First, a letter from former Illinois Appellate Court justice **Gino DiVito**

To Whom It May Concern

April 13, 2010

The March 10, 2010 Tribune Op-Ed ***Don't Call this Pension Reform*** by R. Eden Martin of the Civic Committee of the Commercial Club of Chicago and the March 27, 2010 Tribune Editorial, ***Yes You Can*** claim that Governor Quinn and the General Assembly should have gone further in bringing pension reform to Illinois by reducing the pensions not only of new employees, but of existing employees as well. My colleague, John Fitzgerald, and I have looked closely at this important State issue, and our conclusion is inescapable – as a matter of law, the pension rights of current employees simply cannot be diminished as Mr. Martin and the Tribune contend. (Our legal analysis is below)

The plain language of the Illinois Constitution's Pension Protection Clause (Article XIII, Section 5) states that, "*Membership in any pension or retirement system of the State . . shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired."*

As courts in this State have confirmed, this language is crystal clear. Public employees become members of a pension system at the time of hire or shortly thereafter and once they become members, their pension rights are set and cannot be "diminished or impaired."

This is exactly what the framers of the State's 1970 Constitution intended. At the Constitutional Convention, one of the co-sponsors of the Pension Protection Clause succinctly illustrated the point: "Benefits not being diminished really refers to this situation: If a police officer accepted employment under a provision where he was entitled to retire at two-thirds of his salary after twenty years of service, that could not subsequently be changed to say he was entitled to only one-third of his salary after thirty years of service, or perhaps entitled to nothing." Not surprisingly, as it noted in a 1996 decision *McNamee v. State of Illinois* , the Illinois Supreme Court has "consistently invalidated amendments to the Pension Code where the result is to diminish benefits" to which State employees acquired a vested right when they entered the pension system. Legal analysis that Sidley Austin LLP performed for the Civic Committee glosses over this controlling authority, misconstrues a comment that the Illinois Supreme Court made in a 1974 decision (which has been distinguished in subsequent cases), and incorrectly relies on a 1979 Illinois Attorney General opinion that has been trumped by subsequent Illinois Supreme Court decisions.

Any pension reform effort will depend on the strength of its legal foundation. The Governor and the General Assembly have been careful to comply with the Illinois Constitution's Pension Protection Clause, as well they should. The alternative would be a short-lived pension reform that is invalidated by court order after protracted litigation, which would be a disservice to the taxpayers.

Next, Divito's legal analysis in the form of a memorandum:

MEMORANDUM

To: Hon. Pat Quinn, Governor of the State of Illinois

Theodore T. Chung, General Counsel, Office of the Governor

From: Gino L. DiVito John Fitzgerald

Re: Diminution of Pension Benefits for Current Employees

Date: April 12, 2010

Executive Summary

The Pension Protection Clause of the Illinois Constitution of 1970 (Article XIII, § 5) prohibits the State from diminishing or impairing the pension benefits of current State and other public employees. Contrary analysis provided by the law firm Sidley Austin LLP lacks legal merit and is squarely contradicted by controlling case law.[1]

Analysis

1. **Text of the Pension Protection Clause**

Article XIII, § 5 of the Illinois Constitution of 1970, commonly known as the "Pension Protection Clause," states as follows:

> PENSION AND RETIREMENT RIGHTS
>
> Membership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.

1. **History of the Pension Protection Clause**

"When discerning the purpose of constitutional provisions, the Illinois Supreme Court has attached great weight to the Record of Proceedings of the Constitutional Convention." *Vill. of Sherman v. Vill. of Williamsville*, 106 Ill. App. 3d 174, 178 (4th Dist. 1982). Accordingly, this analysis of the Pension Protection Clause will begin with available evidence of its purpose from the Constitutional Convention's Record of Proceedings.

At the Constitutional Convention, one of the co-sponsors of the Pension Protection Clause explained its purpose as follows:

> MRS. KINNEY: Yes, you are right, Mr. Lyons. That is what it is designed to do. Benefits not being diminished really refers to this situation: If a police officer accepted employment under a provision where he was entitled to retire at two-thirds of his salary after twenty years of service, that could not subsequently be changed to say he was entitled to only one-third of his salary after thirty years of service, or perhaps entitled to nothing. That is the thrust of the word "diminished." . . . It is simply to give them a

> basic protection against abolishing their rights completely or changing the terms of their rights after they have embarked upon the employment ─ to lessen them.

See Record of Proceedings, Sixth Illinois Constitutional Convention, Daily Journals, Verbatim Transcript of July 21, 1970, at 2929. This demonstrates that the Pension Protection Clause prohibits any diminishment in a State employee's pension rights at any time after the State employee has "accepted employment" with the State. Pension rights are fixed as of the time the State employee has "embarked upon the employment."

Another co-sponsor, Mr. Green, likewise explained:

> What we are trying to merely say is that if you mandate the public employees in the state of Illinois to put in their 5 percent or 8 percent or whatever it may be monthly, and you say when you employ these people, "Now, if you do this, when you reach sixty-five, you will receive $287 a month," that is, in fact, is what you will get.

See id. at 2931.

Mrs. Kinney was even more emphatic on this point later in the debate:

> The thrust of it is that people who do accept employment will not find at a future time that they are not entitled to the benefits they thought they were when they accepted the employment. . . . All we are seeking to do is to guarantee that people will have the rights that were in force at the time they entered into the agreement to become an employee, and as Mr. Green has said, if the benefits are $100 a month in 1971, they should not be less than $100 a month in 1990.

See id. at 2931-32. In short, the Pension Protection Clause was clearly intended to prohibit precisely the scenario suggested by the Sidley Austin memorandum: that a State employee's pension rights could be diminished at some point after he enters State employment. Under the Pension Protection Clause, a State employee's pension benefits can never be less than what they were when he entered State employment.

The Sidley Austin memorandum does not discuss these statements by the co-sponsors of the Pension Protection Clause. The Attorney General's Opinion cited in the Sidley Austin memorandum, however, acknowledged that one of Mrs. Kinney's above-quoted statements "seems to imply that any change reducing benefits can take effect only as to persons who enter State employment after the date of the change." *See* Atty. Gen. Op. No. S-1407 (Jan. 10, 1979), at p. 7.

1. **Case Law Interpreting the Pension Protection Clause**

The Sidley Austin memorandum, as well as the Attorney General's Opinion on which it relies, primarily rests upon *dicta* from an early case interpreting the Pension Protection Clause, *Peters v. City of Springfield*, 57 Ill.2d 142, 152 (1974). In *Peters*, the Illinois Supreme Court observed

that the Pension Protection Clause was intended "to insure that pension rights of public employees which had been earned should not be 'diminished or impaired' . . . ." *Id*. The Sidley Austin memorandum focuses on the word "earned" and assumes that the Pension Protection Clause does not apply to pension benefits that a current State employee "may earn in the future," apparently on the theory that a State employee has not earned all of his pension rights until retirement. This analysis suffers from multiple fatal flaws.

A. The statement upon which the Sidley Austin memorandum relies is ***dicta.***

First, as mentioned above, the above-quoted statement from *Peters* was *dicta*. In *Peters*, the Illinois Supreme Court was asked to decide merely whether the Pension Protection Clause permitted a municipality to reduce its mandatory retirement age for policemen and firemen. *See id.* at 143-44. The *Peters* court made no distinction, and was not asked to make any distinction, between earned and unearned pension benefits. Nor did the *Peters* court decide or even suggest *when* a State employee earns his pension benefits, or when he earns the right to have his pension benefits calculated in a certain way.

- 1. **A current State employee has a vested right to have his pension payments calculated in accordance with the law that was in effect when he entered the pension system.**

Second, as hinted in the preceding sentence, the Sidley Austin memorandum asks the wrong question. A current State employee obviously has not yet earned his pension, in the sense that he must wait until retirement before receiving pension payments, and also in the sense that his pension will eventually be determined by his length of service, which has not yet run its course. The relevant question, however, is: When does a State employee earn the right to have his future pension payments calculated in a certain way? That question has already been answered by numerous Illinois cases: The employee's right to have his pension benefits calculated in a certain way vests (or, put another way, is earned) when he enters the retirement system.

"Vesting of an employee's rights in the system occurs either at the time the employee entered the system or in 1971, when the Constitution became effective, whichever is later." *Carr v. Bd. of Trustees of Police Pension Fund of Peoria*, 158 Ill. App. 3d 7, 8 (3d Dist. 1987); *see also Schroeder v. Morton Grove Police Pension Bd.*, 219 Ill. App. 3d 697, 700 (1st Dist. 1991) ("An employee's rights in the system vest, either at the time he enters the system, *e.g.*, making contributions, or in 1971 when the 1970 Constitution became effective, whichever is later"); *Hannigan v. Hoffmeister*, 240 Ill. App. 3d 1065, 1073 (1st Dist. 1992) ("Pension rights vest when a person enters the pension system by making contributions or when the Illinois Constitution of 1970 became effective in 1971, whichever is later"); *Barber v. Bd. of Trustees of Vill. of S. Barrington Police Pension Fund*, 256 Ill. App. 3d 814, 820 (1st Dist. 1993) (same, quoting *Carr*, 158 Ill. App. 3d at 8).

The term "vesting," in this context, "refers to a contractual right to and interest in a pension that may be upheld at law." *See Kraus v. Bd. of Trustees of Police Pension Fund of Vill. of Niles*, 72 Ill. App. 3d 833, 836 (1st Dist. 1979). When a State employee's pension rights vest, they become "constitutionally protected contractual rights under article XIII, section 5." *Barber*, 256 Ill. App. 3d at 820.

Because of this, the "law existing at the time of vesting is incorporated into the [employee's] agreement." *Carr*, 158 Ill. App. 3d at 8; *see also Gualano v. City of Des Plaines*, 139 Ill. App. 3d 456, 458 (1st Dist. 1985); *Schroeder*, 219 Ill. App. 3d at 700 ("The law which exists at the time of the contract formation is deemed to be a part of the contract as though it was expressly referred to or incorporated into it"); *Hannigan*, 240 Ill. App. 3d at 1073 ("[T]he plaintiff's pension became vested on July 1, 1971. . . . Consequently, the law which existed in 1971 controls the interpretation of the agreement in this case").

Accordingly, after the effective date of the Constitution of 1970, a State employee's pension rights are "governed by the actual terms of the Pension Code at the time the employee becomes a member of the pension system." *Di Falco v. Bd. of Trustees of Firemen's Pension Fund of Wood Dale Fire Protection Dist. No. 1*, 122 Ill.2d 22, 26 (1988); *see also McNamee v. State*, 173 Ill.2d 433, 439 (1996) (same); *People ex rel. Sklodowski v. State*, 182 Ill.2d 220, 229 (1998) (same).

In other words, when a State employee enters the retirement system (*i.e.*, when he is hired and begins making contributions), he earns a constitutionally protected right to have his future pension payments calculated in accordance with the law that existed when he entered the system. If a State employee was hired and began contributing to the retirement system in 1980, and if he were to retire in 2020, his pension benefits would be calculated in accordance with the law that was in effect in 1980 and, as noted below, by taking into account any enhancements to those benefits. His pension benefits could not be *diminished* by any amendment enacted after he entered the system in 1980.

In a curious attempt to distinguish the applicable case law, the Sidley Austin memorandum argues that State employees who successfully sued to invalidate diminishments of their pension benefits on the basis of the Pension Protection Clause had earned those benefits "in the past." (In a footnote, the memorandum likewise asserts that the applicable case law discusses benefits that had "already accrued for the employee's prior service . . . .") This misses the point. As demonstrated by the cases cited above, all State employees have earned a vested right to have their pension benefits calculated in accordance with the law as it existed when they entered the system. All current State employees have earned that right "in the past."

- 1. **Illinois courts have already considered and explicitly rejected the same arguments that the Sidley Austin memorandum makes now.**

Third, in a series of cases postdating the Attorney General's Opinion on which the Sidley Austin memorandum relies, the Illinois Supreme Court and the Illinois Appellate Court have "consistently invalidated amendments to the Pension Code where the result is to diminish benefits." *See McNamee v. State of Illinois*, 173 Ill.2d 433, 445 (1996) (collecting cases). These cases squarely contradict the analysis in the Sidley Austin memorandum.

The first such decision was *Kraus v. Bd. of Trustees of Police Pension Fund of Vill. of Niles*, 72 Ill. App. 3d 833 (1st Dist. 1979). In *Kraus*, the appellate court was asked to decide "whether the trial court erred in holding that under section 5 of article XIII of the 1970 Illinois Constitution, plaintiff was entitled to receive a pension based on a section of the Pension Code in effect at the time of his entry into the pension system and at the time the constitutional provision became effective, although the section was subsequently repealed and replaced prior to the time plaintiff retired or became eligible to retire." *Id*. at 834-35. Like the Sidley Austin memorandum, the

defendant in that case argued "that the legislature has the power, as necessity requires, to enact Pension Code modifications which directly diminish the benefits to be received by preexisting members of the pension system, so long as they do not affect the rights of those who are already eligible to retire or have retired." *Id*. at 836.

In affirming the trial court, the Illinois Appellate Court rejected that argument and held that "a Pension Code modification changing the basis upon which pension benefits are directly determined cannot be applied to diminish the benefits of those who became members of the system prior to the statute's effective date." *See Kraus*, 72 Ill. App. 3d at 850 (emphasis added). This holding unambiguously forecloses the analysis in the Sidley Austin memorandum.

The *Kraus* court also explicitly rejected the notion that the reference to "earned" benefits in *Peters* somehow created a distinction between earned and unearned (or accrued and unaccrued) pension benefits: "To imply a requirement that those benefits have fully accrued in this context would, in our opinion, be an unwarranted judicial engraftment on the constitutional provision and would frustrate the express intent of its drafters." *Id*. at 848 (discussing *Peters*). Therefore, the Illinois Appellate Court in 1979 rejected exactly the same distinction on which the Sidley Austin memorandum is based.

The Illinois Supreme Court has since adopted the holding of *Kraus*. *See Felt v. Bd. of Trustees of Judges Retirement System*, 107 Ill.2d 158, 168 (1985) (holding that an amendment to the Illinois Pension Code "is unconstitutional as applied to these plaintiffs and to other judges in service on or before the effective date of the amendment" pursuant to the Pension Protection Clause); *Buddell v. Bd. of Trustees, State Univ. Retirement System of Ill.*, 118 Ill.2d 99, 104-07 (1987) (holding that an amendment to the Illinois Pension Code was unconstitutional as applied to the plaintiff, who became a participant in the retirement system before a new deadline was set by the amendment, and noting that *Kraus* "is in accord with our holding in this case"). The same rule was applied in *Miller v. Retirement Bd. of Policemen's Annuity & Benefit Fund of City of Chicago*, 329 Ill. App. 3d 589, 600 (1st Dist. 2001), *modified upon denial of rehearing* (May 20, 2002) ("In our view, like *Kraus* and *Felt*, the application of the amendment to plaintiffs amounted to a change in the terms of their contract with the pension system and directly diminished their benefits under the contract").

The lesson of *Kraus*, *Felt*, *Buddell* and *Miller* is clear: A State employee's pension must be calculated in accordance with the law in effect when the State employee was hired and entered the pension system. Any attempt to unilaterally diminish the State employee's pension after he is hired and enters the system would violate the Pension Protection Clause.

1. **Continued employment is not adequate consideration for a diminishment of pension benefits.**

The Sidley Austin memorandum discusses the possibility that, in its view, a current State employee's pension benefits could be diminished if the employee agrees to the diminishment in exchange for consideration. Without citation to any authority, the Sidley Austin memorandum asserts that "the consideration for a prospective reduction in benefits would be the State's agreement to continue employing the employee." If the State could diminish a current State employee's pension benefits unilaterally merely by continuing to employ that person for any length of time (even a single day), then the Pension Protection Clause would mean very little. Moreover, "our courts have determined that mere continued employment, standing alone, does not constitute consideration supporting the unilateral modification of an existing employment

contract." *Ross v. May Co.*, 377 Ill. App. 3d 387, 392 (1st Dist. 2007) (*citing Doyle v. Holy Cross Hosp.*, 186 Ill.2d 104, 113-14 (1999)). Accordingly, the Sidley Austin memorandum's assertion is squarely contradicted by settled Illinois law.

The Sidley Austin memorandum also overlooks the fact that civil service laws and collective bargaining agreements may prohibit the State from terminating certain State employees except for cause. The continued employment of such individuals would not constitute valid consideration for a unilateral diminishment of those individuals' pension benefits, since the State is already obligated to continue their employment absent cause for termination.

1. **State employees have a vested right to pension enhancements that were implemented during their employment.**

As discussed above, the Pension Protection Clause prohibits the State from diminishing the pension benefits that existed as of a State employee's entry into the pension system. The Pension Protection Clause, however, was not intended to prevent enhancements to pension benefits. *See* Record of Proceedings, Sixth Illinois Constitutional Convention, Daily Journals, Verbatim Transcript of July 21, 1970, at 2929 (Mrs. Kinney: "As I said before, it is also not intended to preclude greater benefits for beneficiaries, pensioners, or their dependents at some future time").

Illinois courts have further held that, if a State employee's pension benefits are enhanced at some point during his employment, the employee acquires a vested right to that enhancement by virtue of having contributed to the pension system after the enhancement was implemented (thus effecting a modification of the contract). Under the Pension Protection Clause, the enhancement cannot be taken away from the State employee, even if it did not exist when the employee first entered the pension system. As the appellate court explained in *Taft v. Bd. of Trustees of Police Pension Fund of Vill. of Winthrop Harbor*, 133 Ill. App. 3d 566, 572 (2d Dist. 1985):

> In the instant case, plaintiff continued to contribute to his pension fund following the repeal of the reduction provision of the Workers' Compensation Act. Consequently, his contractual rights regarding his pension benefits increased. This modification constitutes the vesting of additional rights.

See also Gualano v. City of Des Plaines, 139 Ill. App. 3d 456, 458-60 (1st Dist. 1985); *Schroeder v. Morton Grove Police Pension Bd.*, 219 Ill. App. 3d 697, 700-02 (1st Dist. 1991); *Carr v. Bd. of Trustees of Police Pension Fund of Peoria*, 158 Ill. App. 3d 7, 8-10 (3d Dist. 1987); *Miller v. Retirement Bd. of Policemen's Annuity & Benefit Fund of City of Chicago*, 329 Ill. App. 3d 589, 597-602 (1st Dist. 2001), *modified upon denial of rehearing* (May 20, 2002).

An early Illinois Appellate Court decision reached a contrary conclusion (*Sellards v. Bd. of Trustees of Rolling Meadows Firemen's Pension Fund*, 133 Ill. App. 3d 415 (1st Dist. 1985)), but has been superseded by subsequent decisions of the appellate court, including decisions within the same appellate district. *See Gualano* , 139 Ill. App. 3d at 458-60; *Schroeder*, 219 Ill. App. 3d at 700-02; Miller, ;329 Ill. App. 3d at 597-602.

Conclusion

The Pension Protection Clause of the Illinois Constitution of 1970 (Article XIII, § 5) prohibits the State from diminishing the pension benefits of current State employees. The distinction that the Sidley Austin memorandum attempts to draw between earned and unearned pension benefits has no basis in law, and in fact is precluded by the controlling case law