court ruling, in all the cases Tony Martin mentions, a lawsuit for adequate funding would be difficult because of a lack of understanding of what "near the verge of default or imminent bankruptcy" meant. In the *Harvey* case, the Illinois Appellate Court defines what constitutes "near the verge of default".

Tony Martin's letter did not go out in April because I objected to it, primarily for two reasons. First, I took exception to Tony Martin writing a letter on the debate between the trustees, because he left the meeting early to attend a Hazmat class in order to maintain his Tech B license. I feel, at a minimum, he should have been in attendance for the entire meeting if he was going to write about it. Second, Tony Martin's letter was very biased towards a legal analysis completely ignoring the financial and economic facts that have been facing this Board for well over a decade. Tony Martin's letter didn't even provide a thorough legal analysis, and instead dragged out the same old tired arguments that will easily get overrun by economic realities. I appreciate the view our pension benefits are guaranteed by the Illinois Constitution, as Tony Martin endlessly reminds the membership, but as I have written before, if our Fund, currently hovering at a 19% funding ratio, runs out of money, retirees cannot pay for essentials like prescription drugs with a copy of the Illinois Constitution. The Constitution matters, but at this point in the Fund's history, funding matters more.

I do not appreciate, nor will I support, utilizing fund assets to perpetuate misinformation out into the field. Tony Martin can say his letter is factual, and from an uninformed sophomoric viewpoint it is 'factual'. But when your opinion is so one sided with 'cherry picked' facts and you refuse to present another aspect of the situation, you are essentially being untruthful to a membership that is expecting a reliable size up of the situation.

So a pension fund member may ask - <u>Are active members subsidizing current benefit payments to retirees?</u> A good starting point is the annual statement the pension fund mails to your home every year indicating how much money you, specifically, have put into the pension fund. If a FF/EMT were to come on when I did, in 2003, by the end of 2017 that FF/EMT would have an individual account of approximately $123,000 at the pension fund. If that same FF/EMT was able to take the refundable portion of his payroll deduction and invest it in an S&P500 index fund every quarter, a very simple automated option to implement, he would have over $224,000. This choice to invest your pension fund payroll deduction into a simple index fund would provide a 15 year FF/EMT with an additional $100,000, or 80% more money than he would have at the pension fund. And remember, in Tony Martin's view, as stated in his recent letter, that money doesn't really belong to that particular FF/EMT. **So from a strictly economic perspective, active members are losing an opportunity to earn meaningful returns on their payroll deductions because they are forced to participate in a fund that is structurally deficient and is not supporting their future retirement benefit.**

Let me be clear on two issues. First, I am not proposing a policy to allow any pension fund member the option to invest their pension fund payroll deductions themselves. I used this example to illustrate the opportunity costs active members pay to sustain a structurally deficient pension plan. Second, the retiree benefits being paid are a promise and we must be willing to viciously engage in battle if anyone tries to diminish them or continues a policy to underfund them, not just on a month to month basis, but on a long term view that extends out many decades. I do not support reducing benefits for any pension fund members; as I have clearly stated before, I think all members deserve a fully funded retirement benefit calculated using a 3% compounded COLA under the Tier I pension language. Members that do the same job should get the same benefit!

Brothers and sisters, I bring these issues to your attention to make you aware that the City is not doing their part, in the partnership, to secure our retirement security. We are doing our part making payroll contributions, and it is imperative we keep the City in check. I appreciate the responsibility you entrusted in me, I do not take it lightly. Please be safe and look out for one another in the field as the weather gets warmer.

Tim McPhillips - Active pension fund trustee

Timothy J McPhillips