STATE OF ILLINOIS
OFFICE OF THE
AUDITOR GENERAL
Frank J. Mautino, Auditor General

REPORT DIGEST

2020 ANNUAL REVIEW

Release Date: November 2020

Review performed in accordance with **Public Act 95-708**

Office of the Auditor General
Iles Park Plaza
740 E. Ash Street
Springfield, IL 62703

Phone: (217) 782-6046
TTY: (888) 261-2887

The full report is available on our website:
www.auditor.illinois.gov

EXECUTIVE SUMMARY

Review of Information Submitted by the Retirement Plan for Chicago Transit Authority Employees

The Illinois State Auditing Act requires the Retirement Plan for Chicago Transit Authority Employees (Retirement Plan or Plan) to submit to the Office of the Auditor General (OAG) an audit, an annual statement, and an actuarial statement by September 30 of each year. The OAG reviewed the documents submitted by the Retirement Plan and concluded that they met the requirements of the Auditing Act.

The funded ratio of the Retirement Plan decreased slightly from 52.62 percent in the January 1, 2019 Valuation to 52.55 percent in the January 1, 2020 Valuation. When the funded ratio declines below 60 percent, the Pension Code requires that contribution rates be increased so that the funded ratio is projected to reach 60 percent within 10 years. The contribution rates certified by the Retirement Plan Board for 2021 were **unchanged** from the 2020 contribution rates. For both 2020 and 2021, the employer contribution rate is 20.647 percent (which is net of the employer debt service credit of 6% of pay) and the employee contribution rate is 13.324 percent.

The January 1, 2020 Actuarial Valuation concluded that the contribution rates applicable for Plan year 2021 would result in the Plan's funded ratio reaching the statutorily required 60 percent level within 10 years (i.e., by 2030) and therefore, there was no need to increase the contribution rates.

The OAG and our consultant, Aon, reviewed the Retirement Plan's assumptions contained in the January 1, 2020 Actuarial Valuation and concluded that they were not unreasonable in the aggregate. However, we believe that two of the assumptions, investment return and inflation, should be monitored and justified on an annual basis. We have consistently made this recommendation for a number of years. However, the **Retirement Plan failed to annually review** either of these two assumptions as recommended. If the Retirement Plan again fails to monitor and justify these two critical assumptions prior to next year's valuation, the likelihood increases that these assumptions may fall outside of what we consider reasonable.

The 8.25 percent investment return assumption used by the Plan is at the upper edge of reasonable based on the Plan's asset allocation and remains at the upper end of investment return assumptions used by other plans. The underlying inflation assumption is on the upper end of the reasonable range based on current and recent historical capital market assumptions. The Plan's investment advisor conducted projections that found an expected 10-year return of 8.18 percent.

This report does not constitute an audit as that term is defined in generally accepted government auditing standards.

ANNUAL REVIEW RESULTS AND CONCLUSIONS

STATUTORY REQUIREMENTS

The OAG reviewed the documents submitted by the Retirement Plan and concluded that they met the requirements of the Auditing Act.

The Illinois State Auditing Act (30 ILCS 5/3-2.3(e)) requires the Retirement Plan for Chicago Transit Authority Employees (Retirement Plan or Plan) to submit to the Office of the Auditor General (OAG) an audit, an annual statement, and an actuarial statement by September 30 of each year.

- On September 30, 2020, the Auditor General received these documents from the Retirement Plan.
- The OAG reviewed these documents and concluded that they met the requirements of the Auditing Act.

In addition, the Illinois Pension Code (40 ILCS 5/22-101(e)(3)) requires the Retirement Plan to determine, based on a report prepared by an enrolled actuary, the estimated funded ratio of the Retirement Plan's total assets to its total actuarially determined liabilities.

- The Plan is also required to determine the employee and employer contribution rates needed to meet funding requirements established by the Pension Code.
- The Auditor General is required to review the determination and the assumptions on which it is based and determine whether they are "unreasonable in the aggregate". (pages 4-5)

REVIEW OF ACTUARIAL VALUATION

The Retirement Plan submitted the Actuarial Valuation as of January 1, 2020, to the OAG on September 30, 2020. This Actuarial Valuation was presented to the Retirement Plan Board at its July 23, 2020 meeting. At that meeting, the Board of Trustees accepted the January 1, 2020 Actuarial Valuation and certified the employer and employee contribution rates for 2021.

The Retirement Plan's assumptions were not unreasonable in the aggregate.

The OAG and our consultant, Aon, reviewed the Retirement Plan's assumptions contained in the January 1, 2020 Actuarial Valuation and concluded that they were not unreasonable in the aggregate. The investment return assumption continues to be higher than most public plans but is supported by an investment return analysis conducted by the Plan's investment advisor and a high underlying inflation assumption. The underlying inflation assumption is on the upper end of the reasonable range based on current and recent historical capital market assumptions.

While we recognize the Plan's policy of completing an experience study every five years, we believe that **these two assumptions, investment return and inflation, should be monitored and justified on an annual basis**. We have consistently made this recommendation for a number of years.

However, **the Retirement Plan failed to annually review** either of these two assumptions as recommended. If the Retirement Plan again fails to monitor and justify these two critical assumptions prior to next year's valuation, the likelihood increases that these assumptions may fall outside of what we consider reasonable.

In 2019, the Plan's actuary completed an experience study for the five year period ending December 31, 2017. An experience study assesses how well assumptions used by the Plan align with the actual experience of the Plan. If past experience differs from the assumptions used, then the actuary may recommend revisions to the assumptions used in future valuations. As a result of the experience study, several of the assumptions used in the Plan's January 1, 2019 Actuarial Valuation were revised. However, the investment return assumption remained unchanged at 8.25 percent. In the Plan's January 1, 2020 Actuarial Valuation, there were no changes in actuarial assumptions compared to the prior year.

Our prior reviews have concluded that the investment return assumption used by the Plan was at the upper range of investment return assumptions for comparable plans. The 8.25 percent investment return assumption is at the upper edge of reasonable based on the Plan's asset allocation and remains at the upper end of investment return assumptions used by other plans. The Plan's December 31, 2019 Investment Report shows that the Plan's investments have earned 7.7 percent over the past 10 years. The Plan's investment advisor conducted projections that found an expected 10-year return of 8.18 percent. We recommend that the investment return and inflation assumptions should be monitored and justified on an annual basis.

Key Retirement Plan Information	
Plan investment return assumption	8.25%
10-year historical rate of return	7.7%
Plan assets	$1.883 billion
Plan liabilities	$3.584 billion
Funded ratio	52.62%
Employee contribution rate (2021)	13.324%
Employer contribution rate (2021)	20.647%

The Retirement Plan's active participant headcount decreased from the prior year. Additionally, the ratio of active participants to annuitants continued to decrease. A study sponsored by the National Association of State Retirement Administrators titled the *Public Fund Survey Summary of Findings for FY 2018* states "*When combined with an unfunded liability, however, a low or declining ratio of actives to annuitants can cause fiscal distress for a pension plan sponsor….*" (pages 4-9)

CONTRIBUTION RATES

The Pension Code requires the Chicago Transit Authority (CTA) to contribute 12 percent of pay, less up to a 6 percent credit for debt service paid on the bonds issued for contribution to the Retirement Plan; employees are required to pay 6 percent of pay. The Pension Code further requires that contribution rates be increased if the funded ratio is projected to decline below 60 percent prior to 2040, with the CTA paying two-thirds and employees paying one-third of the required contribution.

The funded ratio of the Retirement Plan decreased slightly from 52.62 percent in the January 1, 2019 Valuation to 52.55 percent in the January 1, 2020 Valuation. At January 1, 2020, the Plan's assets totaled $1.883 billion and the actuarial accrued liability was $3.584 billion, according to the Plan's January 1, 2020 Actuarial Valuation.

Since the funded ratio of the Plan was below 60 percent in the January 1, 2020 Valuation, the Pension Code requires the Plan to "*…determine the increased contribution required each year as a level percentage of payroll during the years after the then current year…so the funded ratio is projected to reach at least 60% no later than 10 years after the then current year and include that determination in its report.*" (40 ILCS 5/22-101(e)(3)) The contribution rates certified by the Retirement Plan Board for 2021 were unchanged from the 2020 contribution rates. For both 2020 and 2021, the employer contribution rate is 20.647 percent (which is net of the employer debt service credit of 6% of pay) and the employee contribution rate is 13.324 percent.

The January 1, 2020 Actuarial Valuation concluded that the contribution rates applicable for Plan year 2021 would result in the Plan's funded ratio reaching the statutorily required 60 percent level within 10 years (i.e., by 2030) and therefore, there was no need to increase the contribution rates. (pages 9-11)

AGENCY REVIEW

A draft of this Review was provided to the Retirement Plan for their review.

This report does not constitute an audit as that term is defined in generally accepted government auditing standards.

This Annual Review was conducted by OAG staff with the assistance of our consultant, Aon.

SIGNED ORIGINAL ON FILE

JOE BUTCHER
Division Director

This report is transmitted in accordance with Section 3-14 of the Illinois State Auditing Act.

SIGNED ORIGINAL ON FILE

FRANK J. MAUTINO
Auditor General

FJM:DJB