THE THREE TIERS OF TRS

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As I write this article, the Illinois House and Senate are discussing a bill that will change the face of TRS as we know it. Having already made changes to the system which affects new hires, there is now a debate about changing the contribution and payout structure for every member. While there are many discussions that will be had on these developments, an important one is how to analyze your situation, how the changes will affect you and decide what election is right for you and your family.

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In review, the proposal is to split the TRS contribution and payout structure into three tiers. Tier 1 will leave the current structure the same, but initially increase current contributions from 9.4% to 13.77%, and reserving the right of TRS to increase contributions to a much higher level. Tier 2 would reduce this contribution amount from 9.4% to 6%; members would receive a reduced benefit and COLA amount and would not be eligible to receive this benefit until age 67. Tier 3 would freeze the current pension contribution and require members to contribute 6% of their salary into a "401(k)-type" plan with the state matching this contribution. How do you decide which election is right for you and what should you take into account when making this decision?

One of the elements that go into this decision is how long you have been an educator (and/or administrator) and when you aim to retire. For example, an educator aged 58 who will be retiring in 4 years; and is relying on TRS to provide their entire retirement living expenses may be able to handle an increase in contribution amounts for the short period of time before retirement. This increase in contributions could provide the full benefits that they were expecting to receive. This annual benefit would be greater than the amount received in the Tier 2 structure and is available for collection prior to age 67, the minimum age proposed for Tier 2. However, if this educator is currently living paycheck-to-paycheck, an increase in contributions may cause their budget to become unbalanced, therefore staying in Tier 1 may not be an option.

In another example, a 30 year-old educator may have another 30 years until retirement and has plenty of time to weather stock market fluctuations, so may see a greater benefit to Tier 3. A 6% contribution, fully matched by the state, will allow for a 12% annual contribution into a defined contribution account. Should an educator save for 30 years into this account at 12% of their salary, they may have a significant balance as they enter retirement. For those with a spouse contributing to a defined contribution plan (e.g. 401(k)), the educator may benefit from the income-diversification that a defined-benefit plan will provide.

Factors such as whether the monthly cash flow allows for increased contributions would determine whether Tier 1 or 2 is selected.

It's almost inevitable that some decisions will have to be made when it comes to retirement savings and benefits in the evolving TRS system. However, it should be noted that in having a choice whether to contribute to a defined benefit or contribution plan, educators are in an advantageous position over other workers who may not get that option. Given the irrevocable nature of entering a particular Tier, and the household-specific discussion that must take place when making these decisions, it would make sense to involve a Fee-Only financial planner who understands your family's finances. Vantage Financial Partners Limited would be honored to support and assist in this decision making process for you and your family. If you wish to explore how we can help, please contact Dave Grant (dgrant@vantagefinancial.com or 847-590-5555 ext 104).

Materials used in the preparation of this article were gathered from the following websites and their associated publications:

www.trs.illinois.gov

www.ieanea.org

ABOUT THE AUTHOR

Dave is a financial planning analyst at Vantage Financial Partners Limited. As an analyst, Dave is responsible for many crucial facets in the development of the client's financial plan including mentoring the planning associates, reviewing client data and providing planning and investment recommendations to the relationship managers.

Dave's family includes several teachers in various stages of their careers. His wife, Sarah, is early in her teaching career so many of the changes taking place will affect their family directly. Dave seeks to serve teachers and administrators who feel they need to focus on 'controlling the controllable' and take an active approach to preparing for retirement. To contact Dave, either email him at dgrant@vantagefinancial.com or call 847-590-5555, ext. 104.