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Legal Aspects for New Public Pension Trustees

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This material is provided for information and educational purposes and is not intended to be a substitute for legal advice. The author cautions that you consult with your attorney before taking any action based on the material contained in this document.

The information contained in this handout is designed to highlight basic information for individuals who have been elected or appointed as new trustee board members to Police and Firefighter Pension Funds in downstate Illinois. Due to time and space constraints, the subject matter in this handout is greatly condensed. Trustees seeking more detailed information on any of the areas highlighted in this material should consult with the IPPFA or an attorney who is experienced in dealing with Public Pension Fund issues.

1. **LAWS GOVERNING ARTICLE 3 AND ARTICLE 4 PENSION FUNDS:**

Downstate Police Pension Funds are governed by Article 3 of the Pension Code which is 40 ILCS 5/3-101, et seq. Downstate Firefighter Pension Funds are governed by Article 4 of the Pension Code which is 40 ILCS 5/4-121, et seq. Every Trustee should read and be familiar with the provisions contained in the Pension Code which applies to their fund. You can review and download copies of this information from various websites, including the Illinois Public Pension Fund Association website at www.IPPFA.org.

2. **RESPONSIBILITIES AND FIDUCIARY DUTIES:**

Under the Illinois Pension Code, public pension fund trustees are vested with exclusive control and management of the public pension fund. The major duties of a police or firefighter pension fund trustee include, but are not limited to, the following:

- A. Holding trustee elections;
- B. Admitting members into the fund;
- C. Investing pension fund assets;
- D. Deciding retirement and disability claims;
- E. Making sure adequate contributions are made into the fund;
- F. Disbursing pension fund monies;
- G. Hiring necessary expert assistance.

Any mistake regarding any of the above could cost the pension fund tens of thousands of dollars. Each trustee needs to read and understand the following provisions of the Illinois Pension Code.

40 ILCS 5/1-109. Duties of Fiduciaries. A fiduciary with respect to a retirement system or pension fund established under the Code shall discharge his or her duties with respect to the retirement system or pension fund solely in the interest of the participants and beneficiaries and:

- (a) For the exclusive purpose of:
 - (1) Providing benefits to participants and their beneficiaries; and
 - (2) Defraying reasonable expenses of administering the retirement system or pension fund;
- (b) With the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims;
- (c) By diversifying the investments of the retirement system or pension fund so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and
- (d) In accordance with the provisions of the Article or the Pension Code governing the retirement system or pension fund.

In order to comply with these statutory provisions, pension board trustees should have a full understanding of the pension board procedures and any documents used by the board in administering the pension fund. Board members should determine who the board's various advisors are and what function each is to provide. These would include a board attorney, an investment manager(s), an investment consultant, a CPA/Auditor and a board clerk or administrator, if any. Board members should establish investment guidelines and objectives for the fund and the investment manager to follow. Trustees should review carefully the investment manager(s) performance based upon criteria spelled out in the Investment Policy and Guidelines. Board members should attend conferences and join organizations which can provide them with continuing updates and education regarding the law and how it applies to the administration of their duties. Board members should avoid allowing any one person to run or control the pension board or pension fund.

3. **ELECTION AND APPOINTMENT OF TRUSTEES:**

Police and Firefighter Pension Boards currently are organized similarly with boards consisting of five members (2 members are elected from the active duty participants, 2 members are appointed by the Mayor, and 1 member is elected from the retired members or the beneficiaries of the fund). Police Pension Trustees serve 2 year terms. Firefighter Pension Trustees serve 3 year terms. These terms are typically staggered. The election for board members shall be held biennially on the third Monday in April at a place in the municipality and under the Australian ballot system. The Treasurer for the municipality serves as an ex-officio, non-voting member of the Pension Board (unless appointed by the Mayor to serve as a full board member). The Treasurer also serves as the Custodian for the Pension Fund monies. Members of the board shall not receive any salary from the pension fund for services performed as trustee.

The Pension Code provides for the election of officers by sitting board members. These elections take place at the July board meeting when the board should be reorganized on an annual basis. Police Boards are to elect the following officers to serve for 1 year or until the following board elections: President, Vice-President, Secretary, Assistant Secretary. The remaining board member simply serves as a Trustee with no officer title. Firefighter Boards are to elect a President and Secretary.

4. **ADMITTING MEMBERS INTO FUND:**

New employees who are hired as policemen or firefighters are not required to join the police or firefighter's pension fund. However, those new employees wishing to join their respective pension funds must do so by submitting a written application to join the pension fund within three months after receiving his or her first appointment or re-appointment. The Pension Board must then vote on the acceptance of the applicant. The board can no longer base its decision on results of a physical for the new employee. Physicals for new employees are performed by the municipality and not the pension board. Trustees should make certain that the statutory contributions are properly deducted from the applicant's salary and are deposited into the pension fund. It is important for boards to maintain complete files for all members who are participants in the pension fund. These records are subject to review by the Illinois Department of Insurance.

5. MEETINGS OF BOARDS AND THE ILLINOIS OPEN MEETINGS ACT:

The Pension Code provides that Police Boards are required to meet quarterly in the designated months of January, April, July and October. The Pension Code does not designate the frequency for which Firefighter Boards are required to meet. However, it is generally recommended that Firefighter Boards meet at least quarterly. Police and Firefighter Boards may meet more frequently if needed to conduct business related to the Fund.

Police and Firefighter Pension Board meetings are public meetings which are subject to the Illinois Open Meetings Act, 5 ILCS 120/1 et seq. All meetings must be held at specified times and places which are convenient to the public. In 2007, the Open Meetings Act was amended to clarify that for a 5-member public body, 3 members of the body constitute a quorum and the affirmative vote of 3 members is necessary to adopt any motion or resolution unless a greater number is otherwise required.

There are certain exceptions to this Act which allow for “closed meetings” or “executive sessions”. However, these exceptions are narrowly construed by the Courts. No final action may be taken in closed sessions. The Act requires public notice whether the meeting is open or closed to the public. An Agenda for each regular meeting must be posted at the “principal office” of the public body where the meeting is to be held, at least 48 hours in advance of the meeting. A pension board must keep minutes of all meetings, whether open or closed. Minutes shall include the date, time and place of the meeting; members who are present or absent; a general description of all matters proposed, discussed or decided and a record of any votes taken; minutes of open meetings should be available to the public within 7 days of the approval of the minutes; minutes of meetings closed to the public shall be available only after the pension board determines it is no longer in the public interest or privacy of an individual to keep them confidential; pension boards must review minutes of closed sessions at least semi-annually to determine whether the need for confidentiality still exists or if minutes are no longer required to be confidential, the decision must be reported in open session. Non-compliance with provisions of the Illinois Open Meetings Act may result in one or more of the following: a civil suit may be brought by an individual, including a State’s Attorney, within 60 days after the meeting alleged to be in violation of the Act or within 60 days of the date from when facts concerning violation of the Act are discovered; Court’s can declare any final action taken as null and void or issue an Order compelling the pension board to conduct open meetings or

make public minutes; Courts can assess reasonable attorney fees and costs against any party except State's Attorney to the prevailing party; any person who violates the provisions of the Act is guilty of a Class C misdemeanor, 5 ILCS 120/4. Board members should note changes to the Illinois Open Meetings Act are scheduled for January 1, 2010. (See *Heading 17 in this handout*)

6. **DECIDING RETIREMENT & DISABILITY CLAIMS:**

The Police and Firefighter Pension Codes empower the Board of Trustees of the respective pension funds to determine an applicant's entitlement to retirement or disability benefits. The Trustees of the Board are fiduciaries and must exercise their statutory authority for the benefit of those intended to be protected (vested participants), and consistent with the constitutional principle of due process of law. The determination of an application for retirement or disability benefits is considered a quasi-judicial function. Boards would be well advised to hire experienced legal counsel to assist them in the processing of claims, particularly disability claims when they are filed.

The Illinois Department of Insurance maintains a benefits calculator which can be used on line to assist pension boards in calculating retirement and disability benefits. The website for the Department is www.insurance.illinois.gov/Applications/Pension. The email address is: doi.pension@illinois.gov

The Police and Firefighter Pension Codes provide for a variety of different benefits.¹

Of particular interest to pension boards is the manner in which disability hearings (i.e. requests for "line of duty" or "not on duty" disability pensions, etc.) should be conducted. Although the sections of the Police and Firefighter Pension Codes may not parallel one another, the procedures implemented in handling a disability claim, are consistent. The applicant has the burden to prove his alleged disability. The applicant should submit to the board medical evidence relating to his alleged disability along with a physician's medical report and certification of disability. The applicant may produce witnesses

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40 ILCS 5/3-114.1 (Line of Duty); 40 ILCS 5/3-114.2 (Not on Duty); 40 ILCS 5/3-114.3 (Heart Attack or Stroke Suffered in Performance of Duties); 40 ILCS 5/3-114.6 (Occupational Disease Disability); 40 ILCS 5/4-110 (Line of Duty); 40 ILCS 5/4-110.1 (Occupational Disease Disability); 40 ILCS 5/4-111 (Not in Duty).

who may testify to the occurrence in question, especially when the request is for “duty-related” pension benefit.

Under the Police Code (3-115), a Board may not approve a disability claim unless the disability is certified by three (3) practicing physicians selected by the Board. The Board may require other evidence of disability. Under the Firefighters’ Code (4-112), the Statute requires that a disability pension shall not be paid until the disability has been established by the Board by examinations of the firefighter at Pension Fund expense by three (3) physicians selected by the Board and such other evidence as the Board deems necessary. The three physicians selected by the Board need not agree as to the existence of any disability or the nature and extent of a disability.

After all evidence has been reviewed and testimony presented, the board may proceed into executive session to deliberate and discuss legal issues presented in the case. The board must render its decision in open session and should prepare a detailed written decision setting forth its findings, its analysis, conclusions and decision. The written decision should be served upon the applicant by certified mail. Each written decision should contain additional information. Once again, boards would be well advised to hire experienced legal counsel to assist them in the processing of claims, particularly disability claims, and the issuance of a written decision.

7. **ILLINOIS DEPARTMENT OF INSURANCE, (FORMERLY KNOWN AS THE ILLINOIS DEPARTMENT OF FINANCIAL & PROFESSIONAL REGULATION)²:**

The Illinois Department of Insurance regulates Police and Firefighter Pension Funds under Articles 3 and 4 of the Illinois Pension Code. The Department has adopted rules and regulations regarding the operation and conduct of these funds. Boards are required to file Annual Statements with the Department (see paragraph 10). The Department provides each fund with an Actuarial Report annually which provides a snapshot of the fund at the close of each fiscal year (see paragraph 11). The Department conducts periodic audits of pension funds to make certain that pension boards are in compliance with all State laws, rules, and regulations. Should the Department determine that violations of the law have occurred, an administrative hearing can take place. The Department can issue sanctions against the pension board or fund

²Effective June 1, 2009 Governor Quinn signed an Executive Order changing the name of the Illinois Department of Financial and Professional Regulation back to the Illinois Department of Insurance.

which can include monetary fines should violations exist.

8. INVESTMENT FUNCTIONS:

Board members would be prudent to do the following in order to meet their fiduciary responsibilities as trustees:

- A. Establish a written Investment Policy and Guidelines which should be reviewed and followed by all investment managers to the fund. This Investment Policy and Guidelines must be filed with the Illinois Department of Insurance within 30 days after it is adopted by the Board;
- B. Select proper investment vehicles;
- C. Make sure all investments are authorized by law. The law provides for specific ways in which funds are required to invest their monies based upon the size of the fund;
- D. Hire competent investment experts which could include investment managers and investment consultants;
- E. Review all investment contracts and Investment Policy and Guidelines with the pension board's attorney;
- F. Make certain all investment managers/advisors/consultants to the fund are making full disclosure of all fees which they are receiving and from all sources;
- G. Note that a Federal District Court ruled on February 23, 2007 that Public Act 97-0079, known as the Sudan Act, is unconstitutional and the provisions of this Act, including prohibited investments and the requirements to certify compliance with the law, are no longer enforceable.

9. FUNDING SOURCES FOR YOUR PENSION FUND:

Downstate Police and Firefighter Pension Funds receive their monies from four (4) sources:

- A. Contributions by participants which are based upon statutory percentages of their salary;
- B. Return on fund investments;
- C. Contributions by the municipality, typically from a tax levy for pension fund purposes (this amount is usually determined by the State Actuarial Report or an independent Actuarial Report obtained by the board or municipality);
- D. Gifts to the Fund.

Trustees should be aware of and monitor these four (4) funding sources to make certain the integrity of the fund is preserved. Failure to receive sufficient funds from all four (4) of these sources will result in an under funding of the fund. State law requires all pension funds to be fully funded by the year 2033.

10. **ANNUAL STATEMENT FILED WITH THE ILLINOIS DEPARTMENT OF INSURANCE:**

Pension boards are required to submit an Annual Statement to the Illinois Department of Insurance within 6 months of the end of the fund's fiscal year. This Annual Statement will include information regarding the fund including information concerning board members, revenues received, expenses paid (pension and benefits, personal services, insurance, professional services, investment expenses, electronic data processing, equipment, and other expenses), assets (investments, receivables, liabilities). The Annual Statement must be filed with the Illinois Department of Insurance electronically. Once accepted, the Department will forward interrogatories (questions) which must be answered by the board trustees concerning the management of the fund, investments of the fund, as well as actuarial information. A certification form must also be submitted to the Department to conclude the annual reporting process. Every trustee should be familiar with the information contained in the Annual Statement and interrogatories as part of their fiduciary responsibilities.

11. **STATE ACTUARIAL REPORT:**

One of the most important responsibilities as a trustee of a police or firefighter pension fund is for you to be familiar with and review the State actuarial report which is produced on an annual basis by the Illinois Department of Insurance. This actuarial report is produced based upon information which is provided by the pension board in its annual statement and other information which is available to the Department. Part of the information which is generated in this report includes information on the amount your fund is under funded as well as the recommended funding level from the municipality. State law requires all pension funds to be fully funded by the year 2033. Trustees are required to review this information and submit a written request to the municipality for funding (typically through a tax levy) on an annual basis. A pension fund trustee has a fiduciary duty to see that contributions are properly made by the municipality. Trustees are under a statutory duty to investigate any possibility of under funding as it relates to the fund.

12. **MAINTAINING RECORDS BY BOARD MEMBERS:**

Each board member should maintain a three ring binder which contains information important to board members such as agendas, minutes, treasurer's report, investment analysis/reports, legal counsel correspondence, Department Financial and Professional Regulation correspondence, IPPFA correspondence, general correspondence, and information from your CPA, including audits. This will assist board members in carrying out their fiduciary duties in keeping track of board activities.

13. **REVIEW OF VENDOR CONTRACTS:**

The board should review, on an annual basis, all contracts for representatives who provide services to the board. These would include contracts with investors, board attorney, certified public accountant, and board administrator/clerk, if any. Trustees would be wise to hire professionals who have experience and expertise in their respective professions to provide the fund with maximum benefits. Periodically you should obtain bid proposals from other vendors to compare services, pricing and expertise.

14. **PUBLIC ACT 95-950 (EFFECTIVE AUGUST 29, 2008):**

The following is a summary of some of the major points contained in this legislation. Board members and investors should be encouraged to read the entire Public Act to become fully informed as to all of the provisions of this Act.

A. **Penalties for Fiduciaries:** A fiduciary of a Police or Fire Pension Fund shall not knowingly cause or advise the pension fund to engage in an investment transaction when the fiduciary has any direct interest in the income, gains, or profits of the investment advisor through which the investment transaction is made or has a business relationship with that investment advisor that would result in pecuniary benefit to the fiduciary as a result of the investment. VIOLATION IS A CLASS 4 FELONY.

B. **Limitations for Consulting Contracts:** A person or entity that provides consulting services to a pension fund with respect to the selection of fiduciaries may not be awarded a contract to provide consulting services for more than 5 years in duration. The contract to provide consulting services may not be extended or renewed. The contractor shall be eligible to compete for a new contract. No person shall attempt to avoid or contravene the

restrictions of this subsection by any means. NOTE: THIS PROVISION WILL REQUIRE YOUR BOARD TO EXAMINE IT'S RELATIONSHIP WITH ALL INVESTORS WHO DO BUSINESS WITH THE PENSION FUND TO VERIFY COMPLIANCE WITH THIS PROVISION.

C. **Requirements for Consultants:** A consultant who is neither a pension fund board member or employee to be one of the following on or after July 1, 2008: a registered investment advisor under the Federal Investment Advisors Act of 1940; a registered investment advisor under the Illinois Securities Law of 1953; or an insurance company.

D. **Disclosure of Fees by Investment Advisors and Consultants:** All contracts for investment services to fully disclose all direct and indirect fees, commissions, penalties, and other forms of compensation, including reimbursement for expenses that may be paid by or on behalf of the investment advisor or consultant in connection with the provision of investment services. Within 30 days of the effective date (August 29, 2008) of this legislation all current advisors and consultants must disclose to the board of trustees all direct and indirect fees, commission, penalties, and other compensation paid by or on behalf of the investment advisor or consultant in connection with the provision of investment services. NOTE: THIS PROVISION WILL REQUIRE YOUR BOARD TO EXAMINE IT'S RELATIONSHIP WITH ALL INVESTORS WHO DO BUSINESS WITH THE PENSION FUND TO VERIFY COMPLIANCE WITH THIS PROVISION.

E. **Prohibition of Gifts**³: Board members of Downstate Police and Fire Pension funds are prohibited from accepting or soliciting gifts from "prohibited sources." The Act defines a prohibited source as a person who is seeking official action by the board of trustees of the pension fund or has interests that may be substantially affected by the performance or non-performance of the official duties of the board member or employee. VIOLATION IS A CLASS A MISDEMEANOR.

F. **Examination and Investigations:** The Illinois Department of Insurance is required to conduct examinations of Article 3 and Article 4 pension funds every 3 years.

³These provisions were modified with Public Act 96-006, which was effective April 3, 2009

G. **Review of Award of Benefits:** The municipal treasurer shall have the ability to review the total amount of the annuity paid by the pension fund and all information used by the fund in the calculation of the benefit. The board shall review the Treasurer's findings with respect to the accuracy of the benefit calculation and if the board discovers that an error exists it shall recalculate the annuity so that it conforms with the pension code.

H. **Annual Report by Pension Boards to Municipality:** Police and Fire Pension Boards are required to provide annual reports to their municipality which includes information on assumed investment return and actual investment return, total net assets of the fund, the number of total active employees participating in the fund, the number of participants receiving benefits from the fund during its most recently completed fiscal year. This information must be compared to the total net income, assumed investment return, and actual investment return received during the preceding fiscal year. The Act allows municipalities to publish the report in its entirety in a newspaper of general circulation in the municipality or on the municipality's website.

I. **Anti-fraud Provisions:** Any member, trustee, or employee of a downstate police or fire pension fund who knowingly makes a false statement or falsifies any record of a pension fund in an attempt to defraud the fund shall be guilty of a CLASS A MISDEMEANOR.

J. **Report on Fiscal Status of Police and Fire Pensions:** The Commission on Government Forecasting and Accountability is required to analyze data submitted by the Illinois Department of Insurance. The Commission is required to issue a formal report during odd numbered years analyzing the fiscal status of Downstate Police and Fire Pension Funds.

K. **Prohibition on Transfers from Public Pension Regulation Fund:** The Public Pension Regulation Fund is an appropriated fund that was established to receive and record all monies collected by the Illinois Department of Insurance. This Act prohibits transfers from the Public Pension Regulation Fund to the professions indirect cost fund.

L. **Pension Impact Notes for Downstate Police and Fire Funds:** The Pension Impact Note Act stipulates that a pension impact note for any legislation or amendment that the Commission on Government Forecasting and Accountability determines would result in an increase in benefits or

increased costs to a Downstate Police or Fire Pension Fund may demonstrate the fiscal impact of the legislation on selected individual municipalities with such pension funds.

15. **NEW LEGISLATION: P.A. 96-006 (EFFECTIVE APRIL 3, 2009):**

The following is a summary of some of the major points contained in this new law. Board members and Investors are encouraged to read the entire Public Act to become fully informed as to all of the provisions of this Act.

- A. **MANDATORY EDUCATIONAL TRAINING:** Effective April 3, 2009, Public Act 96-006 mandates that Trustees of Article 3 and Article 4 Pension Funds are required to participate in a minimum of eight (8) hours of certified trustee education programs per year on the topics of ethics, fiduciary duty, and investments, along with other topics related to your duties as trustees. Each board shall annually certify its' members compliance by submitting an annual certification to the Division of Insurance of the Illinois Department of Insurance.
- B. **STATEMENTS OF ECONOMIC INTEREST:** Members of the Pension Board are now required to file verified written statements of economic interest which are similar to those currently required of public officials.
- C. **GIFT BAN REVISIONS:** This new law places revisions on Public Act 95-950 which became law in August, 2008.
- D. **INVESTMENT ADVISORS/CONSULTANTS:** This law requires all investment advisors to pension boards to issue a new fee disclosure letter to each board within 30 days of the new law. All investors to boards must have written contracts and be fiduciaries and must sign a fiduciary acknowledgment.
- E. **STATE TREASURER'S WORKING GROUP:** The State Treasurer's office is to establish a working group to review the investment performance and costs of all investment managers and consultants to your pension fund. This working group is required to make public recommendations prior to January 1, 2011.

16. **PUBLIC ACT 96-0429, A/K/A SENATE BILL 1974 (EFFECTIVE AUGUST 13, 2009):**

On August 13, 2009 Governor Pat Quinn signed into law Senate Bill 1974, which is now known as Public Act 96-429. This new law mandates additional trustee educational requirements. All elected and appointed trustees under Article 3 and 4 of the Pension Code must participate in a minimum of 16 hours of continuing trustee education each year after the first year that the trustee is elected or appointed. Any required training shall be paid by the pension fund. Any board member who does not timely complete the training is not eligible to serve on the board of trustees unless the board member completes the missed training within six months after the date the member failed to complete the required training. In the event a board member fails to complete the required training, a successor shall be appointed or elected, as applicable, for the unexpired term. The elected or appointed trustees who are police officers or firefighters or employed by a municipality shall be permitted time away from their duties to attend such training without reduction of accrued leave or benefit time.

All newly elected and appointed trustees under Article 3 and 4 must participate in mandatory certification training that consists of at least 32 hours of initial trustee certification training at a facility that is accredited and affiliated with a State of Illinois certified college or university. The IPPFA currently offers such a program. Active or appointed trustees serving on the effective date of this new law (August 13, 2009) shall not be required to attend the 32 hour certification training.

17. **NEW LEGISLATION: P.A. 096-0542 (EFFECTIVE JANUARY 1, 2010):**

This Act amends, in part, the Open Meetings Act (OMA) by adding Section 1.05 requiring that every public body shall designate employees, officers, or members to receive training on compliance with this Act. Each public body shall submit a list of designated employees, officers, or members to a Public Access Counselor and by July 1, 2010 these individuals must successfully complete an electronic training curriculum created by the Public Access Counselor. This training must then be completed on an annual basis. New members which are appointed to the public body must successfully complete the electronic training curriculum within 30 days after their membership to the board. This Act also amends the Illinois Freedom of Information Act (FOIA) requiring all public bodies to name an FOIA Officer. The FOIA Officer is responsible for responding to FOIA requests. All FOIA Officers must complete an on-line training program provided by the Attorney General's Public Access Counselor. Trustees can obtain information regarding the mandatory training for the OMA and FOIA by visiting the Illinois Attorney General's website at www.illinoisattorneygeneral.gov