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Great Rivers of Spending:

The Legal Tributaries of Municipal Fire and Police Pensions

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To be an Illinois legislator creating great outpourings of benefits targeted to your supporters, accounting or actuarial competence is not required. To be an Illinois municipality charged by law with funding police and fire pensions, however, does require financial competence, and the ability to read the map of Illinois pension spending in some detail. Like the great cartographers of the past, we lawyers can share the excitement of measuring the actual locations of the tributary statutory language forming the rivers of debt now engulfing municipal budgets everywhere in Illinois.

We start with the Illinois constitution, which says that no matter what prior majorities of the Illinois General Assembly did with their math, the resulting spending mandates are for all practical purposes infallible, and may not be reversed, revised, or reduced in any way.¹ This is good news for those legislators who shied away from math in school, but still wanted to make laws about the complexities of pensions.² And interestingly, the Illinois Supreme Court has now confirmed that the Illinois Constitutional Convention of 1970 prohibits us from correcting any such bad math. Legislatively enacted pensions, as a result, can never be corrected – just paid for.

The financial expression of decades of legislative effort in the municipal pension area has become devastating.³ At the state level, Illinois owes at least \$104.6 billion to its pension plans. Accusations of underfunding go back and forth at the state level. However, in the realm of municipal fire and police pensions for the over 6,994 units of local government in Illinois,⁴ there has not been state *underfunding*, because the state *never has funded* these municipal pensions. 1,299 of these governmental units are municipalities.⁵ Police and fire pensions are funded by payroll deductions (which are capped at 9.91 percent of payroll for police, and 9.455 percent for fire) and by general municipal revenue fund contributions (which are *not* capped).

In the recent Illinois State pension litigation, Justice Karmeier, writing for a unanimous court,⁶ analyzed the attempt of the Illinois General Assembly to reduce some benefits under four of Illinois's five state-funded pension systems. The court held that article XIII, section 5 of the Illinois Constitution of 1970⁷ protects any increased pension benefits from ever being decreased by normal legislation; and that no benefit reductions may be made except by amending the Illinois Constitution. Here is what article XIII, section 5 says:

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.

The two ways to change this section of our Illinois Constitution are: (i) a Constitutional convention called by a 3/5 vote of each house of the General Assembly,⁸ or (ii) an Amendment to article XIII, section 5 proposed by a 3/5 vote of each house of the General Assembly, and then submitted for ratification to the people of Illinois in the next general election, who must approve it by "either three-fifths of those voting on the question or a majority of those voting in the election."⁹ There is no possibility of a citizen-initiated petition that could bypass the need to get a 3/5 vote of the General Assembly to start reform rolling.

1. The use of an analogous power in the Roman Catholic Church is known as speaking *ex cathedra*, by unchangeable, infallible decree. See generally, https://en.wikipedia.org/wiki/Papal_infallibility. In the political realm, having a resort to permanence is a key feature of constitutional government, helping our legislators in Illinois to "control themselves" with the disciplinary aid of the judicial system if necessary. See *In re Pension Reform Litigation*, 2015 IL 118585 at ¶89 ("Obliging the government to control itself is what we are called upon to do today.").

2. Backing up this observation, Peter Chan, formerly with the U.S. Securities and Exchange Commission (SEC) office of municipal securities and public pensions unit in Chicago, has observed "I sometimes wonder whether people actually understood the math" (quoted in *Crains*, fn. 3 *infra*).

3. See generally, McKinney, "The Illinois Pension Disaster: What Went Wrong?" *Crain's Chicago Business* (August 10, 2015).

4. U.S. Census, www2.census.gov/govs/cog/2007/il.pdf.

5. *Id.*

6. *In re Pension Reform Litigation*, 2015 IL 118585.

7. Ill. Const. 1970, art. XII, Sec. 5.

8. Ill. Const. 1970, art. XIV, Sec. 1.

9. Ill. Const. 1970, art. XIV, Sec. 2.

In this context, with such a restricted means of reducing any benefits of "any unit of local government," it is worth reviewing what the current majority of the Illinois General Assembly has since 1993 designed into legislation beginning with the defined benefit plans imposed on Illinois municipalities for police¹⁰ and fire¹¹ employees, dramatically increasing the cost of local municipal fire and police pension benefits in Illinois. It is worth noting here that any form of defined contribution plan such as a SIMPLE IRA or 401(k) plan commonly found in the private sector is not permitted for police and fire employee benefit plans.

These are the spending tributaries that the General Assembly is not allowed to reduce, slow, or in any way control by normal legislative adjustment, but solely by means of a Constitutional amendment. The General Assembly knew of this one-way spending valve in our Constitution when it passed the laws that have created a flood of pension benefits for municipal police and fire fighters. Here is a list of the laws they passed, to quantify and pass "downstream" to each municipality in Illinois.


Year	Act	Current Statute	Effect
1993	87-1265	40 ILCS 5/7-139.7 40 ILCS 5/3-121	Increased pension benefits for firefighters and surviving spouses. Added 1.535% of payroll as city cost. ¹²
1993	87-1265	Same	Granted 3% compound cost of living adjustments. Added 1.65% of payroll as city cost.
1997	90-0032	40 ILCS 5/4-109, Sec. 4-109.1(c-1)	Additional dependent children benefits. Added .002% of payroll as city cost.
1999	91-0466	40 ILCS 5/3-113.1, Sec. 3-113.1 (a)-(d) 40 ILCS 5/4-109, Sec. 4-109(a)	Increased pensions, COLAs, disability and dependent benefits. Added 1.306% of payroll as city cost.
2000	91-0939	40 ILCS 5/3-110, Sec. 3-110(a-5) 40 ILCS 5/3-111, Sec. 3-111(a) and (a-5) 40 ILCS 5/3-112, Sec. 3-112(e)	More police benefits same as firefighter 1999 increases. Added 1.306% of payroll as city cost.

10. 40 ILCS 5/3-301, Sec. 3-101 *et seq.*

11. 40 ILCS 5/4-101, Sec. 4-101 *et seq.*

12. The source for the payroll-costing increments for selected statutes as shown is the Illinois Municipal League (IML) "Historical Public Safety Pension Enactments," at www.iml.org/page.cfm?key=3536.

About the Author



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ARTICLES

Year	Act	Current Statute	Effect
2001	92-0003	820 ILCS 315/3, Sec. 3	Line of duty death benefit increase from 100,000 to 118,000 and 3% annually thereafter
2002	92-0609	820 ILCS 315/3, Sec. 3 40 ILCS 5/8-137, Sec. 8-137(a-5)	Line of duty death benefit increase from 118,000 to 259,038 plus COLA from 2003 in perpetuity.
2003	93-0569	820 ILCS 320/3, Sec. 3	Public Safety Employee Benefits Act (PSEBA) health care insurance for life at sole cost of city for line of service disabled employees.
2004	93-0689	40 ILCS 5/4108.4, Sec. 4-108.4(a)-(c)	Increased depended firefighter benefits and allows IMRF benefit transfers to fire funds. Added 4.63% of payroll as city cost.
2005	94-0317	40 ILCS 5/4-121, Sec. 4-121 40 ILCS 5/3-128, Sec. 3-128	Fire and police take majority voting control (3-2) of all municipal pension boards to invest funds, set assumptions, and rule on disability applications of their fellow officers.
2007	94-0316	50 ILCS 135/12, Sec. 12	Firefighters can serve on municipal boards employing them, and vote on the "employer" side of their collective bargaining contracts and benefits
2007	94-0316	820 ILCS 305/6, Sec. 6(f) 820 ILCS 310/1, Sec. 1(d)	Expand Workers Comp to add presumptions in favor of "duty" determination for certain diseases.
2007	95-0681	40 ILCS 5/4-112, Sec. 4-112	Eliminates any requirement for objective medical opinion for a 3-2 employee-dominated fire pension board to declare a firefighter disabled.
2007	95-0681	30 ILCS 805/8.31, Sec. 8.31	Specifically prohibits a town from seeking state reimbursement for the costs of implementing the unfunded mandate effects of state-ordered municipal pension enhancements.
2009	96-0775	40 ILCS 5/4-109.1, Sec. 4-109.1(f)	3% perpetual COLAs for any firefighter who retired before 7/1/1977.
2009	96-0775	30 ILCS 805/8.33, Sec. 8.33	Prohibits any attempt by any town to seek state reimbursement for the cost of the unfunded retroactive and perpetual 3% COLA increase for firefighters retiring after 7/1/1977.
2013	98-0391	40 ILCS 5/4-114, Sec. 4-114(a)(1) 40 ILCS 5/4-114, Sec. 4-114(b)	Increased benefits for dependent children of firefighters, regardless of firefighter marital status.
2013	98-0391	30 ILCS 805/8.37, Sec. 8.37	Prohibits any attempt by any town to seek state reimbursement for the cost of increased dependent firefighter benefits town must pay.

ARTICLES

Did all of these legislative benefit increases have measurable costs? Did the employee-controlled pension boards do well on their investments? Are police and firefighters living longer? Yes, no, and yes. To make math matters worse, interest rates have been historically low, as anyone with a savings account knows. Low interest rates depress pension fund earnings, since Illinois law dictates that roughly half of police and fire pension funds be invested in interest-bearing instruments.¹³ The downward trend of investment returns, and the upward trend in benefit amounts payable to people and spouses living longer, can be quantified by actuaries. As these reports have been made, they show the extent of unfunded pension payments the municipality must make from general revenues into those pension funds. Each municipality is now, as of 2015, required by the Government Accounting Standards Board (GASB), to prepare its own actuarial report, incorporating the actuarial findings of the police and fire pension boards into the municipality's own budget and comprehensive year-end financial report.¹⁴

For a specific example, we now consider the Village of Oak Brook. Oak Brook contains less than 8,000 residents, and hosts 90,000 visitors each day. 40 police and 28 firefighters protect the public safety of Oak Brook, and three appointees from each department control the police and fire pension boards. In times past, before the General Assembly voted all of the foregoing pension benefit increases, Oak Brook's pensions were over-funded at a 113 percent plus level.

Today, Oak Brook (for its combined fire and police pensions), has an unfunded liability in the amount of \$37,656,600, which is more than 50 percent of Oak Brook's current annual budget. To make regular ongoing payments in addition to the payments required to catch-up on the currently unfunded amount to pay it up to a 90 percent funding level by 2040¹⁵ Oak Brook must pay a total of \$119,624,400. Over the same 25 year period, the fire and police employees from their paychecks must pay \$21,555,800. These payments will cover the unfunded liability plus the ongoing new pension costs going forward for retirement, death benefits, and disability for employees, their dependents and spouses.

“ The financial expression of decades of legislative effort in the municipal pension area has become devastating

Oak Brook's annual payments¹⁶ must go from \$3,339,400 in 2015 up to \$8,031,600 by 2040. Just ten years ago, in 2005, Oak Brook's combined fire and police pension payment was \$1,082,038. And five years ago, that amount was \$1,878,733. Here is the progression:

2005	\$1,082,038
2010	\$1,878,733
2015	\$3,339,400
2040	\$8,031,600

It is not assuring to realize that life expectancies continue to increase; that investment returns continue to be depressed by U.S. federal monetary policy, and that the mandated benefit increases to fire and police pensions continue to swell from their statutory headwaters opened in the 1990s and increased ever since up until 2013.

According to statistics published in the Daily Herald,¹⁷ Oak Brook has the second-strongest balance sheet among all Illinois municipalities, right behind Rosemont. Many Illinois municipalities are in far more severe straits.¹⁸

Academics seek to describe our current predicament, using language like this: ". . . two measures in particular could be

13. See 40 ILCS 5/3-135, Sec. 3-135, requiring investment per 40 ILCS 5/1-113.1 through 1.113.10 (police) and 40 ILCS 5/4-123, Sec. 4-123, requiring investment per a broader reference to the same provisions, specifically 40 ILCS 5/Art. 1 and 40 ILCS 5/Art. 1A.

14. See Statement No. 68, *Accounting and Financial Reporting for Pensions* (GASB).

15. Required by 40 ILCS 5/3-125, Sec. 3-125(a) (police) and 40 ILCS 5/4-118, Sec. 4-118 (a)(fire).

16. All values are taken from the Foster & Foster actuarial modeling report furnished to the Village of Oak Brook and currently used by Village staff and Trustees in making budget allocations.

17. Jake Griffin, "Rauner plan could cost suburbs 25% of reserves," *Daily Herald* (March 5, 2015) (graphic chart included in article).

18. See, e.g., Walsh, "Bad Math and a Coming Public Pension Crisis," *New York Times* (July 8, 2015) (discussing LaGrange, Illinois).

effective in changing the trend of underfunding in American state and local pension plans, and thus producing longer-term sustainability: first, a quicker and less limited recognition of the amortization burden in the contribution rate; and, second, a mitigation of inflation indexation, either by rule or by relating indexation to the funding ratio. However, both measures lead to high transfers of value . . . from current taxpayers to future taxpayers . . . [and] from current and future beneficiaries to taxpayers . . .¹⁹ What they mean is that the pensions are a great cost to future taxpayers, and that to reduce this cost, the current river of fire and police benefits would have to be slowed and reduced. Yet academics can only describe what the Illinois Supreme Court says our Constitution alone prescribes.

Municipal bankruptcy is not currently an option in Illinois, insofar as the Illinois General Assembly has declined to opt in to Chapter 9 of the United States Bankruptcy Code,²⁰ which affords the protections of United States Bankruptcy law to any municipality of a state that has authorized it.²¹ Meanwhile, municipalities unable to fund runaway state-mandated pension benefit increases will wonder how it is that they can go bankrupt. Right now, they won't. First, the State of Illinois will take away the local share of Illinois sale tax receipts, and will pay those receipts directly into the fire and police pension funds, leaving any other municipal spending priorities unpaid.²² The police and fire pension funds can also file suit in equity for a writ of mandamus or the appointment of a receiver to implement increased property taxes on all of the real property in a municipality.²³ Next, municipal assets could conceivably be attached and sold to fund the police and fire funds. Before non-core services like municipal libraries are closed to divert their funding to fire and police pensions, interested residents may wish to check out a copy of Hemingway's *The Sun Also Rises*, for the literary recognition of our problem contained in the dialogue:

"How did you go bankrupt?" Bill asked.

"Two ways," Mike said. "Gradually and then suddenly."²⁴

As we see from this review, the massive and increasing flow of Illinois fire and pension benefits was very carefully planned, and rolls along without constraint, piling up debts downstream faster than many municipalities can pay them. And yet this map of its tributaries is worth keeping, and may someday prove valuable as part of any constitutional effort to recover and protect the municipal assets and taxable private property within each town currently being swamped by this river. □

19. Beetsma, Lekniute and Ponds, "Reforming American Public-Sector Pension Plans: Truth and Consequences," *Rotman Int'l J. of Pension Management*, Vol. 7, Issue 2 (Fall 2014) at 72.

20. 11 U.S.C. Sec. 109(c).

21. Rep. Ron Sandack from Downers Grove has introduced legislation in the Illinois House of Representatives to do exactly that. See House Bill 0298 to amend the Illinois Municipal Code to provide simply that "Any municipality may file a petition and exercise powers pursuant to applicable federal bankruptcy law." 25 States have adopted similar legislation, but Illinois seems poised to let the Sandack bill languish.

22. See 40 ILCS 5/4-118, Sec. 4-118(b-5) for fire, and 40 ILCS 5/3-125, Sec. 3-125 (c) for police. Both provisions require the Illinois Comptroller to divert any state funds the municipality would otherwise receive, and instead pay those monies direct to the police and fire pension funds. This is a new provision that can take effect for the first time in 2016 "and each fiscal year thereafter."

23. The police can do this to enforce 40 ILCS 5/3-125, Sec. 3-125(a); and the fire employees can do this to enforce 40 ILCS 5/4-118, Sec. 4-118(a). Both of these statutes require the city council or trustees of a municipality to levy a tax on all of the real estate in the municipality to meet the annual requirements of the pension funds.

24. Ernest Hemingway, *The Sun Also Rises*, (1926) at 136.