

Governor Quinn Signs Public Act 98-0599, Enacting Landmark Pension “Reform”

On December 5, 2013, Governor Quinn signed Public Act 98-0599 (hereinafter “Act”), which became sweeping legislation for the five state retirement funds. While P.A. 98-0599 does not affect Article III, IV, V, and VI (i.e. changing benefits for Chicago police, downstate police and fire pension funds), it is widely believed many of the changes incorporated may become a template for pension reform related to Article III, IV, V, and VI in future legislative sessions.

Of the 325 page Act, the following are some of the aspects of the Act that may be of potential concern for police and fire pension fund participants and beneficiaries: Future COLAs will be adjusted by CPI each year, retirement age will be increased on a graduated scale, up to five percent (5%), Tier I members will have the option of participating in a defined contribution plan, and all pension matters, with the exception pension pick-ups, are removed from the collective bargaining process. The good news is that the employee contribution towards their pension will be one percent (1%) less and mandatory one hundred percent (100%) funding is required no later than 2044. The Act also contains a “funding guarantee,” which compels the state to make required pension payments and/or contributions.

As discussed in this newsletter, lawsuits challenging this law have already been filed. More will join. We are hopeful the General Assembly will not apply similar changes to police and fire funds until the courts have determined the legality of this legislation. Our attorneys are closely monitoring the lawsuits and will continue to provide updates.

Retirees File Suit to Strike Down Latest Round of Pension “Reform”

Heaton et al. v. Quinn et al.,

Case No. 2013-CH-28406 (Circuit Court of Cook County)

Near the end of 2013, members of the Teachers’ Retirement System (TRS) filed a class action law suit seeking to strike down Public Act 98-0599 (hereinafter “Act”). Plaintiffs claim the Act violates the Pension Protection Clause, Article XIII, Section V of the Illinois Constitution in three ways. Plaintiff argue first, the formula used to calculate COLAs for pension annuities diminishes the amount retirees currently receive and have been promised. Second, Plaintiffs allege the Act is unconstitutional because it raises the retirement age for members of certain retirement systems. Finally, that the Act imposes a new cap on the amount of pensionable salary for certain members of the retirement system. Plaintiffs’ ask the court to enter an injunction barring the Act from being applied. Plaintiffs’ also ask the court to declare the Act unconstitutional, award money damages, and grant attorneys’ fees to the Plaintiffs.

Illinois State Employees Association, Retirees v. St. of Ill.,

Case No. 2014CH0003 (Circuit Court of Sangamon County)

Similarly, on January 2, 2014, the Illinois State Employees Association, Retirees representing more than 9,000 retired state workers, filed a lawsuit in Sangamon County seeking to strike down the most recent round of pension “reform.” Plaintiffs argue portions of Public Act 98-0599 violate Article XIII, Section 5 of the Illinois Constitution. In addition, the suit contends that the Act violates the equal protection clause of the Illinois Constitution because it does not apply to the

Judicial Retirement System. This lawsuit also seeks class certification. So far only retirees and their representative organizations have filed suit.

Several labor unions and unrepresented employees have vowed to file suit. We are following each of these cases closely and will continue to provide updates.

Bankruptcy Court Issues Preliminary Opinion Allowing Detroit Bankruptcy to Proceed

In Re City of Detroit, Debtor, No. 13-53846, Honorable Steven W. Rhodes, Presiding

As previously reported in Volume 11, Issue 4 of the R&K Legal and Legislative Update, the City of Detroit bankruptcy filing has potential implications for Illinois public pension funds, despite the fact that Illinois does not currently authorize its municipalities to file bankruptcy.

On December 5, 2013 Judge Rhodes issued a 143 page opinion refusing to dismiss the City of Detroit bankruptcy petition under Chapter 9 of the Bankruptcy Code. The court found the City was eligible for bankruptcy, was insolvent, and that the City did *not* negotiate in good faith with its creditors, but was not required to do so, because negotiations were impracticable.

The Court was faced with 109 individual objectors, including the Detroit Police and Fire Retirement System (“PFRS”), which administers the pension plan for Detroit’s uniformed personnel. The average annual benefit received by beneficiaries is about \$30,000. Generally, like most Illinois Public Employees, PFRS’s retirees are not eligible for social security retirement or disability benefits. Among the reasons relied upon by the City for filing its bankruptcy petition, was the \$3.5 billion in unfunded pension obligations, which include PFRS.

Prior to filing the bankruptcy proceeding, the City met with its creditors, including representatives from PFRS. At the meeting, the City was to provide additional information about its pension restructuring proposal and discuss the process for reaching an agreement on pension underfunding issues. In addition, prior to the bankruptcy filing on July 3, 2013, two lawsuits were filed in state court contending Public Act 436 violated the Michigan Constitution to the extent it may authorize bankruptcy proceedings where vested pension benefits will be impaired. On July 17, 2013, the pension systems’ initiated a similar law suit. On July 19, 2013, the Ingham County Circuit Court Judge entered an Order of Declaratory Judgment, holding that Michigan’s authorization to commence the Chapter 9 bankruptcy case violated Michigan’s State Constitution’s “pension protection clause.” *Gracy Webster et al. v. State of Michigan et al.*, No. 13-734-CZ. The bankruptcy court ignored this holding.

The bankruptcy objectors raised numerous legal arguments in opposition to the bankruptcy proceeding. All were rejected by the court. The Court found that Chapter 9 does not violate Article I, Section 10 of the United States Constitution, known as the “contract clause.” The Court characterized this agreement as “frivolous,” noting that the bankruptcy clause necessarily authorizes Congress to make laws that would impair contracts. In addition, the Court found that Chapter 9 does not violate the Tenth Amendment to the U.S. Constitution, which provides that all rights not specifically given to the United States Government, are retained by the States.

Most disturbing is the Court's rejection of the Michigan pension plans' arguments premised on the Michigan Constitution, that pension plans have greater protection than other contract debt. After a historical review of the pension protections found in the Michigan Constitution, the Court concluded a slight difference between the language protecting contracts (no "impairment") and the language protecting pensions ("no impairment" or "diminishment"), did not demonstrate pensions were given any extraordinary protection. In its ruling on this issue, the Court concluded under the Michigan Constitution, pension rights are contract rights and are subject to impairment in federal bankruptcy proceedings. Of note, the Court did comment: "No one should interpret this holding that pension rights are subject to impairment in this bankruptcy case to mean that the Court will necessarily confirm any plan of adjustment that impairs pensions. The Court emphasizes that it will not likely or casually exercise the power under Federal Bankruptcy Law to impair pensions."

The Court explained its decision was a "preliminary matter" in a bankruptcy case. The ultimate goal, is confirmation of a plan of adjustment and the Court encouraged the parties to begin to negotiate in an attempt to obtain a consensual plan. Appeals will follow. R&K attorneys will continue to monitor this case and keep you apprised of any developments.