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Illinois Supreme Court provides premonition of constitutional decisions yet to come

by Carolyn Welch Clifford

With the Illinois Supreme Court's decision to declare unconstitutional the State of Illinois' law which altered the state's contribution obligation for state workers' health insurance premiums, the court showed its hand on the pending lawsuits challenging the State's pension reform law enacted in December. In *Kanerva v. Weems,* 2014 IL 115811 (July 3, 2014), the Illinois Supreme Court reviewed a constitutional challenge to amendments to the State Employees Group Insurance Act. In a six to one decision, the Illinois Supreme Court declared the law unconstitutional under the pension protection clause of the Illinois Constitution.

Prior to the amendments, the State Employee Group Insurance Act originally provided that the State would cover the full cost of health benefits for pre-1988 members of the state's employee retirement systems and make specified contributions for post-1988 members of those systems. Over the years, various changes and agreements regarding health insurance premiums ensued, including an early retirement incentive program enacted in 2002 that tied certain creditable service to health insurance coverage once pension benefits began. Ten years later, in July of 2012, the State enacted P.A. 97-695 which significantly altered the State's obligation to contribute toward the cost of health insurance coverage to employees participating in three of the State's retirement systems – State Employees Retirement System (SERS), State University Retirement System (SURS) and Teachers' Retirement System (TRS).

Four separate lawsuits challenged the constitutionality of the amendments, asserting that the State's obligations under the prior law to make specified contributions toward the health insurance premiums of members constituted a "benefit of membership" in the retirement systems within the meaning of Article XIII, Section 5 of the Illinois Constitution of 1970 (the "pension protection clause"). The lawsuits contended that the amendments to the State Employee Group Insurance Act had "diminished or impaired" their retirement system membership benefit by requiring members to contribute additional amounts toward their health care that had been previous borne by the State. Additional legal challenges included assertions that the changes violated the separation of powers and contract clauses in the Illinois Constitution, as well as violated the principle of promissory estoppel for those now-retired employees who took the early retirement option in reliance on the State's promises regarding health insurance premiums.

The question before the court was essentially whether a health insurance subsidy provided in retirement qualifies as a benefit of membership in a pension system, such that it is protected by the pension protection clause of the Illinois Constitution. The court initially stated that this presented an issue of first impression before it, while noting that two Illinois courts had recently addressed this issue, reaching opposite conclusions (*Marconi v. City of Joliet*, No. 10 -MR-165, July 21, 2011, *reversed and remanded on other grounds,* 2013 IL App

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Court derails pension board's legal challenge to a decade of municipal underfunding

by Shawn Flaherty

The Village of Riverdale, like many municipalities in our state, is a community in financial stress. The mayor has admitted as much in his January 1, 2014 letter to Village residents stating that in the past, the Village "continuously ran annual deficits, borrowing against our future revenues and leaving unpaid bills behind." One aspect of the Village's failure to meet its obligations was challenged by the Riverdale Police Pension Fund in a declaratory judgment action filed by the Fund against the Village in August 2010; namely, whether the Village breached its statutory funding obligations by failing to levy appropriate property taxes for police pension purposes pursuant to Sections 3-125 and 3-127 of the Illinois Pension Code (40 ILCS 5/3-125 and 5/3-127) In *Board of Trustees of the Riverdale Police Pension Fund v. Village of Riverdale*, 2014 IL App (1st) 130416, the First District Appellate Court concluded that while any taxes levied for pension purposes must be provided to the Fund, the Village was not obligated to provide contributions to the Fund at an actuarially calculated level.

Section 3-125 of the Illinois Pension Code provides in pertinent part that the "municipality shall annually levy a tax upon all the taxable property of the municipality" that when added to police officer contributions and other revenues will "equal a sum sufficient to meet the annual requirements of the police pension fund." Section 3-127 provides a mechanism whereby the municipality has a period of 40 years to ensure that the

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necessary pension reserves are in place for the benefit of the pension fund.

In its pleadings, the Village admitted that it did not follow the tax levy recommendations issued by the Illinois Department of Insurance for more than a decade, nor did the Village retain its own actuary to determine an appropriate tax levy amount pursuant to Section 3-125 over this same time period. The Village argued that it was not required to levy at a particular funding level for the pension fund and that Article XIII, Section 5 of the Illinois Constitution did not provide pension fund participants with any expectation as to a particular level of pension funding, but only the right to pension benefits upon retirement. The Cook County Circuit Court granted summary judgment to the Village as a matter of law, and the case was appealed to the Illinois Appellate Court for the First District.

On appeal, the pension board argued that the circuit court erred in determining that the Village was not statutorily or constitutionally mandated to provide a particular level of funding to the pension fund. The appellate court first reviewed existing legal precedent in finding that the Illinois Constitution's pension protection clause extended to pension benefits only and had no impact on the funding of the benefits, citing two Illinois Supreme Court cases: *McNamee v. State of Illinois*, 173 Ill.2d 433 (1996) and *People ex rel. Sklodowski v. State*, 182 Ill.2d 220 (1998). The *Riverdale* opinion echoed the language of these previous decisions that stated that the Illinois Constitution pension protection clause does not serve to freeze "the politically sensitive area of pension financing" and does not evince a legislative intent to create vested contractual rights to anything beyond benefits.

The *Riverdale* court next reviewed whether Sections 3-125 or 3-127 of the Illinois Pension Code demonstrated a legislative intent to establish a contractual right to a specified level of pension funding. The appellate court found no such intent. Neither statute used the term "contract" in relation to funding or establishing anything more beyond a right to the pension earned, and the appellate court declined to find any implied right of contract in either statute. The appellate court upheld the circuit court judgment on the merits and declined to address a standing issue raised on appeal.

Despite its success on the pension funding issue, the Village of Riverdale did not exit this litigation unscathed. The appellate court ordered that the Village was liable to calculate and pay its pension fund for the value of all property tax dollars levied and collected by the Village for pension purposes but instead spent on other Village expenses. The court remanded the matter back to the circuit court to determine how much collected tax money the Village owes to the pension fund.

It is clear from this case that property tax dollars levied, extended and collected for pension purposes may only be spent for legitimate pension purposes and not for other municipal debts. This is consistent with the language of Section 3-132 of the Illinois Pension Code that provides that "all money received or collected shall be credited by the treasurer of the municipality to the account of the pension fund" subject to pension board order and direction (40 ILCS 5/3-132). While there is no contractual right to specified pension funding level, the *Riverdale* opinion does require that pension levies be paid to pension funds for pension purposes. ■

When a workers' compensation settlement offsets disability payment

by Vladimir Shuliga

Illinois courts have long held that if an employee receives workers' compensation while also receiving disability pension payments, the pension fund is required to offset the amount of the workers' compensation benefit. The purpose of the offset provision is to prevent a pension fund participant from obtaining double recoveries of disability benefits for the same time period. In *Wright v. SURS*, 2014 IL App (4th) 130719, the Illinois Appellate Court recently considered whether the timing of the workers' compensation settlement payment determines the applicability of the offset. The court held that the timing of the actual payment is irrelevant for the purposes of the offset, as long as the workers' compensation benefit is paid for the same period of time that the disability pension benefits are payable.

In *Wright*, the plaintiff was awarded a disability benefit in July 2007 from the State Universities Retirement System of Illinois (SURS). Upon learning of a workers' compensation settlement, SURS notified Wright that she owed $51,413.62 back to SURS. Initially, Wright followed the administrative procedures within SURS to challenge the offset. Wright contended that her workers' compensation award was not paid until January 11, 2011; therefore, the offset should only apply to SURS benefits received after that date. Wright had retired in February 2011, thereby terminating her disability benefits. Thus, she argued that she only owed the $2,185.25 she received between January 11, 2011, and her retirement in February 2011, rather than $51,413.62 claimed by SURS. In February 2012, the Claims Panel of SURS issued a written opinion upholding the SURS staff determination that Wright owed $51,413.62. In June 2012, the Executive Committee of the

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(3d) 110865; *Underwood v. City of Chicago*, No. 13 C 5687, 2013 WL 6578777, at *5-11 (N.D.Ill. December 13, 2013).

The defendants argued that the pension protection clause was confined strictly to retirement benefits authorized under the Illinois Pension Code. The court disagreed, concluding that there was nothing in the text of the Illinois Constitution which warranted such limitation. The court explained:

> If [the drafters of the Illinois Constitution] had intended to protect only core pension annuity benefits and to exclude the various other benefits state employees were and are entitled to receive as a result of membership in the State's pensions systems, the drafters could have so specified. But they did not.

The court then reviewed the context of the then-proposed pension protection clause at the time of the constitution convention, providing some insight as to the clause's meaning. The court explained that at the time of the constitutional convention, Illinois adhered to the "traditional classification of pension plans as either mandatory or optional." Under this classification, if the employee's participation was mandatory, the rights created were considered to be in the nature of a "gratuity" which could be revoked at will. However, where the employee's participation in a pension plan was optional, the pension was considered "enforceable under contract principles."

The court noted that this created uncertainty regarding the enforceability of pension rights, and this was further exacerbated by proposed creation of broad home rule powers for municipalities. Ironically, some convention delegates "feared" that these home rule powers "could lead municipalities into debt and result in their abandoning their pension obligations to public employees, including police officers and firefighters." The court stated:

> Delegates [at the constitutional convention] were also mindful that in the past, appropriations to cover state pension obligations had "been made a political football" and "the party in power would just use the amount of the state contribution to help balance budgets," jeopardizing the resources available to meet the State's obligations to participants in its pension systems in the future.

According to the constitutional convention floor debates, the proposed pension protection clause would accomplish two goals:

> [I]t first mandates a contractual relationship between the employer and the employee; and secondly, it mandates the General Assembly not to impair or diminish these rights.

The court further noted:

> It does so … in order to protect "public employees who are beginning to lose faith in the ability of the state and its political subdivisions to meet these benefit payments" and to address the "insecurity on the part of the public employees [which] is really defeating the very purpose for which the retirement system was established."
>
> Delegate Kemp, who spoke in support of the measure, viewed its purposes as "mak[ing] certain that *irrespective of the financial condition of a municipality or even the state government*, that those persons who have worked for often substandard wages over a long period of time could at least expect to live in some kind of dignity during the golden years..." (emphasis added)

After reviewing the floor debates, the court concluded that the pension protection clause was "intended to eliminate the uncertainty" of the traditional classification of retirement systems, and that the *"provision was aimed at protecting the right to receive the promised retirement benefits, not the adequacy of the funding to pay for them."* (emphasis added) In short, the court held that "all of the benefits that flow from that relationship (including subsidized health care following retirement) are constitutionally protected under article XIII, section 5." In making this determination, the court noted that it was mindful of the liberal construction that pension statutes are to be afforded in favor of the rights of the pensioner, which it concluded applied "with equal force to our interpretation of the pension protection provisions set forth in article XIII, section 5."

A dissenting opinion by Justice Burke argued that subsidized health insurance premiums provided under the Group Insurance Act are "not pension benefits," noting that pension benefits differ substantially from subsidized health insurance premiums. Justice Burke further noted:

> Moreover, by adding language to the pension protection clause, the majority fundamentally changes its meaning. The clause no longer protects the statutory benefits provided by a pension or retirement system. Instead, it provides constitutional protection to any statutory benefit – however unrelated to pensions – if the recipient of the benefit is a member of a pension system.

Speculation as to what the court's decision in *Kanerva* means for the pending litigation challenging the constitutionality of the pension reform law signed into law in December 2013 (P.A. 98-599) was swift. While proponents of pension reform reportedly are not conceding defeat, other

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commentators have declared the pension reform law to be "dead as a doornail." Others have speculated that the State's "Plan B" may be to revisit a constitutional amendment to modify or eliminate the pension protection clause, a plan that may only provide prospective relief. In any event, there is a belief that the pending litigation will be expedited and summarily disposed by the court without going to trial. (See "Amending the Illinois Constitution a tough path for pension reform," *Crain's Chicago Business*, July 16, 2014) ■

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Board of Trustees of SURS adopted the administrative decision of the Claims Panel. Wright filed a lawsuit, and in July 2013, the circuit court affirmed the decision of the Executive Committee.

Wright appealed the decision, maintaining that the offset should only apply to disability benefit payments made after she received her workers' compensation settlement. The court determined that the case turned on the meaning of the term "payable" as used in the Illinois Pension Code.

Wright argued that her workers' compensation settlement was not paid until 180 days after the award was approved, and that it should not be considered "payable" until payment was actually received on January 11, 2011. SURS, on the other hand, argued that the date the payment was made was irrelevant. If that were the case, disability benefit recipients could simply delay receipt of the workers' compensation settlement and avoid reimbursing SURS for the offset. The court found that the legislature could not have intended the offset provision of the Illinois Pension Code to create such a result.

The court agreed with SURS, finding that the date of actual payment was irrelevant. Instead, the court found the relevant issue to be "whether the workers' compensation award is being issued for the same period of time for which the SURS participant also received disability benefits." It was clear that Wright's workers' compensation settlement and disability benefits were being paid for the same period of time. Therefore, the court upheld the circuit court's order finding that Wright must reimburse SURS $51,413.62.

The workers' compensation offset provisions of Articles 3 and 4 of the Illinois Pension Code are identical to each other but slightly different than provision which applied to Wright's pension in *Wright*. (40 ILCS 5/3-114.5; 40 ILCS 5/4-114.2; 40 ILCS 5/15-153.1) Under all three provisions, certain workers' compensation payments cannot be counted for offset purposes.

The primary takeaway from the *Wright* case holds true for Article 3 and Article 4 disability pension claimants: any temporary total disability payments received from workers' compensation for the same injuries and period of time that disability benefits are sought will be offset from the amount of the disability pension benefit. Once the workers' compensation payment is finalized -- perhaps with a finding of permanent partial disability -- the offset will no longer apply, and the claimant will be entitled to the full amount of the disability pension benefit.

Although the dynamic between workers' compensation and a disability pension is slightly different depending on the facts of a particular situation, *Wright* reiterated the general principle that a pension fund is entitled to an offset from workers' compensation payments that are received for the same period of time that disability pension benefits are received. Whether Wright was intentionally delaying her workers' compensation settlement in this case is unclear. However, it certainly would not have been a surprising result to see disability claimants purposefully delay the receipt of workers' compensation benefits if Wright had succeeded in her claim against SURS. As noted by the court "in almost any situation . . . disability benefits will be paid long before a workers' compensation award is issued." Thus, the delay in receiving workers' compensation payments may also be the innocent result of a lengthy process. Nonetheless, the result in this case makes clear that a pension fund will be entitled to reimbursement for payments received from workers' compensation for the time period in which the beneficiary received disability benefits. ■