STATE OF ILLINOIS
OFFICE OF THE
AUDITOR GENERAL
William G. Holland, Auditor General

SUMMARY REPORT DIGEST

REVIEW OF INFORMATION SUBMITTED BY THE RETIREMENT PLAN FOR CHICAGO TRANSIT AUTHORITY EMPLOYEES

2012 ANNUAL REVIEW
Release Date: November 2012

SYNOPSIS

The Illinois State Auditing Act requires the Retirement Plan for Chicago Transit Authority Employees (Retirement Plan) to submit its most recent audit, annual statement, and actuarial statement to the Office of the Auditor General (OAG) by September 30 of each year. These documents were submitted by the Retirement Plan on September 28, 2012. The OAG reviewed these documents and concluded that the Retirement Plan had complied with the requirements established in the Auditing Act.

The Illinois Pension Code (40 ILCS 5/22-101(e)(3)) requires the Retirement Plan determine, based on a report prepared by an enrolled actuary, the estimated funded ratio of the total assets of the Retirement Plan to its total actuarially determined liabilities. The Retirement Plan is also required to determine the contribution rates needed to meet the funding requirements established by the Pension Code. The Auditor General is then required to review the Retirement Plan's determination and assumptions to determine whether they are "*unreasonable in the aggregate*". This report does not constitute an audit as that term is defined in generally accepted government auditing standards.

- The OAG reviewed the Retirement Plan's assumptions in the January 1, 2012 Actuarial Valuation and concluded they were not unreasonable in the aggregate.
  - As in our prior Annual Reviews, we continue to conclude that the investment return assumption used by the Plan is an optimistic assumption. According to the Plan, its actuary conducted an analysis and concluded that the 8.50 percent investment rate of return falls within the 25th to 75th percentile of expected returns and is thus compliant with Actuarial Standard of Practice No. 27. However, the 8.50 percent return is at the upper range of investment returns for comparable plans. The Plan indicated that the investment return assumption will be reviewed in its next experience study, scheduled for 2013.
- In September 2012, the Retirement Plan increased the employer and employee contribution rates for 2013 as delineated in the January 1, 2012 Actuarial Valuation: the employer rate increased from 11.3 to 14.250 percent (which is net of the employer debt service credit of 6% of pay); the employee rate increased from 8.65 to 10.125 percent. The January 1, 2012 Actuarial Valuation noted that contribution increases were necessary to have the Plan's funded ratio at the statutorily required 60 percent level within 10 years of 2012 (i.e., by 2022) and all subsequent years through 2039.
- The funded ratio of the Retirement Plan declined from 70.1 percent as of January 1, 2011 to 59.2 percent as of January 1, 2012. The actuarial value of assets was $1.662 billion at January 1, 2012 and the actuarial accrued liability was $2.808 billion.

ANNUAL REVIEW
RESULTS AND CONCLUSIONS

STATUTORY REQUIREMENTS

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

OAG reviewed the documents submitted by the Retirement Plan and concluded the Retirement Plan had complied with the Auditing Act.

- On September 28, 2012, the Retirement Plan submitted these documents to the Auditor General.
- The OAG reviewed these documents and concluded that the Retirement Plan had complied with the requirements established in the Auditing Act.

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

- The Retirement Plan is also required to determine the contribution rates needed to meet the funding requirements established by the Pension Code.
- The Auditor General is then required to review the determination and the assumptions to determine whether they are "*unreasonable in the aggregate*". (pages 3-5)

REVIEW OF ACTUARIAL VALUATION

The Retirement Plan submitted the Actuarial Valuation as of January 1, 2012 to the OAG on September 28, 2012. This Actuarial Valuation was accepted by the Retirement Plan's Board of Trustees (Board) at its September 25, 2012 meeting.

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

The OAG and our consultants, Aon Hewitt, reviewed the Retirement Plan's assumptions contained in the January 1, 2012 Actuarial Valuation and concluded that they were not unreasonable in the aggregate. Our report does not constitute an audit as that term is defined in generally accepted government auditing standards.

As in our prior Annual Reviews, we continue to conclude that the investment return assumption used by the Plan is an optimistic assumption. According to the Plan, its actuary conducted an analysis and concluded that the 8.50 percent investment rate of return falls within the 25th to 75th percentile of expected returns and is thus compliant with Actuarial Standard of Practice No. 27. Also, since 1990, the Plan has averaged an 8.99 percent rate of return on its investments, according to the Plan's Investment Report for the period ending December 31, 2011. However, the 8.50 percent return is at the upper range of investment returns for comparable plans. The Plan indicated that the investment return assumption will be reviewed in its next experience study, scheduled for 2013. (pages 5-8)

January 1, 2012:
- **Assets . . . . $1.662 billion**
- **Liabilities . . . .$2.808 billion**
- **Funded Ratio 59.2%**

The funded ratio of the Retirement Plan declined from 70.1 percent as of January 1, 2011 to 59.2 percent as of January 1, 2012. The actuarial value of assets was $1.910 billion at January 1, 2011. At January 1, 2012, the actuarial value of assets was $1.662 billion and the actuarial accrued liability was $2.808 billion. According to the Retirement Plan's January 1, 2012 Actuarial Valuation, there were two major reasons for the decline in the actuarial value of assets and the funded ratio.

- First, the Plan revised its asset valuation method from a five year smoothed method to the actual market value of the assets as of January 1, 2012. According to the January 1, 2012 Actuarial Valuation, this resulted in a $183.3 million reduction in the actuarial value of assets and decreased the Plan's funded ratio by 6.5 percent.

- Second, the Plan's experience differed from the assumptions that were used in the prior Valuation. The largest contributing factor was that the assumed 8.50 percent rate of return was not met -- the actual rate of return on the actuarial value of assets before the asset valuation method change for the year ending December 31, 2011 was 2.87 percent, resulting in an asset loss of $104.3 million. This loss increased the unfunded actuarial accrued liability by $104.3 million and decreased the funded ratio by 3.7 percent. Also, demographic experience (such as mortality, turnover, retirement, pay increases, etc.) that differed from actuarial projections increased the Plan's unfunded accrued actuarial liability by $34.5 million. (pages 11-12)

CONTRIBUTION RATES

The Pension Code requires the 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 declines, or is projected to decline, below 60 percent prior to 2040, with the CTA paying two-thirds and employees one-third of the required contribution.

For 2013, the Board increased employee contribution rates from 8.65% to 10.125% of pay and employer contribution rates from 11.3% to 14.250% of pay (the employer contribution rate is net of debt service credit of 6% of pay).

- In September 2012, the Retirement Plan increased the employer and employee contribution rates for 2013 as delineated in the January 1, 2012 Actuarial Valuation: the employer rate increased from 11.3 to 14.250 percent (which is net of the employer debt service credit of 6% of pay); the employee rate increased from 8.65 to 10.125 percent.

- The January 1, 2012 Actuarial Valuation noted that contribution increases were necessary to have the Plan's funded ratio at the statutorily required 60 percent level within 10 years of 2012 (i.e., by 2022) and all subsequent years through 2039. (page 11)

WILLIAM G. HOLLAND
Auditor General

WGH:JS

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