Village of La Grange

VILLAGE OF LA GRANGE

SPECIAL MEETING OF THE
VILLAGE BOARD OF TRUSTEES

Village Hall Auditorium
53 South La Grange Road
La Grange, IL 60525

Monday, October 26, 2009
(immediately following the regular Village Board meeting)

AGENDA

1. CALL TO ORDER AND ROLL CALL

2. PENSION FUND WORKSHOP

   A. OVERVIEW AND INTRODUCTIONS
      Liz Asperger, Village President
      Robert Pilipiszyn, Village Manager

   B. STATE REQUIREMENTS FOR LOCAL POLICE AND FIRE PENSION FUNDS AND RECENT STATE-WIDE ISSUES
      Joe Mc Coy, Senior Legislative Advocate – Illinois Municipal League

   C. VILLAGE OF LA GRANGE – PENSION FACTS AND REVIEW
      Dick Barrett, Managing Director–Investments, Wells Fargo Securities
      Fred Lantz, Partner, Director of Government Services & Dan Berg, Partner, Sikich LLC

   D. QUESTIONS

   E. CONTINUED DISCUSSION – MONDAY, NOVEMBER 9, 2009
      Liz Asperger, Village President

3. ADJOURNMENT

Individuals with disabilities and who require certain accommodations to participate at this meeting are requested to contact the ADA Coordinator at (708) 579-2315 to allow the Village to make reasonable accommodations.

VILLAGE OF LA GRANGE
Administrative Offices

BOARD REPORT

TO: Village President, Village Clerk,
Village Board of Trustees and Village Attorney

FROM: Robert J. Pilipiszyn, Village Manager
Lou Cipparrone, Finance Director

DATE: October 26, 2009

RE: **PENSION FUND WORKSHOP**

OVERVIEW

In follow up to this year's budget workshop discussion concerning the funding status of the Village's two municipal pension funds (Police and Fire), we have scheduled a Village Board workshop on this issue.

The purpose of the workshop is two-fold. First, it is to provide the Village Board with a comprehensive understanding of the following:

- state pension requirements and emerging issues;
- pension fund portfolio performance and current economic conditions;
- report on the financial condition of our pension funds by the Village's auditing firm; and
- latest actuarial results and how they impact the Village's preliminary property tax levy for its two municipal pension funds.

Second, based on the foregoing, the direction being sought from the Village Board is a policy decision as to whether the Village should and, if so, to what extent, increase the property tax levy to enhance funding of its police and fire pension funds above the annual actuarial required contribution.

The pension workshop itself will be divided into two sessions. The first session, scheduled for Monday, October 26, will serve as a primer on municipal pension funds and the current funding status of our two funds. The second session, scheduled for Monday, November 9, will provide the Village Board with an opportunity to have a discussion on the funding status of our two municipal pension funds, which will serve as a springboard going into a discussion of the Village's preliminary 2009 property tax levy.

To aid in the Village Board's understanding of this matter, we have prepared a pension fact sheet (see attached). We have also identified and invited several consultants to participate in the workshop. The first presenter will be Joe Mc Coy, senior legislative advocate for the Illinois Municipal League. Mr. Mc Coy will explain state pension requirements, describe current statewide trends and update the Village on legislation which could effect the current deadline of 2033 for achieving full funding status.

The second presenter will be Dick Barrett of Wells Fargo Securities. Mr. Barrett will review historic investment returns, asset allocation, current economic conditions, and other issues effecting portfolio returns for our two pension funds.

The third presenter will be Fred Lantz, senior partner at Sikich LLC, our auditors. Mr. Lantz will discuss findings from an "independent review" of our pension funds. The added benefit to Mr. Lantz's participation is his firm's familiarity with our financial practices and financial condition.

The final presenter will be Tim Sharpe (attending the November 9 Village Board meeting), the independent actuary engaged by both of our pension fund boards. Mr. Sharpe will present the latest actuarial results and the preliminary property tax levy for each fund.

VILLAGE POLICY – PENSION FUND LEVIES

It has been the Village's long-standing policy to fund annual contributions (tax levies) for the Police and Fire Pension Funds as determined by an independent actuarial valuation. When the full-funding status legislation was last amended by the State in 1993, the Village affirmed its policy by committing to annually fund the minimum required annual contribution in order for the pension funds to reach 100% funded status by 2033. As long as the Village continues to fund the minimum required annual contribution, both funds will achieve full-funding status within the statutorily – prescribed timeframe.

This policy has served the Village well in two ways. First, the Village has met its pension obligations and will continue to do so in a financially reasonable and responsible manner. Second, this financially sound approach has allowed the Village to make funds available under the overall property tax levy for general corporate purposes. In other words, the Village has not over-taxed its residents by over-funding its pension contribution requirements.

Historically, the Village has treated its pension fund levies very conservatively, and thus, they are the first to be funded by the Village's property tax levy. As these two obligations have consistently grown over the years at a rate higher than the Consumer Price Index, which is the limiting factor for increasing the property tax levy, there is less and less property tax revenue available for general operating purposes. Absent some structural shift to the property tax system in Illinois, such as removing pension fund levies from under the tax cap, this trend will continue. The Village has been able to off-set the impact of pension fund levies as an ever-increasing proportion of its property tax levy as part of our five-year budget process through revenue enhancements, temporary reduction in capital expenditures and operational efficiencies / General Fund revenues.

State law requires that pension benefits be paid by a municipal tax levy. The State has a history of increasing benefits without a corresponding revenue source or relief to municipalities (unfunded state mandates). Coupled with property tax cap limitations, one can begin to see the financial challenges and burdens placed on municipalities to adequately fund pension contributions.

STAFF OPINIONS

We would like to provide the Village Board of Trustees several staff observations and opinions. First, both of our pension fund boards have a professional understanding that pension fund management is a long-term strategy. They are disciplined investors and do not take this responsibility lightly. Because of this operational control, no current employees or retirees have expressed to us concerns with the funded status of either pension fund. The discussion is squarely with Village Board.

Second, in the event of a catastrophic loss of public safety personnel in the line of duty, we would be able to and recommend the issuance of bonds to ensure survivor benefits and to not impair the underlying integrity of the effected pension fund.

Third, pension funds are "living" funds; there is an ebb and flow based on individual retirement plans, unanticipated disabilities, and other factors. They will live beyond the current fully funded deadline of 2033, unlike mortgages which have a defined end date.

Fourth, we (staff and pension boards in concert) are doing the best we can in this economy. There have been volatile swings in this decade, many towards the downside. Perhaps these economic conditions have prompted more of a short-term focus than a long-term perspective.

OPTIONS

Two years ago, when prompted by a member of the Village Board, Tim Sharpe provided his opinion on the subject matter of enhanced pension funding when the 2007 actuarial results were presented. Mr. Sharpe made three salient points:

1. stay the course on funding;

2. a significant, one-time financial contribution from general fund reserves ($500,000) had little impact on funding status (a couple percentage points); and

3. the Village may be better served by using those tax payer dollars elsewhere recognizing that the Village was meeting its pension obligations.

At that time Mr. Sharpe also noted that the La Grange pension funds have the ability to meet pension payment requirements for the next 10 years even if no additional income was earned during that period which speaks to the overall financial condition of the fund.

Mr. Sharpe has most recently provided us with preliminary results for the 2009 Police and Fire pension levies, and the increases are significant; Fire $773,525 ($179,958 from last year's levy) and Police $823,760 ($258,826 from last year's levy). The increases are directly a result of investment losses incurred in each fund last year. The budget impact is substantial, especially in the out years. This is approximately $325,000 more than we had budgeted for in FY 2010-11.

Options available to the Village Board are as follows:

1. Maintain annual required contributions. This would result in approximately $325,000 in additional pension fund contributions each year. As this amount is an unanticipated expense, we would need to offset it with either reduced capital and/or operating expenditures. We could incorporate the increased pension levies into our budget for one year. Beyond that, if there is no legislative relief, we would need to consider decreasing the levies.

2. According to Village Attorney Mark Burkland, the only legal requirement for the Village is to reach fully-funded status by 2033. There is no legal requirement to make annual contributions.

   Another option for the Village is to increase pension contributions by 10% annually. The current budget includes a 10% increase for FY 2010-11, and 5% in subsequent years.

   We would have similar budgetary issues as the first option, but to a lesser extent.

   Because of similar investment loss experiences, the other municipal employee retirement fund (IMRF) has implemented a similar phase-in approach to provide the flexibility to moderate the significant increases in the employer contribution (tax levy) while maintaining the commitment to fully fund the pension plans over a reasonable time period. Future year tax levies will be adjusted as subsequent year investment activity is factored into the actuarial valuations.

3. Go back to utilizing a five-year smoothed market method of recognizing gains and losses, which would result in a $200,000 reduction in the annual required contributions. We would still however have a budget gap of approximately $125,000.

Beginning with the 2006 property tax levy, both actuarial valuations for the Police and Fire Pension Funds changed from the 5-year smoothed market method of recognizing gains and losses to the actual market method, based upon a recommendation from our actuary, Tim Sharpe. The primary reason for changing to the actual method is based on the assumption that the investment portfolio will incur earnings annually, on an ongoing basis and not fluctuate between years with losses and gains. As the stock market is generally upwardly biased, there is no reason to leave deferred gains unrecognized if we expect gains in subsequent years also. Using the 5-year smoothed market method we were typically deferring only gains to future years with no offsetting losses. In addition, in years where losses are incurred, the loss is still amortized over the remaining unfunded liability period, therefore the impact of the loss is already being deferred. This method is more straight forward in calculating the value of the investment portfolio as there is no longer a difference in actual asset value and actuarial asset value.

PRELIMINARY RECOMMENDATIONS

It is our recommendation that the Village fund its pension levies according to the independent actuarial valuations for the 2009 Property Tax Levy.

Further, if market conditions do not improve or legislative relief is not forthcoming, we would have to review our current policy to fund pursuant to the actuarial required contributions and consider a reduced funding option (e.g. – 10% cap) for FY 2011-12 and subsequent years.

Based on the information contained in this report, the Village is not in a position to "enhance" funding to its two municipal pension funds above the annual actuarial required contribution at this time.

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VILLAGE OF LA GRANGE
PENSION WORKSHOP
INFORMATION SHEET
OCTOBER 26, 2009

1. STATE REQUIREMENTS – BACKGROUND INFORMATION

- **Overview of Downstate Police & Fire Fighter Pension Systems**
- **Summary of Aggregate Financial Information**
- **Role of the Illinois General Assembly**
- **Pension Reform Efforts**

The La Grange Police and Firefighters pension plans are single-employer, defined benefit plans.

Municipal pensions are governed by the following:

Illinois Pension Code (40 ILCS 5/) Article 1 – General Provisions
Illinois Pension Code (40 ILCS 5/) Article 3 Police Pension Fund - Municipalities 500,000 & Under
Illinois Pension Code (40 ILCS 5/) Article 4 – Fire Pension Fund - Municipalities 500,000 & Under

Although the pension funds are regulated by state statute, no state funding is received, nor is the state able to access or utilize the pension funds for state obligations.

Legislative relief may come in the form of:

- extension of the full funded amortization period for downstate police and firefighter pension funds from 2033 to 2049. Legislation introduced (SB 2011) no action taken to date.
- annual 10% increase in pension levies for 10 years (revised SB 2011)
- removal of pension fund levies from underneath the property tax caps
- moratorium or reduction in pension benefits

2. LA GRANGE PENSION FUNDS – INVESTMENT AND FINANCIAL INFORMATION

A. INVESTMENT INFORMATION

- **Investment Policies**
- **State Regulated Investments**
- **Investment Benchmarks**
- **Capital Market Assumptions**

Police and Fire Pension Funds investment policy objectives include:
- first and foremost, the safety and preservation of principal
- diversify investments to avoid incurring unreasonable risk regarding specific security types
- remain sufficiently liquid to meet all operating requirements
- seek to maximize investment returns, consistent with risk limitations

- invest in securities, pursuant to state stature, which over the term of an economic cycle, will equal or exceed market-average rate of returns from comparable portfolios

Investment Income – Investments regulated by (40 ILCS 5/1-113)

Investments are regulated by (40 ILCS 5/1-113.4). A pension fund's total investment in stocks, equities and variable annuities shall not exceed 45% of the market value of the pension fund's net present assets stated in its most recent annual report on file with the Illinois Department of Insurance. The remaining funds (55%) shall be invested in fixed investment instruments including: government securities, backed by the full faith and credit of the US government (bonds, notes, agencies), fixed annuities, certificates of deposit and cash.

The 45% equity section of the La Grange Police and Fire pension fund portfolios reflect a long term, conservative growth model consisting of 15% large cap, 9% mid cap, 5% small cap, 15% international and 1% cash.

Standard industry benchmarks are utilized in order to monitor equity investments returns, with underperforming managers and/or funds being replaced.

The most recent 5 & 10 year investment returns from Tim Sharpe are attached. These portfolio returns have been compared to a blended index and to comparable municipal pension funds as follows:

- Blended Index: 40% S&P 500 index & 60% Barclays (Lehman Bros) Aggregate Bond index; based upon average pension portfolio composition of equities and fixed investments.

Blended Index 5 year: 2.01%	Blended Index 10 year: 2.71%
Police Pension 5 year: 2.47%	Police Pension 10 year: 3.051%
Fire Pension 5 year: 2.69%	Fire Pension 10 year: 3.053%

- Three year comparison of 18 local municipal police pension funds and 14 local municipal fire pension funds / fire protection districts. (Available information from Dept of Insurance website for: FY 2001-02, FY 2004-05, FY 2005-06)

Downstate Police Pension Funds average return: 4.52%
La Grange Police Pension Fund: 5.91%

Downstate Fire Pension Funds average return: 4.67%
La Grange Firefighters Pension Fund: 5.32%

It took several years for the equities market to recover from the significant decline in the early 2000's resulting from the collapse of technology stocks. Historically, significant losses in equity markets are followed by positive returns.

The pension funds remain positioned to participate in the anticipated recovery of the domestic and international markets. (Average return of equity investments in La Grange Police and Fire pensions from May 1 through September 30, 2009 are approximately 23.5%)

Moreover, even though the pension funds experienced negative returns from variable annuities over the past year, these types of investments are long term in nature and historically average returns of between 8%-10%.

History demonstrates that the value of a well-diversified portfolio, comprised of fixed and variable investment products, will outperform other financial assets such as government securities, bonds and cash over long periods of time.

B. AUDITED FINANCIAL INFORMATION

- **Village Required Annual Contribution**
- **Actuarial Assumptions**
- **Funded Status**
- **Management Letter Comments**

The Village of La Grange is committed to annually fund the minimum required annual contributions (tax levies) for the Police and Fire Pension Funds, as determined by independent actuarial valuations.

Village funding of the required annual contribution over the past five for the Police and Fire pension funds averaged 98.6% and 99.2%; respectively. Funding varies annually depending upon final property tax collections (see attached audit table).

Key actuarial assumptions are reasonable:

- Salaries – 5%, plus 5% step years 1-6
- Interest Rate – 7.5%
- Percent Funded – Police 70.6%; Fire 56.5% (as of 4/30/2008)
- Asset Valuation – Market
- Retirement – Beginning at age 50, maximum age 70, several years ago the retirement age assumption was changed from a normal bell curve distribution to shift the probability of an officer retiring closer to age 50 rather than 70.

Funding progress over the past five years has been significantly impacted by lower than anticipated investment returns due to equity market conditions. The Police Pension funded status decreased from 76.1% in 2003 to 70.6% in 2008, the Fire Pension funded status decreased from 63.9% in 2003 to 56.5% in 2008 (see attached audit table).

According to Tim Sharpe, the average funded status for police & fire pension funds with actuarial valuation dates in 2008, was approximately 55%-60%

Sikich compared previous year information from municipalities who received the 2008 Certificate of Achievement in Financial Reporting, with actuarial valuation dates in 2007. The average percent funded status for municipal police and fire pension funds was 68.1% and 72.0%; respectively, with the La Grange Police and Fire Pension funds at 75.6% and 60.1%; respectively.

The La Grange Fire Pension Fund has been significantly impacted by several disability pensions over the past decade.

No Management Letter comments have been issued regarding pension funds.

3. 2009 ACTUARIAL RESULTS

Preliminary Actuarial Valuation Results for April 30, 2009.

Investment Returns:	Police (-14.7%) Fire (-13.4%)
Percent Funded:	Police – decrease from 70.6% to 55.1% Fire – decrease from 56.5% to 43.9%
Required Annual: Contribution:	Police – increase from \$564,934 to \$823,760 Fire – increase from \$593,567 to \$773,525

According to Tim Sharpe, the average investment return for police & fire pension funds, with actuarial valuations dates in 2009 is approximately -13% to -14% and the average state funded status for police & fire pension funds is approximately 50%-55%.

These results will be discussed in greater detail with Tim Sharpe at the November 9th Village Board meeting.

Village of La Grange Police Pension - Investment Performance 2000-2009

	FYE 00	FYE 01	FYE 02	FYE 03	FYE 04	FYE 05	FYE 06	FYE 07	FYE 08	FYE 09
BOY Assets	13,315,497	13,678,073	13,358,409	13,077,249	12,614,155	13,493,828	13,777,644	14,973,591	15,821,318	15,482,325
Village Contribution	225,470	235,418	261,670	245,832	285,454	379,460	441,849	530,333	459,277	482,475
Police Officer Contribution	123,819	137,085	152,937	156,989	215,609	161,829	174,946	189,440	190,237	209,698
Pension Payments	691,494	797,022	811,110	853,490	980,068	1,105,733	1,049,934	1,056,553	1,078,825	1,153,258
Expenses	7,021	7,934	6,338	5,637	6,409	8,445	8,827	8,484	35,383	26,049
Income	711,802	112,790	121,681	(6,787)	1,365,087	806,705	1,637,914	1,192,991	125,702	(2,239,694)
EOY Assets	13,678,073	13,358,409	13,077,249	12,614,15	13,493,828	13,777,644	14,973,591	15,821,318	15,482,325	12,755,497
Annual Yield	**5.42%**	**0.84%**	**.92%**	**-0.05%**	**11.03%**	**6.10%**	**12.08%**	**8.06%**	**0.81%**	**-14.70%**
5-Year Yield (2005-09)	2.47%									
10-Year Yield (2000-09)	3.05%									

Village of La Grange Firefighters Pension - Investment Performance 2000-2009

	FYE 00	FYE 01	FYE 02	FYE 03	FYE 04	FYE 05	FYE 06	FYE 07	FYE 08	FYE 09
;OY Assets	7,763,226	8,033,232	7,882,868	7,568,755	7,219,822	7,860,187	8,052,187	8,776,760	9,219,172	8,994,331
'illage Contribution	187,186	214,810	222,351	277,583	313,303	379,276	420,926	482,634	476,960	536,622
irefighter Contribution	76,769	83,305	84,887	90,988	95,488	105,796	112,914	119,475	125,011	131,715
ension Payments	480,308	479,308	561,764	598,935	638,373	715,350	810,800	818,217	864,360	928,941
xpenses	4,934	13,700	6,238	4,786	5,471	5,625	16,430	16,397	29,635	20,145
ıcome	491,292	44,530	(53,349)	(113,782)	875,419	427,904	1,017,961	674,917	67,183	(1,194,738)
OY Assets	8,033,232	7,882,868	7,568,755	7,219,822	7,860,187	8,052,189	8,776,758	9,219,172	8,994,331	7,518,844
ınnual Yield	**6.42%**	**0.56%**	**-0.69%**	**-1.53%**	**12.33%**	**5.53%**	**12.88%**	**7.79%**	**0.74%**	**-13.49%**
-Year Yield (2005-09)	2.69%									
0-Year Yield (2000-09)	3.05%									

VILLAGE OF LA GRANGE, ILLINOIS

POLICE PENSION FUND
SCHEDULE OF EMPLOYER CONTRIBUTIONS

April 30, 2009

Fiscal Year	Employer Contributions	Annual Required Contribution (ARC)	Percentage Contributed *
2004	$ 285,454	$ 281,560	101.38%
2005	379,460	393,322	96.48%
2006	441,849	449,786	98.24%
2007	530,333	532,305	99.63%
2008	459,277	471,380	97.43%
2009	482,475	N/A	N/A

*Based on actual property tax collections.

VILLAGE OF LA GRANGE, ILLINOIS

FIREFIGHTERS' PENSION FUND
SCHEDULE OF EMPLOYER CONTRIBUTIONS

April 30, 2009

Fiscal Year	Employer Contributions	Annual Required Contribution (ARC)	Percentage Contributed *
2004	$ 313,303	$ 309,094	101.36%
2005	379,276	394,258	96.20%
2006	420,926	428,130	98.32%
2007	482,634	471,556	102.35%
2008	476,960	486,327	98.07%
2009	536,622	N/A	N/A

*Based on actual property tax collections.

VILLAGE OF LA GRANGE, ILLINOIS

POLICE PENSION FUND
SCHEDULE OF FUNDING PROGRESS

April 30, 2009

Actuarial Valuation Date April 30,	(1) Actuarial Value of Assets	(2) Actuarial Accrued Liability (AAL) Entry-Age	(3) Funded Ratio (1) / (2)	(4) Unfunded AAL (UAAL) (2) - (1)	(5) Covered Payroll	UAAL As a Percentage of Covered Payroll (4) / (5)
2003	$ 13,279,478	$ 17,448,207	76.11%	$ 4,168,729	$ 1,485,556	280.62%
2004	13,030,019	18,291,520	71.24%	5,261,501	1,559,834	337.31%
2005	12,881,409	19,177,261	67.17%	6,295,852	1,652,918	380.89%
2006	14,973,591	20,051,960	74.67%	5,078,369	1,735,564	292.61%
2007	15,821,318	20,937,302	75.57%	5,115,984	1,920,639	266.37%
2008	15,482,325	21,921,736	70.63%	6,439,411	2,016,671	319.31%

VILLAGE OF LA GRANGE, ILLINOIS

FIREFIGHTERS' PENSION FUND
SCHEDULE OF FUNDING PROGRESS

April 30, 2009

Actuarial Valuation Date April 30,	(1) Actuarial Value of Assets	(2) Actuarial Accrued Liability (AAL) Entry-Age	(3) Funded Ratio (1) / (2)	(4) Unfunded AAL (UAAL) (OAAL) (2) - (1)	(5) Covered Payroll	UAAL As a Percentage of Covered Payroll (4) / (5)
2003	$ 7,612,396	$ 11,896,147	63.99%	$ 4,283,751	$ 1,059,927	404.16%
2004	7,602,966	12,469,779	60.97%	4,866,813	1,112,923	437.30%
2005	7,560,450	13,334,072	56.70%	5,773,622	1,092,198	528.62%
2006	8,776,758	14,062,301	62.41%	5,285,543	1,185,318	445.92%
2007	9,219,172	15,335,206	60.12%	6,116,034	1,240,865	492.88%
2008	8,994,331	15,919,958	56.50%	6,925,627	1,302,908	531.55%