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PENSIONS:
Effect of Pension Code
Revision on Vested Rights

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Michael L. Mory
Executive Secretary
State Employees' Retirement System of Illinois
1201 South Fifth Street
Springfield, Illinois 62706

Dear Mr. Mory:

You have asked for my interpretation of the effect of Public Act 80-841, which completely revised article 14 of the Illinois Pension Code effective January 1, 1978. The new Act, by changing the way in which State employees' compensation is considered for pension calculation purposes, may result in lower pensions for some employees than they would have received otherwise. Your concern is whether these changes may diminish or impair employees' vested rights which are protected by article XIII, section 5 of the Illinois Constitution of 1970.

The new Act makes two sets of changes in the method of considering compensation for pension purposes. The first applies only to State employees who work fewer than fifteen days in an average month and are paid on a per diem basis; the second applies to all State employees.

The pensions of State employees are now calculated on the basis of "final average compensation" (referred to as "average final compensation" in the Illinois Pension Code before the amendments). For full-time employees, this is based on actual monthly pay during four of their last ten years of service, as will be discussed below. Until revised by Public Act 80-841, however, section 14-119 of the Illinois Pension Code (Ill. Rev. Stat. 1975, ch. 108 1/2, par. 14-119) contained a more favorable provision for the computation of average final compensation for part-time per diem employees. Section 14-119 provided in pertinent part as follows:

" * * *

> * * * for any person employed on a per diem basis for an average of fewer than 15 days per month, the average final compensation per month shall be computed by dividing the amount of his earnings during the period of employment for which he received his last 4 years of service credit, by 48, unless that period is longer than 10 years, in which event his average final compensation per month shall be computed by dividing the amount of his earnings during the last 10 years of his period of employment by the number of

> months of service credit received by him for service in those 10 years." (Emphasis added.)

Under the above language, employees were allowed to combine fractional months which they had worked over a period of up to 10 years. The total amount of pay received from the State for those fractional months was then treated for pension purposes as if it had been earned during a contiguous period of four calendar years.

Public Act 80-841 simply deleted this favorable provision for part-time employees paid per diem. Their pensions, like those of full-time State employees, are now to be calculated on the basis of actual earnings during a calendar period of four years. Under the new method of calculation, a per diem employee who earns $50 per day an average of five days per month during the four-year period will have "final average compensation" of $250 per month. This amount is a fraction of what an employee's "average final compensation" could have been under the old provision.

The second change, as noted, applies to all State employees. Under the previous section 14-118 of the Illinois Pension Code (Ill. Rev. Stat. 1975, ch. 108 1/2, par. 14-118), "earnable compensation", on which "average final compensation" was based, consisted only of regular pay and excluded any

overtime pay an employee may have received. New section 14-103.10(b) (Ill. Rev. Stat. 1977, ch. 108 1/2, par. 14-103.10(b)), however, includes overtime pay "[f]or periods of service on and after January 1, 1978" within the definition of "compensation".

In an apparent move to prevent employees eligible for overtime pay from unduly swelling their pensions by doing large amounts of overtime work in the fourth year, the General Assembly limited the amount of compensation paid during the fourth year, which may be considered for pension purposes. Section 14-103.12(a)3 (Ill. Rev. Stat. 1977, ch. 108 1/2, par. 14-103.12(a)3), which contains the limitation, provides as follows:

> " * * * provided that (3) for purposes of a retirement annuity the average compensation for the last 12 months of the 48-month period shall not exceed the final average compensation by more than 25%."

For illustration, if an employee received $9,000 in each of the first, second and third years of the employee's four-year measuring period, and $13,000 the last year, the employee's total pay for the four-year period would be $40,000, and the average thus would be $10,000. But since $13,000 is more than 25 percent above $10,000, not all of the fourth year's pay can be considered for pension purposes.

This change would have raised no constitutional questions if the limitation on the amount of fourth-year pay which can be considered for pension purposes affected only overtime pay. In that case, the General Assembly would simply have put a limitation on what inclusion of overtime in the definition of compensation had granted. The new Act, however, is not so limited. If a State employee happened to receive $9,000 each of the first three years and then was appointed to a $13,000 position the fourth year, the limitation would apply just as much as if the extra money had come from overtime work. Thus, each of the changes described above may cause the amount of some employees' "final average compensation" to be less than it otherwise would have been.

Your questions are as follows:

"1. Does the 25% restriction contained in Section 14-103.12 of Public Act 80-841 represent a diminishment of benefits if applied to the final average compensation calculation effective January 1, 1978? Since the definition of compensation continues to be base pay for periods prior to January 1, 1978, a no answer to this question could mean reduction of pre-January 1, 1978 earnings used for benefit purposes.

2. If the answer to question #1 is yes, could the 25% restriction be applied only to earnings received after January 1, 1978? A yes answer to this question would, in essence, mean that the 25% limitation could only be applied if the total 48 month period consisted of earnings received after January 1, 1978.

3. If the answer to question #2 is no, would it follow that the 25% limitation could only be applied in the case of a state employee first entering service after January 1, 1978?

4. As to per diem employees working less than 15 days per month, does elimination of the special accumulation provision from Public Act 80-841 represent a diminishment of benefits for such an employee who entered state service prior to January 1, 1978?

5. If the answer to question #4 is yes, should the System, in essence, interpret the existence of a savings clause in Public Act 80-841 and grant the accumulation of earnings as currently provided in Section 14-119 to any qualifying per diem employee who entered state service prior to January 1, 1978?"

The basic question is whether the amendment violates article XIII, section 5 of the Illinois Constitution of 1970, which provides as follows:

> "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."

This provision was introduced on the floor of the Constitutional Convention in 1970, and therefore was not discussed in a committee report. The statement of its intended purpose that is most relevant to the present question was made by Delegate Kinney, one of its proponents (IV Record of Proceedings, Sixth Illinois Constitutional Convention at 2931 - 2932):

> " * * * [W]e thought that it would be quite fair if a person undertook employment under a statute that provided for a contingency for lowering the benefits at some future time, that this was, indeed, the contract that he had accepted. 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 be not less than $100 a month in 1990."

This rather stringent interpretation 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.

The Illinois court decision most relevant to this point is Peters v. City of Springfield (1974), 57 Ill. 2d 142. The statute governing firemen's pensions, somewhat like the Act involved here, provided for increasing a fireman's pension by one percent of a certain base rate for each year of service beyond 20 years. Unlike the present situation in which the base rate itself is potentially being changed (by changing "final average compensation"), that case involved a restriction on the number of additional years of service a fireman could put in caused by a reduction in the mandatory retirement age from 65 to 63. Thus, Peters does not settle the present question. But the court's opinion in that case is significant because it seems, in the following language, to interpret the constitutional pro-

vision less stringently than Mrs. Kinney in the Convention (57 Ill. 2d at 151 to 152):

* * *

> * * * The debate on the provision (4 Proceedings 2925-2933) indicates a general intent to protect the pension benefits of public employees, but, other than concern that vested rights not be defeated by reason of the failure to provide necessary funding, reflects uncertainty as to the scope of the restriction which the section imposed on legislative bodies.
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> * * * From our review of the constitutional debates and the authorities, we conclude that the purpose and intent of the constitutional provision was to insure that pension rights of public employees <u>which had been earned</u> should not be 'diminished or impaired' but that it was not intended, and did not serve, to prevent the defendant City from reducing the maximum retirement age, even though the reduction might affect the pensions which plaintiffs would ultimately have received." (Emphasis added.)

The application of these principles to the 25 percent limitation on fourth-year pay is relatively simple. There is no earned right to increase one's pension by being appointed to a higher paid position in the last of the four measuring years. Such an event is contingent and merely speculative. Moreover, as mentioned above, employees could not before January 1, 1978, increase their pensions by doing overtime work, because overtime pay was not counted for pension purposes. The only possible constitutional infirmity would be in applying the new 25 percent

limitation to pay received before January 1, 1978. Thus, although new section 14-103.12 is not by its terms limited to compensation received after the effective date of the Act, it should be so interpreted in order to avoid unconstitutionality.

Therefore, in answer to questions 1, 2, and 3, it is my opinion that the 25 percent restriction may be applied only to earnings received after January 1, 1978. However, I do not agree that this means that the 25 percent limitation could only be applied if the total 48-month period consisted of earnings received after January 1, 1978. The limitation applies only to earnings received in the last year. Thus, although it must be applied proportionately between January 1, 1978, and January 1, 1979, the limitation may be applied in full after January 1, 1979. Furthermore, the restriction applies to all State employees, not just those who started after January 1, 1978.

The same analysis applies to your fourth question relating to the per diem employee. His earned pension may not be diminished. If he had earned a right to a pension on January 1, 1978, the amount of that pension may not be reduced by changing the method of calculation. Thus, a person retiring

after January 1, 1978, whose pension vested prior to that date, is entitled to a pension at least as great as if he had retired on December 31, 1977, calculated on the old basis. Anybody who did not have a pension vested on January 1, 1978, would have a pension calculated under the new method.

Very truly yours,

ATTORNEY GENERAL