PENSION ADVISOR

POLICEMEN'S ANNUITY & BENEFIT FUND OF CHICAGO March 2011, No. 43

The sun was warm but the wind was chill.
You know how it is with an April day.

~Robert Frost

A NEW WEBSITE
Annuity Calculator

The Fund has a new and improved web page. An annuity calculator is available for you to obtain an estimate of future benefits you would be eligible to receive.We believe it is user-friendly with the ability to quickly obtain the information you are seeking. We appreciate any feed-back from our membership. You may visit us @ www.chipabf.org

ANNUAL STATEMENTS

If you do not have time to visit our website, the Annual Participant Statements will be mailed to all **active members** by mid-May 2011. The address used for distribution is the address the City had on file for you for the 02/28/2011 payroll.

Please review the information for any errors. Any married police officer who wants to have her name changed needs to visit our office and produce a certified copy of the marriage certificate and the name will be changed accordingly.

EQUIPMENT & SUPPLY

Retiring members please make note, The Equipment & Supply Division (Unit 172) has moved! No longer at 14th Street...
New Location is

1869 West Pershing, 4th Floor
312-745-1290 745-1219

RETIREMENT APPOINTMENTS

The Pension Fund schedules appointments for members to complete the application process for retirement.
After you have completed a retirement PAR, make a copy of the electronic form and your exit interview and call the Pension Fund Office at 744-3891 or PAX 0357 to schedule your appointment. Appointments will be Monday through Fridays from 9:00 am to 3:30 pm.

ADDRESS CHANGES

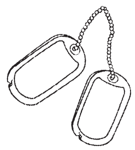
Don't miss out on important news or updates. This Pension Fund relies on the City to provide us with all **active members'** addresses. Therefore, we ask that you keep the Personnel Division of the CPD updated of your address to ensure receipt of all mailed information. Address Changes requires a Personnel Change Notice No. 11.611 and a City of Chicago residency affidavit must be completed and submitted to Personnel Division along with proof of residency.

PURCHASING MILITARY SERVICE

Attention Veterans and Reservists:

Under Senate Bill 3022, active members may purchase up to two years of service for credit for ***prior*** military service with the United States Armed Forces. In order to start the process, please submit a copy of your DD-214, along with your completed application which can be downloaded from our website.

- ✦ The DD-214 must display periods of service that are ***before*** your hire date with the Chicago Police Department.
- ✦ Reservists/National Guard: In addition to any DD-214's that you submit, you will also have to submit a copy of your Chronological Statement of Retirement Points.
    - ❍ You will receive one day service credit for every active duty point that you earned, prior to your date of hire with the Chicago Police Department. This information can be located under line 8 of the statement.



Military Leaves of Absence

If you are required to take a leave of absence from the Chicago Police Department for military reasons, you may also be eligible to purchase service credit. In order to keep your record of service up to date, please forward the following information to our office:

- ✦ All PAR forms submitted regarding your initial military leave of absence, any subsequent extensions of leave,and your reinstatement to active duty with the Chicago Police Department.
- ✦ Any other personnel orders or for documenting your military leave of absence and subsequent return to duty.

How much do I owe?

The amount due for **prior military service** under SB3022 is calculated on an actuarial basis, taking into consideration what your prior salaries with the Chicago Police Department would have been at that time, along with 8% compound interest and other actuarial factors.

The amounts owed for **military leaves of absence** are calculated differently, and are based on a comparison of salary deductions made during the period versus salary deductions that would have occurred had no military leave of absence taken place. **No interest** is charged on balances due for a military leave of absence.

Your indebtedness must be paid in full before your date of retirement. You may make installment payments in amounts of at least $100.00. If you are a participant of Deferred Compensation, you may also elect to directly transfer funds from your Nationwide Retirement Solutions account without a tax penalty to you.

TRUSTEES' CORNER

By Sgt. Michael Lazzaro, Trustee

THE FUNDS' INVESTMENT POLICY

The Fund's overall investment policy is based on the following principles:

1. Maintain a long term investment horizon for the Fund.
2. Emphasize equity investments to enhance long-term growth.
3. **Diversify** investments across several asset classes.
   Asset classes:
   U.S Equity
   International Equity
   Fixed Income
   Private Equity
   Infrastructure
   Fund of Hedge
   Funds Private Real Estate
   Public Real Estate

The Funds' investment committee (IC) has formalized investment policy, a 96 page document available on The Funds' website (chipabf.org). The policy's objective is to enforce logical, disciplined investment decisions, and limiting the temptation to make counter-productive changes during times of market turmoil.

The Funds' IC meets every month and consists of all 8 Trustees. The committee reviews the assets allocation of the plan on a quarterly basis, relative to the allocation target and ranges delineated in this policy. The IC invests in multiple asset classes and uses outside investment managers with well diversified portfolios. This is done with the goal of insulating the portfolio from the effects of substantial losses in any single security, or sector of the market.

As a Trustee, I am very aware of my fiduciary responsibility. A fiduciary "manages the financial affairs of others, with substantial knowledge of their needs and objectives, putting those needs and objectives ahead of their own, and taking full responsibility for decisions made."

Also guiding my investment decisions is an informal 21 word summary of the fiduciary from George Cowles of Bankers Trust:

"Be fruitful and multiply
Be prudent and diversify
When I doubt, ask an expert
And remember, it is not your money."

By P.O. Michael Shields

2010 Performance

Based on figures obtained prior to the auditor's report, the Pension Fund's value is currently \$3.154B. The Fund had a 12.72% total return for 2010. Our equity returns were 15.60%. Equity is our largest allocation comprising 60% of the total portfolio. Our fund's equity portfolio beat the industry benchmark by a substantial 2.93% because of an overweight to Non-U.S. Equity. Fixed income returned 7.82%, beating its benchmark by 1.28% because of our underweight to U.S. Treasuries. The fund lagged in its alternative space at .19%. Alternative investments, while harder to benchmark, set us back somewhat. We should note, however, that our program's value is not "mature" and it will take several years to fully deploy our capital and thus be able to fully capture the returns we our seeking. Accounting requirements force the fund to include the current values of alternatives, forcing the total returns of the fund to be lower.

Retirement Number Review

336 officers of all ranks retired in 2007, followed by 340 and 262 in 2008 and 2009, respectively. That number jumped to 553 in 2010. The numbers anticipated for 2011 may also soar over 500 as well. As the amount of active officers shrink, the dollars contributed to the fund by both the active members and the City of Chicago are diminished. A greater reliance on the assets will be sought from the board, unless a cash injection occurs. \$270M of investment money was used to make disbursements in 2010. That totals 8.6% of the fund's total assets. 2011's demand will be greater on the fund.

Active Members' Paycheck

On January 13, 2011, the State withholding income tax rate went from 3% to 5%. This means that for every \$1,000 earned, approximately \$50 will be withheld and sent to the State of Illinois for income taxes. Previously, the amount would have been \$30. These numbers are approximate, as actual withholdings will vary based upon the exemptions claimed by the wage earner. This decreases the "take-home" dollar amount in the active members' paycheck.

Secondly, the American Recovery and Reinvestment Act of 2009 contained the "Making Work Pay" tax credit. This credit temporarily increased "take-home" pay in 2009 and 2010 by reducing the Federal Income Tax withholding rates. The "Making Work Pay" tax credit was designed to act as a special stimulus to help the economy out of a recession by putting extra money in wage earners' hands. This expired December 31, 2010 and the Federal withholding tax tables reverted to previous levels. (IRS notice 1036 contains more information on this along with current tax tables.) The impact of the removal of this credit varies by wage earner, based upon taxable earnings and exemptions claimed. However, in most cases, the credit expired and federal withholding levels are back to 2008 tables.

Retirees' Paycheck

The "Making Work Pay" credit was enacted only for 2009 and 2010. While the "Making Work Pay" credit only applied to wage earners (and not pensions), the taxable withholding tables used for pension payments were the same as those for current wage earners. The "Making Work Pay" credit was approximately 6.2% of income, up to $400 for a single filer and $800 for a married filer. While pension wages were not eligible for this credit (since the withholding tables used reflected that same credit), the average pension payment would be reduced by about $400 annually for a single filer or $800 annually for a married filer.

By Annuitant Trustee, Ken Hauser

Defined Benefit vs Deferred Contribution Plans

Since the mid-1990s, legislation has been proposed to replace defined benefit (DB) pension plans with defined contribution (DC) plans. The issue is whether DB plans should be eliminated and replaced with DC plans. While recognizing that DC plans are useful in providing supplemental retirement benefits, this article argues against replacing DB plans with DC plans. Eliminating the DB plan and switching to a DC plan is likely to be a lose-lose situation for governments, their employees and taxpayers.

How DB Plans Work

In a typical DB plan, employers promise to pay retirement benefits based on an employee's period of service and final average salary. A typical benefit formula is: 2% for every year of service and the highest four years salary average out of the last ten years of service with a 75% maximum of that average. Most public employees in a DB plan also receive a cost-of-living adjustment (COLA) as a protection against inflation, a surviving spousal lifetime annuity and disability and preretirement death benefits. DB plan benefits are financed by contributions from the employer and the employees and investment income. Annuity benefits are paid from accumulated contributions and investment earnings. A key advantage of DB plans is that investment earnings supplement employer contributions. A disadvantage of DB plans is that when investment earnings are lower than expected, additional employer contributions are required, as evidenced by the recent market downturns. For annuitants, a key advantage of DB plans is that they are provided income based on preretirement earnings.

How DC Plans Work

In a DC plan, employers provide employees with individual investment accounts and promise to contribute a certain amount to the accounts annually. For governmental DC plans, the employer's contributions range approximately from 3.5 to 8 percent per year. Usually, employees also contribute to their accounts and decide how the assets are invested, choosing from a number of funds representing major investment categories. Investment management fees are paid from the employee's account, reducing the funds available to pay benefits. At retirement, the employee's benefit is paid solely from the contributions and investment earnings that have accumulated in the individual's account.
For employers, one advantage of DC plans is that the employer's contribution rate is fixed and unaffected by downturns in investment markets. Moreover, the employer has no financial liability for the employees after they retire, even if DC accounts are insufficient to provide an adequate retirement benefit.
A major disadvantage is that DC accounts are subject to investment risk and may not be sufficient to sustain employees throughout their retirement. Another disadvantage is that a high percentage of employees cash out and spend some or all of their DC accounts, significantly reducing the amounts available to pay retirement benefits.

Background

State and local government retirement plans in the United States cover 14.7 million active public employees (about 12 percent of the U.S. workforce) and 7.6 million retirees, including teachers, police officers, firefighters, legislators, judges and general employees. In addition, there are 4.4 million former employees who will be eligible to receive benefits upon reaching retirement age. Ninety-one percent of full-time government employees have access to

DB retirement plans. Approximately twenty-five percent are not covered by Social Security, including many teachers, police officers and firefighters. At the end of 2009, state and local plans had accumulated $2.7 trillion in assets, up from $2.3 trillion at the end of 2008 but down from $3.4 trillion in 2007. However, even in 2008, state and local pension assets were, on average, 13 times the amount needed to pay annual benefits. In 2009, assets had increased to more than 14 times the amount needed to pay annual benefits.

Proponents of switching to a DC plan argue that it would lower the government's cost of providing retirement benefits, thereby reducing state and local taxes. Some proponents also argue that DC plans would benefit public employees by giving them higher benefits through DC plan investment earnings and by making it easier for employees to transfer their benefits when they change jobs. As this article will show, it is likely that switching to a DC plan would increase retirement costs for governments over the short term and possibly over the long term as well. In addition, studies indicate that retirement benefits provided through DC plans are, on average, significantly lower than benefits provided through DB plans. Moreover, although DC plans are useful for providing supplemental, tax-deferred retirement savings, replacing DB plans with DC plans could cause severe, unintended consequences such as: (a) governments could lose a valuable tool for attracting and retaining qualified employees, (b) public employees could lose a significant amount of retirement income, potentially affecting state and local economies, (c) legislators could face additional pressure to increase DC retirement benefits and provide additional financial assistance for public-sector retires.

In the June Pension Advisor I will discuss the advantages of a Defined Benefit Pension Plan.

The information for this article has been obtained from a research series from the National Conference on Public Employee Retirement Systems (NCPERS).

Pension Advisor is a publication of the Policemen's Annuity and Benefit Fund. You will be receiving a copy to update you on the matters that affect your pension and the concerns of active police officers, retirees and widows that make up our membership. If you have a question about your pension or the Fund, or, if there is a particular issue you would like to see addressed, please feel free to send a note to:

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Sonny Panaligan
Assistant Comptroller

Samuel Kunz
Chief Investment Officer

Visit our website at: **chipabf.org**

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