

Questions.....	54
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## Chapter Six: Service Credit

Days that count toward earning service credit.....	1
Maximum creditable service in one year .....	1
Adding service credit to a member’s record .....	1
Sick leave.....	2
Sick leave days for service credit.....	4
Personal leave days.....	4
Days withdrawn from a sick leave bank.....	4
Sick leave days not reportable for service credit.....	5
Unused vacation days .....	5
Sabbatical leave .....	5
Leave of absence.....	6
Duplicate service .....	6
Labor contract litigation.....	6
Occupational disability service credit .....	6

## Chapter Seven: Optional Service Credit and Payment Options

Optional service credit.....	1
Out-of-system service.....	1
Part-time teaching .....	2
Substitute teaching, homebound instruction, and tutoring .....	2
Military service and post-military teacher retraining .....	3
Leave of absence and involuntary layoff .....	4
Leave of absence, layoff, and absence due to pregnancy or adoption .....	5
Private School Credit.....	6
Repayment of a refund .....	6
Correcting errors after more than four fiscal years.....	6
Required contribution and interest rates for the purchase of optional service credit.....	7
The 2.2 formula .....	8
2.2 upgrade .....	8
Purchasing credit for optional service .....	8
Employer’s payment of member’s 2.2 upgrade balance or optional contribution balance .....	8
After-tax payments .....	9
Before-tax payments.....	10

## Chapter Eight: Payroll Deduction Program

Discontinuation of Program .....	1
Overview.....	1
Program criteria .....	1
Remitting deductions to TRS .....	2
Verifying payment information.....	2
Suspending PDP agreements.....	2
Terminating PDP agreements .....	3
PDP completion .....	3

## Chapter Nine: Member Refunds

Refund of retirement contributions .....	1
Repayment of refunds .....	2
Refunds of 1 percent retirement contributions .....	2
Refund of survivor benefit contributions .....	3
Refund or reduction of the 2.2 upgrade cost ...	4
Refund of excess purchases and repayments ...	4
Refunds of the 0.4 percent member retirement contributions .....	5
Refunds eligible for rollovers .....	5
Taxability of refunds.....	5

## Chapter Ten: Post-Retirement Matters

Collecting contributions from employees who are TRS annuitants.....	1
Eligibility for a TRS retirement annuity.....	1
Employment limitations for TRS annuitants ...	1
Health insurance available after retirement .....	5

## Chapter Eleven: Retirement Benefits

Single-sum retirement benefit .....	1
Retirement annuity.....	1
How to estimate an upgrade contribution.....	3
How to estimate average salary.....	3
How to estimate a retirement annuity .....	4
Exact age .....	4
Discounted annuity .....	5
Early Retirement Option .....	6
ERO costs.....	6
Employer limits on utilization .....	7
Establishing eligibility for ERO.....	7
Member ERO contribution .....	7
Employer's ERO contribution .....	8
Reversionary annuity .....	8
Application procedures.....	9
Retirement application for annuitants who re-enter TRS membership .....	9
Effective date of retirement.....	10
Annuity payments.....	10
Direct deposit.....	10
Mailing address .....	10
Automatic annual increases in annuity.....	10
Reciprocal service.....	12
Taxability of retirement benefits .....	13
Fraction of a year table .....	15

## Chapter Twelve: Disability Benefits

Types of disability benefits available.....	1
Service credit .....	1
Employment .....	1
Medical examinations .....	1
Nonoccupational disability benefits.....	2
Occupational disability benefits.....	4
Disability retirement annuity.....	6
Taxability of disability benefits.....	9
Law allows limited, part-time teaching .....	10

## Chapter Thirteen: Death Benefits

Benefits payable .....	1
Designation of beneficiaries .....	1
Types of beneficiaries .....	1
Beneficiary refund.....	3
Survivor benefits .....	3
Payment of accumulated contributions.....	7
Payment of survivor benefits.....	9
Federal tax withholding .....	11
Tax reporting for all TRS payments .....	12
State income tax .....	12
How to obtain additional information .....	12

# Chapter Seven: Optional Service Credit and Payment Options

## Optional service credit

Credit for several types of optional service can be obtained by verifying the service and making a contribution to TRS. In general, the amount due for the service credit is equal to the contributions that would have been required if the service had been earned under TRS plus interest.

A member may reinstate service that has been cancelled by a refund and purchase service credit for the following certificated teaching:

- out-of-system service,
- part-time teaching,
- substitute and homebound teaching,
- military service and post-military teacher retraining,
- leave of absence and involuntary layoff,
- an absence due to pregnancy or adoption prior to July 1, 1983, and
- recognized Illinois private school service. (Members must apply on or before August 1, 2012.)

With the exception of absences due to pregnancy or adoption prior to July 1, 1983, a member must pay for optional service credit before retirement. Only the paid portion of optional service credit is used to calculate retirement benefits. Refunds, however, must be repaid in full before the service credit can be used.

A member should have any optional service recorded with TRS as soon as possible. If the member waits until retirement to confirm the service, the employer's records may have been lost or destroyed. Without a record of the service, TRS cannot grant the member credit.

## Out-of-system service

A member may purchase out-of-system service for full-time, part-time, or substitute public school teaching performed in:

- other states, territories, or dependencies of the United States,
- Chicago public schools, or
- public common schools operated by or under the auspices of the United States or any agency or department of any other state. However, service as an instructor in a United States military instructional center while the member was in the military is *not* eligible for optional service credit.

A member may also purchase out-of-system service for any period of work in professional speech correction or special education in a public agency within Illinois or any other state, territory, dependency, or possession of the United States.

Out-of-system service for teaching in colleges, universities, and private schools cannot be purchased.

The out-of-system service that is purchased cannot exceed two-fifths of the member's total creditable service with TRS at retirement. The maximum credit for out-of-system service is 10 years. The out-of-system service must be followed by at least five years of creditable service earned with TRS, the Public School Teachers' Pension and Retirement Fund of Chicago (CTRF), or the State Universities Retirement System (SURS).

To verify optional service credit for out-of-system teaching, TRS requires the member's former employer to file an Out-of-System Service Certification form based upon existing school records. Once the credit is verified, the service will be added to the member's record at TRS as "pending service credit" and an accounts receivable balance will be established for the amount due.

For the applicable contribution and interest rates in effect at the time the service was rendered, see "Required contribution and interest rates for the purchase of optional service credit." For persons who were not members on June 30, 1963, the minimum required contribution is \$420 per year of service plus 4 percent interest per year compounded annually from July 1 of the first year of membership until June 30, 1977, after which interest is computed as detailed in "Required contribution and interest rates for the purchase of optional service credit."

## **Part-time teaching**

All part-time teaching performed after June 30, 1990 is reported to TRS and contributions are remitted by the employer. From July 1, 1969, to June 30, 1990, only part-time teaching on a permanent and continuous basis in a position for which services were expected to be rendered for the entire school term was reportable. Part-time teaching was not reportable prior to July 1, 1969.

For a member to purchase service credit for part-time service prior to July 1990 that was not reportable by an employer, employers must – based on existing school records – verify the applicable days on the Part-Time Service Certification form, which is shown at the end of this chapter, and file the completed form with TRS. Once the credit is verified, the service will be added to the member's record at TRS as "pending service credit" and an accounts receivable balance will be established for the amount due. Contributions are based on the member's creditable earnings.

## **Substitute teaching, homebound instruction, and tutoring**

All substitute teaching performed after June 30, 1990 is reported to TRS and contributions are remitted by the employer. A member who performed substitute teaching prior to July 1990 for TRS-covered employers may purchase credit for the fraction of a year that is equal to the ratio of days paid to the number of days in the legal school term at the time the service was performed.

Service credit may also be obtained for homebound instruction and tutoring paid by the employer.

For a member to purchase credit for this service, the employer must – based on existing school records – verify the applicable days on the Substitute or Homebound Service Certification form, which is shown at the end of this chapter, and file the completed form with TRS. Once the credit is verified, the service will be added to the member's record at TRS as "pending service credit" and an accounts receivable balance will be established for the amount due. Contributions are based on the member's creditable earnings.

is shown at the end of this chapter, and file the completed form with TRS. The employer or the member may be asked to file a copy of the board resolution granting the leave.

A member may verify credit for an involuntary layoff by sending TRS a copy of the layoff notice he or she received from the employer engaging in the reduction in force.

Once the credit is verified, the service will be added to the member's record at TRS as "pending service credit" and an accounts receivable balance will be established for the amount due. Contributions to TRS for this service credit are based on a salary rate equal to the member's teaching salary rate immediately preceding the leave.

Beginning with the 2000-01 school year, TRS included the Employer's Leave of Absence Report with the Employer's Annual Report of Earnings form. Complete an Employer's Leave of Absence Report for all TRS-covered members on an unpaid leave of absence during any portion of the school year. For more information regarding the Employer's Leave of Absence Report included with the Employer's Annual Report of Earnings form, please refer to Chapter 5, Reporting, "Leave of Absence."

## **Leave of absence, layoff, and absence due to pregnancy or adoption**

A member may purchase credit for periods away from a TRS-covered position prior to July 1, 1983, due to pregnancy or adoption.

To be eligible to purchase this credit, the member must

- have returned to covered employment with either TRS or the State Universities Retirement System (SURS) and
- send TRS a completed Adoption Service Certification form or Pregnancy Service Certification form and all required supporting documentation.

Once the credit is verified, the service will be added to the member's record at TRS as "pending service credit" and an accounts receivable balance will be established for the amount due. Contributions to TRS for this service credit are based on a salary rate equal to the member's teaching salary rate immediately preceding the leave.

If the member has not yet retired, he or she must complete the pregnancy or adoption credit purchase prior to retirement if the credit is to be included in the benefit calculation. Payment made after the member retires will result in the recalculation of the retirement benefit, effective the first of the month following payment.

Annuitants are permitted one opportunity to purchase the credit. Although it is advantageous for an annuitant to purchase the credit as soon as possible, there is no deadline. Both annuitants and members may purchase all or a portion of the credit to which they are entitled, but annuitants may make only one purchase.

Three years is the maximum combined service credit that may be purchased for absences due to pregnancy or adoption, leaves of absence, and involuntary layoffs.

## Private School Credit

The Illinois Pension Code allows a limited opportunity to purchase credit for service as a teacher or administrator in a recognized Illinois private school. Post-secondary institutions are not included. Retired members may not purchase this service. The member must apply for this credit on or before August 1, 2012.

To qualify, the member must have:

- been employed in a private school recognized by the Illinois State Board of Education,
- been certified as a teacher or administrator during the period of private school service,
- completed at least 10 years of contributing TRS service, and
- established at least one full-time salary following the private school service.

A maximum of two years of private school credit may be purchased. If the member previously purchased two years of private school credit, he or she may not purchase additional private school credit.

To verify private school credit, TRS requires the member's former employer to file a Recognized Illinois Non-public Service Certification form.

For each year of service credit purchased, the member must contribute the normal cost in effect on the date of the application. This rate, which is determined by our actuaries each year, includes both employer and employee contribution costs. The rate is multiplied by the salary for the member's first year of full-time employment in a TRS-covered position following the private school service. Interest, currently at the rate of 8.5 percent, begins on the first date of full-time TRS employment following the private school service and continues until the contribution is paid.

## Repayment of a refund

When a member withdraws service by taking a refund of contributions, TRS membership ends and all creditable service is cancelled. Service credit that was previously forfeited by taking a refund may not be used as a basis for payment of benefits until the member:

- repays the *entire* refund with interest from the date the refund was made to the date the refund is repaid and
- completes one year of TRS creditable service following the refunded service. Repayment of the refund is permitted under the provisions of the Illinois Retirement Systems Reciprocal Act after the member completes at least two years of service with a reciprocal system following the date of the refunded service credit.

These requirements must be completed prior to the member's retirement, death, or commencement of disability benefits.

## Correcting errors after more than four fiscal years

Section 16-192 of the Illinois Pension Code requires TRS to correct its members' creditable earnings for four fiscal years prior to the date in which the error was noted. For example, if an error discovered in the 2008-09 school year occurred during the 2004-05, 2005-06, 2006-07,

or 2007-08 school years, the employer must contact the TRS Employer Services Department for an Employer's Report of Adjustments to Earnings form. For more information on the Employer's Report of Adjustment to Earnings form, please see Chapter 5, Reporting.

For an error discovered more than four fiscal years after its occurrence, the member may contact TRS for an Unreported TRS Service Certification form. An example of the form is shown at the end of this chapter.

For a member to purchase credit for unreported service, the employer must, based on existing records, verify the days paid and the earnings information on the Unreported TRS Service Certification form, which is shown at the end of this chapter, and file the completed form with TRS. Once the credit is verified, the service will be added to the member's record at TRS as "pending service credit" and an accounts receivable balance will be established for the amount due. Contributions are based on the member's creditable earnings.

## **Required contribution and interest rates for the purchase of optional service credit**

*(40 ILCS 5/16-128)*

Required contributions are equal to the contributions that would have been required if the service had been rendered under TRS, plus interest. Interest is compounded annually from the date the contributions would have been due to the date of payment according to the following schedule unless otherwise noted in the explanation.

Required TRS contributions as a percentage of earnings are:

- 4 percent, July 1, 1939 to June 30, 1947;
- 5 percent, July 1, 1947 to June 30, 1953;
- 6 percent, July 1, 1953 to June 30, 1959;
- 7 percent, July 1, 1959 to June 30, 1969;
- 7.5 percent, July 1, 1969 to June 30, 1971;
- 8 percent, July 1, 1971 to June 30, 1995;
- 8 percent plus 0.5 percent health insurance contributions, July 1, 1995 to June 30, 1998;
- 9 percent plus 0.5 percent health insurance contributions, July 1, 1998 to December 31, 2001;
- 9 percent plus 0.65 percent health insurance contributions, January 1, 2002 to June 30, 2003;
- 9 percent plus 0.75 percent health insurance contributions, July 1, 2003 to June 30, 2005; and
- 9.4 percent plus 0.80 percent health insurance contributions July 1, 2005 to June 30, 2007; and
- 9.4 percent plus 0.84 percent health insurance contributions after July 1, 2007.

Contributions were subject to a maximum amount until 1961. Minimum contributions were in force continuously.

Interest, compounded annually, is computed as follows:

- 3 percent annually for periods before July 1, 1965;
- 4 percent annually, July 1, 1965, through June 30, 1977;
- 5 percent annually, July 1, 1977, through June 30, 1981; and
- 6 percent annually beginning July 1, 1981.

## The 2.2 formula

The 2.2 formula improves the retirement benefit for TRS members by accelerating the rate at which future retirement benefits accrue. Formerly retirement benefits accrued at a slower rate in the early years as an educator and at a faster rate as service credit increased. The table below compares the previous four-step formula to the 2.2 formula.

### Annual Accrual Rate

<u>Years of service</u>	<u>Four-step formula</u>	<u>2.2% formula</u>
First 10 years	1.67%	2.2%
Second 10 years	1.9%	2.2%
Third 10 years	2.1%	2.2%
Years beyond 30	2.3%	2.2%

## 2.2 upgrade

Credit earned before July 1, 1998, may be upgraded to the 2.2 formula by making an optional payment. If a member does not upgrade pre-July 1998 service, benefits for this service will be based on the four-step formula. The upgrade to the 2.2 formula is entirely voluntary and may be elected by completing an upgrade application form. See Chapter 11, Retirement Benefits for an example of the upgrade cost.

## Purchasing credit for optional service

Several payment options – lump-sum, installments, direct rollover, payroll deduction – are available when a member wants to purchase credit for optional service, to repay refunded service, and to upgrade pre-1998 service to the 2.2 flat rate formula.

## Employer’s payment of member’s 2.2 upgrade balance or optional contribution balance

Provided a member has not entered into a payroll deduction agreement to pay the balance, an employer may pay all or part of the member’s 2.2 upgrade balance or optional contribution balance directly to TRS. If an employer is paying a member’s 2.2 upgrade, TRS can accept only one employer payment per year. The Employer Payment Coupon, which is shown at the end of this chapter, must be remitted with the payment. The employer must indicate on the form if the payment is a before-tax or after-tax payment.

If the employer chooses to “pick up” the amount on a before-tax basis in accordance with the Internal Revenue Code, Section 414(h), the amount is not included in the member’s gross taxable income for income tax purposes.

Federal guidelines require that a pick up authorization be included in either a collective bargaining agreement, a contract, or a resolution because the employer payment is not of a statutory nature. The authorization should read similar to the following language:

The contributions for the upgrade required under the Pension Code, Section 16-129.1 (40 ILCS 5/16-129.1), although designated as employee contributions, are being paid by {*name of employer*} in lieu of contributions by the employees and are being picked up pursuant to the Internal Revenue Code of 1986, Section 414(h)(2), as amended. The employees covered by the {*collective bargaining agreement, contract, resolution, etc.*} shall not have the option of choosing to receive the contributed amounts directly instead of having them paid by the employer to the Teachers' Retirement System.

The above language should also indicate the employee or group of employees for whom the pick up will be made.

## After-tax payments

After-tax payments are quick and simple. Full-time, part-time, and substitute teachers are eligible. Once a member has established their purchase cost by contacting TRS, they simply mail their check, include their Social Security number, and tell TRS how to apply their payment.

There are a few disadvantages. There are no current tax savings and no automatic deductions from a member's paycheck.

## Lump-sum or installment payments

TRS accepts personal checks, money orders, cashiers' checks, or online payments as either a lump-sum payment or installment payments using after-tax dollars. Cash and credit card payments are not accepted.

A member may make a lump-sum payment or installment payments directly to TRS when purchasing optional service credit or repaying a refund. Each installment payment must be a minimum of \$50. If the total balance due is less than \$50, the member's payment must be for the full amount due.

A member may make a lump-sum payment directly to TRS when purchasing credit for optional service, repaying refunded service, upgrading pre-1998 service to the 2.2 flat rate formula, or paying his/her early retirement option (ERO) contribution. A member may not be able to make direct payments if they are in a PDP.

A check(s) payable to THIS Fund is required for health insurance contributions due for periods of optional service after June 30, 1995.

Effective July 15, 2004, members may pay accounts receivable balances online using the Electronic funds transfer (EFT) automated clearing house (ACH) debit method

- to upgrade service to the 2.2 benefit formula;
- to purchase optional service credit and to pay health insurance contributions due on the purchase, if applicable;
- to repay a refund;

- to pay annuitant health insurance; and
- to pay ERO contributions.

Balances covered by a payroll deduction agreement are not eligible for online payment.

## Before-tax payments

### Payroll Deduction Program (PDP)

All PDP agreements end on June 30, 2010 in order to comply with recent IRS guidance. For more information about the program ending, see Chapter 8, Payroll Deduction Program.

A member who is employed on a full-time basis may make an irrevocable payroll deduction election with his/her employer to have the employer deduct optional service payments, 2.2 upgrade payments, or estimated ERO payments from the member's paycheck. This election enables the member to take advantage of tax-sheltered payments, which reduces their taxable income. Federal tax regulations generally do not allow a member to make direct payments or rollovers to TRS during the length of the PDP agreement.

### Rollovers

Rollovers allow a member to transfer pre-tax funds from many different types of retirement plans to TRS to pay for credit for optional service, repay refunded service, upgrade pre-1998 service to the 2.2 flat rate formula, or to pay his/her ERO contribution without loss of tax benefits. In many cases, this is a real advantage. A member's current custodian must agree to make the transfer, and the member must follow specific requirements set forth in federal tax regulations. TRS will accept rollovers from most qualified retirement plans. For more information, call (800) 877-7896.

TRS will accept spousal rollovers of distributions from Section 401(a), 401(k), Keogh, 403(a), 403(b), and 457(b) plans that the member's deceased spouse participated in or that have been divided by a Qualified Domestic Relations Order. Internal Revenue Service regulations do not allow TRS to accept rollovers from Roth IRAs.

Rollover payments are processed after TRS receives a completed Rollover Certification form. Members who entered into a PDP agreement may be restricted from using a rollover to pay for certain optional contributions.