



# Illinois Firefighters' Pension Investment Fund

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Transition Plan

March 2021

# Asset transition plan executive summary

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The Illinois Firefighters' Pension Investment Fund (FPIF) was established as a result of Public Act 101-0610, which was officially signed by Governor Pritzker on December 18<sup>th</sup>, 2019 and then took effect on January 1<sup>st</sup>, 2020. The law requires all 296 Article 4 pension funds to be consolidated into one statewide fund in an effort to reduce costs and increase performance. The transition of assets from the underlying funds must occur no later than June 30<sup>th</sup>, 2022.

The transition of assets from the 296 Article 4 pension funds to FPIF will be a major undertaking and have long term implications for FPIF and all underlying member funds. Numerous interdependencies exist that can challenge the success of the transition and the outcomes to stakeholders. The member funds consist of a complex set of assets and stakeholders which will require substantial coordination to ensure a smooth transition and the mitigation of risks.

FPIF is focused on delivering a successful transition and has prioritized this effort. In order to guide the transition, FPIF has defined 5 foundational guiding principles: **maximize risk adjusted returns, provide equitable treatment, reduce costs, act as a fiduciary, and facilitate transparency.** The key parties involved in the transition are: the FPIF Board, FPIF Leadership and Staff, Member Funds, Investment and Operational Consultants, External Auditors, Outside Counsel, and the Custodian.

A robust plan is required to effectively organize and execute the transition of assets in an effective manner. Through strategic discussions, the following report has been developed to guide the next steps of the transition. This report will assist with the execution of the transfer of assets with minimal member fund impacts while setting up the consolidated fund to achieve expected investment outcomes. This plan creates clarity on the roles, risks, and expected outcomes along with key tools to achieve a successful transition. A governance framework has been created to support addressing member fund complaints and potential remediation of issues at a later date. This report has been developed based on strategic discussions with key parties to support a successful transition while taking into account the complexity and regulatory expectations. The report is summarized in the below sections:

1. Approach to develop transition plan
2. Options considered for the transition
3. Key components required for a successful transition
4. Key control framework and consideration required to support the transition
5. Governance considerations to manage risks

This report has been developed based on information and insights as of March 2, 2021. Elements may evolved based on additional information.

# Approach to develop transition plan

## Objective

To develop a fit-for-purpose plan that covers all relevant key aspects to enable an effective and efficient transition while recognizing the complexities and context of the transition. This includes the following key components: determine how to transition the assets, what third parties are required to be in place, the necessary controls to mitigate risk, and overall framework.

Perform Scenario Analysis	Determine Transition Components	Perform Controls Considerations	Establish Asset Transition Governance
<ul style="list-style-type: none"><li>• Understand universe of potential options for transition</li><li>• Analyze and understand pros and cons for each option</li><li>• Summarize governance process</li></ul>	<ul style="list-style-type: none"><li>• Document key components required for a successful transition</li><li>• Analyze details of each component including risks, implications, partner impact, benefits, and challenges</li><li>• Present next steps for each component</li></ul>	<ul style="list-style-type: none"><li>• Provide controls framework overview</li><li>• Analyze key risks and associate transition controls</li><li>• Outlining how to mitigate risks through controls</li></ul>	<ul style="list-style-type: none"><li>• Outline the principle authorization of FPIF and member fund roles</li><li>• Provide an asset transition governance framework</li><li>• Present next steps for operationalizing transition governance framework</li></ul>
<b>Outputs</b> <ul style="list-style-type: none"><li>• Selected scenario</li></ul>	<b>Outputs</b> <ul style="list-style-type: none"><li>• Components timeline</li></ul>	<b>Outputs</b> <ul style="list-style-type: none"><li>• Controls framework and key summary</li></ul>	<b>Outputs</b> <ul style="list-style-type: none"><li>• Governance considerations</li></ul>

# Transition scenario analysis overview

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## Problem Statement

Determine the most suitable option for the asset transition to occur in an efficient, accurate and timely manner while recognizing the complexities for FPIF, member funds, the FPIF custodian and other relevant parties. A documented analysis of **how** to transfer the assets is required to determine the best suited approach for FPIF members and all stakeholders. Key considerations include: operational capability, interdependencies, 22C requirements, asset complexity, member fund and third party readiness.

### Scope\*

- Outline conceptual transition options for consideration
- Summarize key criteria to be evaluated for each option including: compliance, benefits, challenges, costs, critical path and partner impact
- Highlight and provide context on key results
- Provide a decision framework for FPIF to decide and evolve as required
- Outline expected roles to operationalize the transition option
- FPIF and the selected custodian are responsible for the operationalization of the included information

### Purpose

- Enable an informed FPIF decision on the transition of assets by highlighting key risks, interdependencies, and other information relevant to the successful transition
- Provide governance for transition planning, execution and evidencing for both FPIF and member funds
- Create risk and interdependency awareness for the complex transition process
- Outline the additional dependencies (i.e. certified Asset List auditor, 22C requirements etc.)
- Support FPIF custodian to faster appreciate as well as adequately plan and cost their role in the transition process while better understanding member fund complexities

### Key Risk Considerations

- FPIF custodian may not be ready / capable to implement specific parts and / or has different considerations leading to need for change
- Specific assets may be more difficult or not able to transfer
- Unexpected effort to transition may delay transition of all or parts of the plan
- Individual member funds may not be ready for transition and expectations will need to be managed

\* Operationalization of the detailed transition planning is not in scope. Reconsideration of transition option may be required based on new information

# Transition options and valuation criteria

Several options exist to transition assets from the local funds to the consolidated FPIF portfolio. Summaries of the various options are provided below.

	<b>Option 1: Bulk transition</b>	<b>Option 2: Phased approach</b>		
<b>Description</b>	Transition all member funds and their underlying assets on a single transfer date.	Transition sequencing based on various criteria (i.e. asset classes, member fund common attributes, custodians, etc.)		
<b>Sub-categories</b>	None	i. Sequence by asset class	ii. Sequence by member funds arbitrarily grouped	iii. Sequence by member fund (organized by Custodian, similar assets, size, FYs, etc.)
<b>Key Criteria*</b>	Regulatory Compliance ✓	X	✓	✓
Key risks	High	High	High	Medium
Benefits	Medium	Low	Medium	Medium
Partner Impact	High	Medium	High	Medium
Cost Impact	Medium	Medium	Low	Low
Complexity	High	High	Medium	Medium

Low	Smaller resource demand/effort will be required for transition activities. Reduced complexity and risk.
Medium	Moderate resource demand/effort will be required for transition activities. Increased complexity and risk.
High	Substantial resource demand/effort will be required for transition activities. Significantly increased complexity and risk

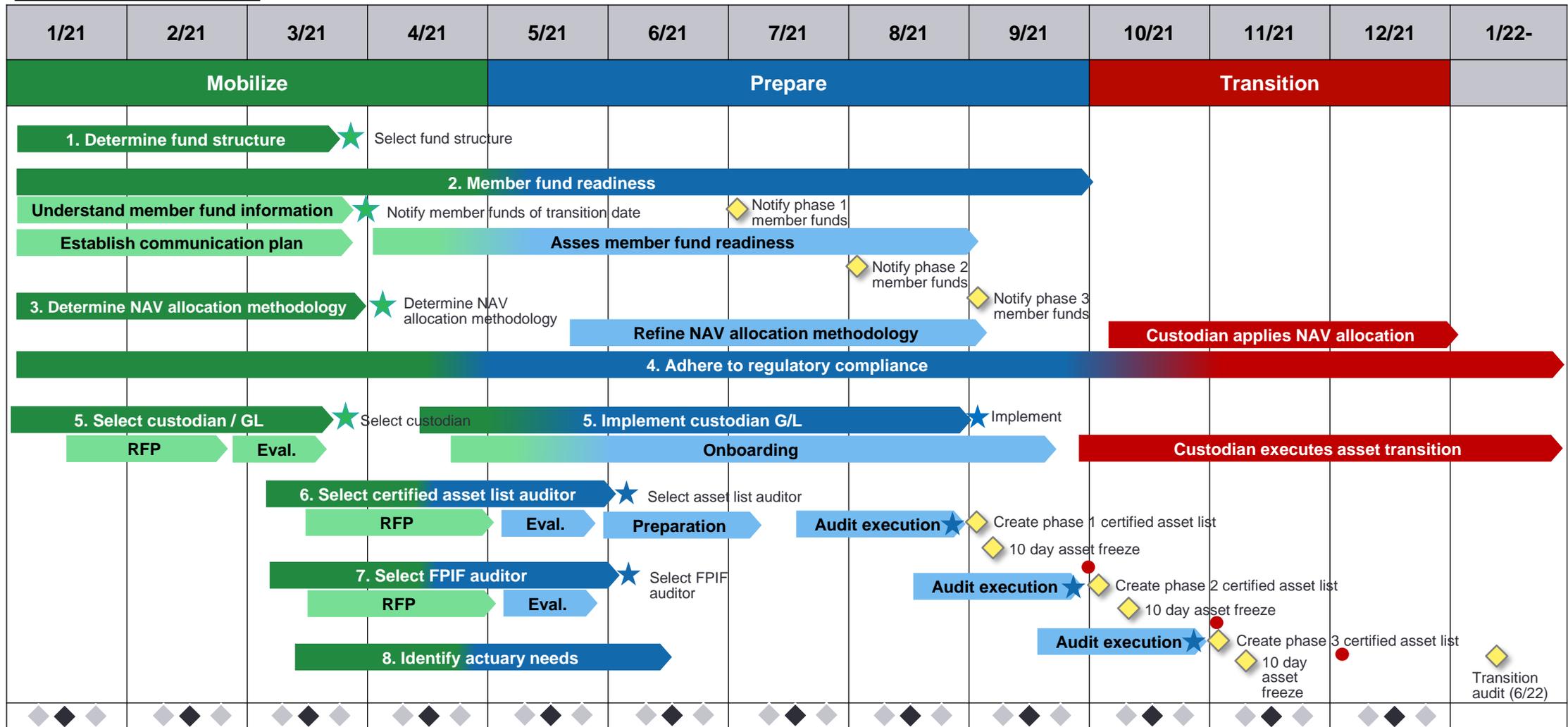
# Transition plan key components

The key components were determined based on analysis of the key elements of a successful transition and considerations on regulatory and member fund context to enable an effective transition.

Ref #	Key Component*	Rationale	Other considerations
1	<b>Set up FPIF fund structure</b>	<ul style="list-style-type: none"> <li>Foundation for reporting, accounting, and investment decisions</li> </ul>	<ul style="list-style-type: none"> <li>Statutory implications</li> </ul>
2	<b>Understand member fund readiness</b> <ul style="list-style-type: none"> <li>Understand member fund context</li> <li>Understand impacts on member funds</li> <li>Establish communication plan</li> <li>Assess member fund readiness</li> </ul>	<ul style="list-style-type: none"> <li>Understanding scope, member fund diversity, and complexity of transfer</li> <li>Conceptual impact of key topics for member funds (reporting, accounting, year ends, etc.)</li> <li>Consider member fund readiness support for complexity, diversity, and resource constraints</li> <li>Consider monitoring member fund readiness to minimize broader transition impact</li> </ul>	<ul style="list-style-type: none"> <li>Transition method</li> <li>Exception handling for select asset classes (insurance contracts)</li> <li>Management of public and private information</li> <li>Notification in writing to Local Boards for FPIF to assume fiduciary control</li> <li>Readiness monitoring framework</li> </ul>
3	<b>Determine NAV allocation methodology</b>	<ul style="list-style-type: none"> <li>Identify agreed mechanisms to value asset categories to be applied during transition</li> <li>Member fund asset ownership accounting (Unitization vs. commingled)</li> </ul>	<ul style="list-style-type: none"> <li>Impact of standardize valuation mechanism on member funds</li> </ul>
4	<b>Adhere to regulatory compliance requirements</b>	<ul style="list-style-type: none"> <li>Section 22C and other asset transition requirements</li> <li>Compliant with statute</li> </ul>	<ul style="list-style-type: none"> <li>Notification, asset freeze, book end date (6/22)</li> <li>Transition date communication</li> </ul>
5	<b>Select custodian and determine G/L and implement</b>	<ul style="list-style-type: none"> <li>Custodian required to safeguard assets</li> </ul>	<ul style="list-style-type: none"> <li>Custodian qualifications</li> </ul>
6	<b>Select auditor to perform certified asset list audit of 296 member funds</b>	<ul style="list-style-type: none"> <li>Mandated by statute</li> <li>Critical component for custodian transition plans</li> <li>Critical path that would prevent transition from occurring</li> <li>Critical component of control plan</li> </ul>	<ul style="list-style-type: none"> <li>Sequence of audit, ability of auditor to conduct</li> </ul>
7	<b>Select FPIF auditor(s)</b>	<ul style="list-style-type: none"> <li>Auditor will comment on fund structure</li> <li>Implications on member fund reporting and GASB</li> </ul>	<ul style="list-style-type: none"> <li>Selection timing</li> <li>Agreement on auditor for 3 audits (6/21 year end, transition, and 6/22 year end)</li> </ul>
8	<b>Identify actuary needs</b>	<ul style="list-style-type: none"> <li>Placeholder, subject to further discussions</li> </ul>	<ul style="list-style-type: none"> <li>N/A</li> </ul>

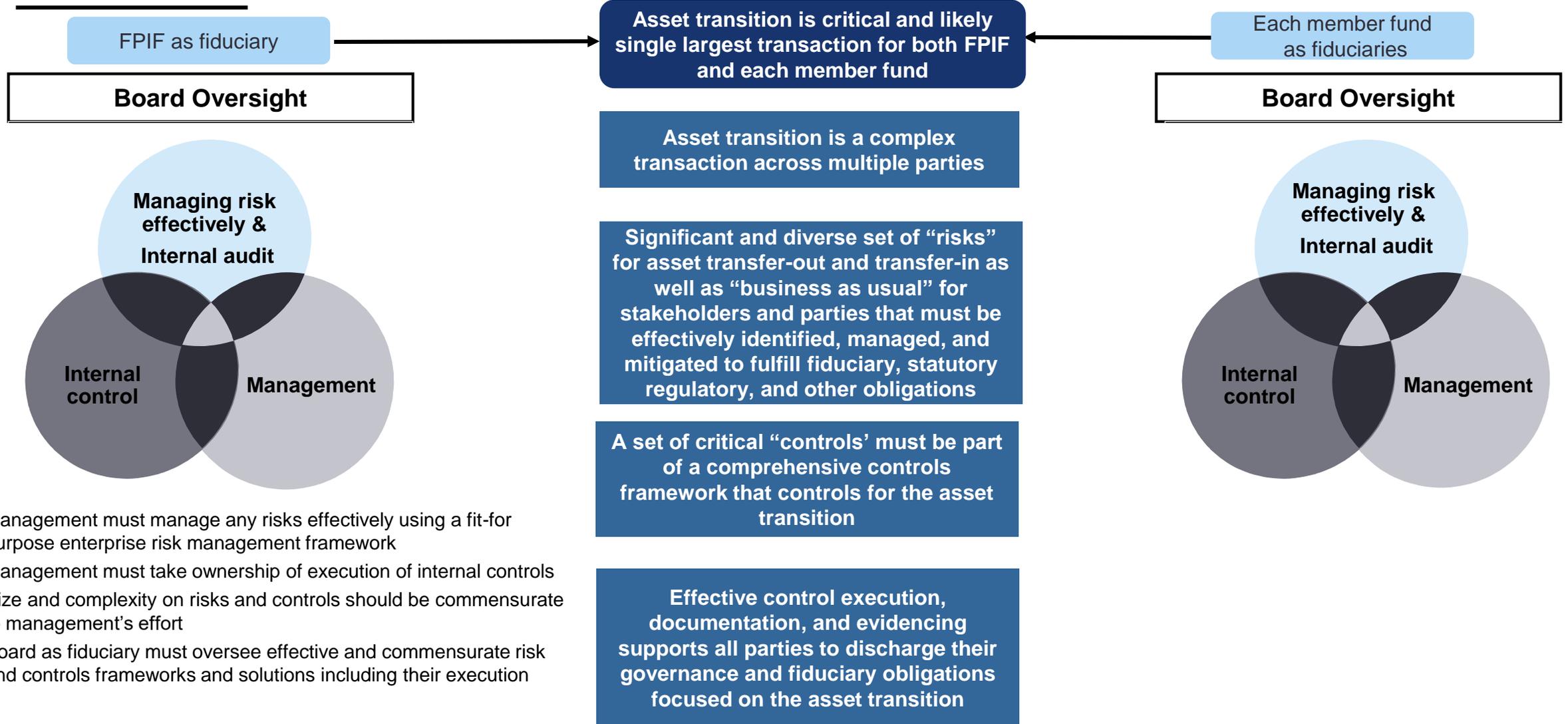
\*Transition checklist components are not ordered by priority

# Transition components timeline



LEGEND: ▶ Key phase   Activities ★ Critical Path Milestone   Steering committee   Audit committee   Key statute activity ● Transition date

# Controls in the asset transition context



- ▶ Management must manage any risks effectively using a fit-for purpose enterprise risk management framework
- ▶ Management must take ownership of execution of internal controls
- ▶ Size and complexity on risks and controls should be commensurate to management’s effort
- ▶ Board as fiduciary must oversee effective and commensurate risk and controls frameworks and solutions including their execution

# Transition governance initial framework

A key aspect of the transition will be to establish a **'fit-for-purpose'** governance framework for the asset transition to support an efficient and accurate asset transition while aiming to minimize undue impact.

Section 22C paragraph 119 authorizes FPIF to determine the asset transition process while individual member funds are required to adequately support and prepare for transition. As such, governance and role clarity is important to recognize the policy intent and regulation that empowers FPIF to drive the process.

The complexity of this transition across FPIF, member funds and third parties, requires an organized decision-making and oversight process to effectively manage risks while maintaining fairness. With this in mind, FPIF aspires to support member funds in a prudent and practical manner to limit impact.

