IN THE CIRCUIT COURT FOR THE SEVENTH JUDICIAL CIRCUIT,
SANGAMON COUNTY, ILLINOIS

IN RE: PENSION REFORM LITIGATION	) No. 2014 MR 1) Hon. John W. Belz
This document relates to: RETIRED STATE EMPLOYEES ASSOCIATION, an Illinois not-for-profit corporation, and LAWRENCE WORT, GLADYS HAJEK, LINDA GUELDENER and MAURINE RICHTER, for themselves and on behalf of a class of persons similarly situated, Plaintiffs, v. PATRICK QUINN, in his capacity of the Governor of the State of Illinois, JUDY BAAR TOPINKA, Comptroller of the State of Illinois, DAN RUTHERFORD, Treasurer of the State of Illinois, and the BOARD OF TRUSTEES OF THE STATE EMPLOYEES RETIREMENT SYSTEM, Defendants.	) Originally Filed as Sangamon County Case No. 2014 MR 1

ANSWER AND DEFENSES

Defendants Patrick Quinn, in his official capacity as Governor of the State of Illinois, Judy Baar Topinka, in her official capacity as the Comptroller of the State of Illinois, Dan Rutherford, in his official capacity as the Treasurer of the State of Illinois, and the Board of Trustees of the State Employees' Retirement System (collectively "Defendants") for their answer to the Amended Complaint filed by Plaintiffs Retired State Employees Association, *et al.*, state as follows:

COUNT I
(Pension Protection Clause)

1. Plaintiff Retired State Employees Association (the "Association") is an Illinois not-for-profit corporation headquartered in Sangamon County. The Association has over 9,000 members. The purpose and mission of the Association is to protect the interests of retired participants in the State Employees Retirement System, and in particular, their interests with respect to pension and other retirement benefits.

ANSWER: Defendants lack knowledge sufficient to form a belief regarding the allegations in Paragraph 1 and therefore deny the allegations.

2. Plaintiff Lawrence Wort is an individual residing in Sangamon County, Illinois. He loyally served the State of Illinois for over 39 years, retiring in 2000 as an employee of the Department of Transportation. He is an annuitant member of the State Employee Retirement System ("SERS") and is a member of the Association.

ANSWER: Defendants admit that Mr. Wort is an annuitant in SERS, that he retired in 2000 as an employee of the Illinois Department of Transportation, and that he retired with over 39 years of service. Defendants lack knowledge sufficient to form a belief regarding the remaining allegations in Paragraph 2 and therefore deny the allegations.

3. Plaintiff Gladys Hajek is an individual residing in Sangamon County, Illinois. She loyally served the State of Illinois for over 30 years, retiring in 2002 as an employee of the Department of Transportation. She is an annuitant member of SERS and is a member of the Association.

ANSWER: Defendants admit that Ms. Hajek is an annuitant in SERS, that she retired in 2002 as an employee of the Department of Transportation, and that she retired with over 30 years of service. Defendants lack knowledge sufficient to form a belief regarding the remaining allegations in Paragraph 3 and therefore deny the allegations.

4. Plaintiff Linda Gueldener is an individual residing in Sangamon County, Illinois. She loyally served the State of Illinois for over 27 years, retiring in 2006 as an employee of the Department of Natural Resources. She is an annuitant member of SERS and is a member of the Association.

ANSWER: Defendants admit that Ms. Gueldener is an annuitant in SERS, that she retired in 2006 as an employee of the Illinois Department of Natural Resources, and that she retired with over 27 years of service. Defendants lack knowledge sufficient to form a belief regarding the remaining allegations in Paragraph 4 and therefore deny the allegations.

5. Plaintiff Maurine Richter is an individual residing in Sangamon County, Illinois. She loyally served the State of Illinois for over 25 years, retiring in 2002 as an employee of the Department of Natural Resources. She is an annuitant member of SERS and is a member of the Association.

ANSWER: Defendants admit that Ms. Richter is an annuitant in SERS, that she retired in 2002 as an employee of the Illinois Department of Natural Resources, and that she retired with over 25 years of service. Defendants lack knowledge sufficient to form a belief regarding the remaining allegations in Paragraph 5 and therefore deny the allegations.

6. Defendant Patrick Quinn is the Governor of the State of Illinois. Pursuant to Article V, Section 8 of the Illinois Constitution, "the Governor shall have the supreme executive power, and shall be responsible for the faithful execution of the laws." Governor Quinn was the architect of PA 98-599 and is ultimately responsible for the administration of the law, PA 98-599, challenged in this case. Governor Quinn is sued in his official capacity only.

ANSWER: Defendants admit that Mr. Quinn is the Governor of the State of Illinois and that Mr. Quinn is sued in his official capacity only. Defendants further admit that Paragraph 6 correctly quotes Article V, Section 8 of the Illinois Constitution. Defendants deny the remaining allegations in Paragraph 6.

7. Defendant Judy Baar Topinka is the Comptroller of the State of Illinois. Pursuant to Article V, Section 17 of the Illinois Constitution, "the Comptroller, in accordance with the law, shall maintain the State's central fiscal accounts and order payments into and out of the funds held by the Treasurer." As such, Comptroller Topinka signs paychecks or grants approval to electronic payments made by the State to its retirees, and as such, is involved in the administration of the law, PA 98-599, challenged in this case. Comptroller Topinka is also the Chairman of the Board of Trustees. Comptroller Topinka is sued in her official capacity only.

ANSWER: Defendants admit the allegations in Paragraph 7 and further state that Comptroller Topinka is a nominal defendant sued only in her official capacity.

8. Defendant Dan Rutherford is the Treasurer of the State of Illinois. Pursuant to Article V, Section 18 of the Illinois Constitution, "the Treasurer, in accordance with law, shall be responsible for the safe keeping and investment of monies and securities deposited with him, and for their disbursement upon order of the Comptroller." As such, Treasurer Rutherford is involved in the administration of the law, PA 98-599, challenged in this case. Treasurer Rutherford is sued in his official capacity only.

ANSWER: Defendants admit the allegations in Paragraph 8 and further state that Treasurer Rutherford is a nominal defendant sued only in his official capacity.

9. Defendant Board of Trustees of the State Employees Retirement System ("Board of Trustees") is an independent agency of the State of Illinois, organized and existing pursuant to

Article XIV of the Illinois Pension Code, 40 ILCS 5/14-101, *etseq.* The Board of Trustees is the agency primarily involved in the administration of the law, PA 98-599, challenged in this case. The Board of Trustees is sued in its official capacity only.

ANSWER: Defendants admit that the Board of Trustees is involved in the administration of Public Act 98-599 as it relates to Article 14 of the Pension Code. Defendants admit the remaining allegations in Paragraph 9.

10. Plaintiff Association brings this lawsuit on behalf of its members. Those members otherwise have standing to sue in their own right; the interests sought to be protected in this lawsuit are germane to the purpose of the organization, and neither the claim asserted nor the relief requested requires the participation of individual members in the lawsuit.

ANSWER: Paragraph 10 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

11. Plaintiffs Wort, Hajek, Gueldener and Richter bring this lawsuit on behalf of a class of persons which includes most of the membership of the Association, but which is also broader than the membership of the Association, namely all retired members of SERS and other persons, such as survivors and inactive employees entitled to SERS benefits but not yet receiving them, who are or would be entitled to receive an annuity based upon the law as it exists as of the date of filing of this Complaint and will exist through May 31, 2014. As set forth in most recent SERS Annual Report dated January 9, 2013, a copy of which is attached hereto as Exhibit A and is incorporated by reference, the number of persons in the class exceeds 60,000 persons, such that joinder of all members is impracticable. There are questions of law or fact common to the class, which common questions predominate over questions affecting only individual members. The representative parties will fairly and adequately protect the interests of the class.

ANSWER: Defendants admit that Plaintiffs purport to bring this lawsuit on behalf of the class of persons described in Paragraph 11. The remainder of Paragraph 11 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

12. Plaintiffs also seek the creation of a subclass of persons who availed themselves of early retirement incentive programs in 1991, 2002 or later. This subclass (the "ERI Subclass") exceeds 10,000 persons. Plaintiffs Hajek and Richter are members of the ERI Subclass, having taken early retirement in 2002, and will adequately represent the subclass. The ERI Subclass involves only Count IV of this Complaint. With respect to all other counts, the claims of the ERI Subclass are identical to those of the other members of the class.

ANSWER: Defendants admit that Ms. Hajek and Ms. Richter participated in the 2002 Early

Retirement Incentive Program. Defendants further admit that Plaintiffs purport to bring this lawsuit on behalf of the subclass of persons described in Paragraph 12. The remainder of Paragraph 12 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

13. This case concerns the constitutionality of Public Act 98-599, which was adopted by both Houses of the General Assembly on December 3, 2013 and was signed by Governor Quinn on December 5, 2013. PA 98-599 implements a number of changes in the various pension systems of the State of Illinois, including SERS, the State Universities Retirement System ("SURS"), the Teachers Retirement System of the State of Illinois ("TRS"); the Public School Teachers' Pension and Retirement Fund ("PSTPRF") the General Assembly Retirement System ("GARS"). PA 98-599, however, omits to make any changes to the Judges' Retirement System.

ANSWER: Defendants admit that this case concerns the constitutionality of Public Act 98-599, which was adopted by both Houses of the General Assembly on December 3, 2013 and was signed by Governor Quinn on December 5, 2013. Defendants further admit that PA 98-599 implements a number of changes in the various pension systems of the State of Illinois, and that PA 98-599 does not make any changes to the Judges' Retirement System.

14. In 1970, when the current Illinois Constitution was drafted, the State-sponsored pension funds were actuarially underfunded. In February, 2012, Eric Madiar, counsel to Illinois Senate President John J. Cullerton and Parliamentarian of the Illinois Senate, accurately described the situation in a well-known treatise published on the internet and widely circulated in the halls of the General Assembly, *Is Welching On Public Pension Promises An Option For Illinois'?,* as follows:

> At the time of the Convention, the Pension Laws Commission reported that the General Assembly Retirement System (GARS) was 68.5% funded, while the State University Retirement System (SURS) was 47% funded. The remaining state-funded retirement systems had the following funding percentages: State Employees Retirement System (SERS) 43%; Judicial Retirement System (JRS) 32.3%; and Teachers Retirement System (TRS) 40%. The five State pension systems had an aggregate funding ratio of 41.8%. By comparison police and firemen pension funds were respectively only 33.8% and 19.1% funded. As noted at the outset, the five systems currently have a combined funding ratio of 43.3%.

ANSWER: Defendants admit that the State-sponsored pension funds were actuarially underfunded in 1970. Defendants deny the remaining allegations in Paragraph 14.

15. The 1970 Constitution defined "membership in a pension or retirement system" as an "enforceable contractual right." As shown by the Con-Con debates; the drafters of the 1970 Constitution intended that the General Assembly would begin a process of properly funding the pension systems. In 1995, in the wake of litigation over the issue, the General Assembly adopted Public Act 88-0593, requiring the state during fiscal years 1996 through 2045 to make sufficient payments into the pension systems so that the State could fund the system at a 90% level by fiscal year 2045 and beyond. By the year 2000, the State had funded SERS to the level of 81.65%.

ANSWER: Defendants admit that the 1970 Constitution states that "membership in a pension or retirement system" as an "enforceable contractual right"; that in 1995 the General Assembly enacted Public Act 88-0593 prescribing certain levels of contributions by the State to the state-funded retirement systems, and that as of the end of fiscal year 2000, the ratio of SERS assets to its unfunded actuarial liability, according to its actuaries, was approximately 81.65 %. The remaining allegations of paragraph 15 consist of legal conclusions that Defendants deny, and to the extent they contain any factual allegations, Defendants deny them.

16. Since the year 2000, prior governors and the General Assembly have consistently failed to fund SERS and the other pension systems, preferring to use SERS and those other systems as lenders of last resort, and using funds which pursuant to PA 88-593, were to be earmarked for pensions, to pay for other pet projects. The General Assembly and past Governors have even declared pension "holidays", intentionally refusing to fund SERS in certain years. Because of 13 years of abuse, and as noted by Mr. Madiar, the funds are today about where they were in 1970.

ANSWER: Defendants deny the allegations in Paragraph 16.

17. While the General Assembly and prior Governors have failed to uphold the State's side of the enforceable contractual relationship contemplated by the Constitution, the State has at all times forced its employees and retirees to keep *their* side of the deal, at all times continuing to withhold the employees' contributions from their paychecks. There has never been a "holiday" for the Plaintiffs, either while they were employees or as retirees.

ANSWER: Defendants deny the allegations in Paragraph 17.

18. The preamble to PA 98-599, which purports to express the legislative intent of the State, is pure political theater and not a valid statement of intent, inasmuch as it ignores the history of the State refusing to honor its obligations to its employees and retirees. The preamble also ignores the State's repeated failure to comply with its own prior pension reform statutes, notably Public Act 88-0593. It ignores the fact that in 2000, SERS was over 80% funded and has purposefully been underfunded ever since. The preamble says:

At the time of passage of this amendatory Act of the 98th General Assembly, Illinois has both atypically large debts and structural budgetary imbalances that will, unless addressed by the General Assembly, lead to even greater and rapidly growing debts and deficits.

Ignoring the fact that the General Assembly's and prior governors' consistent failures to fund SERS and the other pension funds is the entire cause of the problem, the preamble continues:

> Meanwhile, the State's annual pension contribution has substantially increased in recent years, and will continue to increase in coming years. The General Assembly recognizes that without significant pension reform, the unfunded liability and the State's pension contribution will continue to grow, and further burden the fiscal stability of both the State and its retirement systems.

ANSWER: Defendants admit that Paragraph 18 accurately quotes parts of the preamble to Public Act 98-599. Defendants deny the remaining allegations in Paragraph 18.

19. Thus PA 98-599 rewrites history and proposes to balance the State budget on the backs of retirees, making retirees the scapegoat for the State's fiscal sins. In a similar vein, Defendant Governor Quinn issued a press release the day he signed SBl into law as PA 98-599. The press release, a copy of which is attached hereto as Exhibit B, says:

> Under the new law, the state will adopt an actuarially sound funding schedule that requires level payments and achieves 100 percent funding no later than the end of fiscal year 2044.

In other words, PA 98-599 purports to do precisely what PA 88-0593 was supposed to do— until prior Governors, in concert with the General Assembly, decided to ignore their constitutional duty to "be responsible for the faithful execution of the laws." There is no reason to believe that future Governors or legislatures will act any differently unless compelled to do so now by the Courts.

ANSWER: Defendants admit that Governor Quinn released the press release attached as Exhibit B, and that Paragraph 19 accurately quotes portions of the press release. Defendants deny the remaining allegations in Paragraph 19.

20. Governor Quinn's press release goes on to state:

> Under the new law, there will be no reductions in the pension checks going out to current retirees. The law will also minimize the impact on the lower-earning, longer-serving employees. There will continue to be Cost of Living Adjustments (COLA); however, they will grow at a slower rate. For most employees, the COLA will be adjusted from the current 3 percent annually compounding increases that are unsustainable to a new formula based on years of service that includes protections

for lower-earning, longer-serving employees.

The quoted language is simply untrue. There *will be* reductions in pension checks going out to current retirees. The Pension Code is a complete stranger to the term, "Cost of Living Adjustment."

ANSWER: Defendants admit that Paragraph 20 accurately quotes portions of Governor Quinn's press release. Defendants deny the remaining allegations in Paragraph 20.

21. The issue in this case concerns PA 98-599's insertion of new subsection (a-1) to Section 14-114 of the Illinois Pension Code, 40 ILCS 5/14-114. Prior to enactment of PA 98-599, Section 14-114 of the Illinois Pension Code entitled all annuitants to an automatic 3% annual increase in their annuities (hereinafter, the "Automatic 3% Increase"), providing as follows:

> § 14-114. Automatic increase in retirement annuity.
>
> (a) Any person receiving a retirement annuity under this Article who retires having attained age 60, or who retires before age 60 having at least 35 years of creditable service, or who retires on or after January 1, 2001 at an age which, when added to the number of years of his or her creditable service, equals at least 85, shall, on January 1 next following the first full year of retirement, have the amount of the then fixed and payable monthly retirement annuity increased 3%.

ANSWER: Defendants admit the allegations in Paragraph 21.

22. The new subsection (a-1), which becomes effective on June 1, 2014, substantially impairs and diminishes the Automatic 3% Increase. It states as follows:

> (a-1) Notwithstanding subsection (a), but subject to the provisions of subsection (a-2), all automatic increases payable under subsection (a) on or after the effective date of this amendatory Act of the 98th General Assembly shall be calculated as 3% of the lesser of (1) the total annuity payable at the time of the increase, including previous increases granted, or (2) $800 ($1,000 for portions of the annuity based on service as a noncovered employee) multiplied by the number of years of creditable service upon which the annuity is based. Beginning January 1, 2016, the $800 ($1,000 for portions of the annuity based on service as a noncovered employee) referred in item (2) of this subsection (a-1) shall be increased on each January 1 by the annual unadjusted percentage increase (but not less than zero) in the consumer price index-u for the 12 months ending with the preceding September; these adjustments shall be cumulative and compounded. For the purposes of this subsection (a-1), "consumer price index-u" means the index published by the Bureau of Labor Statistics of the United States Department of Labor that measures the average change in prices of goods and services purchased by all urban consumers, United States city average, all items, 1982-84 = 100. The new dollar amount resulting from each annual adjustment shall be determined by the Public Pension

Division of the Department of Insurance and made available to the System by November 1 of each year. This subsection (a-1) is applicable without regard to whether the person is in service on or after the effective date of this amendatory Act of the 98th General Assembly.

ANSWER: Defendants admit that 40 ILCS 5/14-114(a-1) becomes effective on June 1, 2014 and that Paragraph 22 accurately quotes the language of 40 ILCS 5/14-114(a-1). Defendants deny the remaining allegations in Paragraph 22.

23. Section 14-114 of the Pension Code has been part of the Pension Code since 1969. It has been amended and renumbered a number of times, but history of the Section most relevant to this case are as follows:

A. Prior to 1969, a retiring SERS annuitant's annuity was fixed as of the date of his or her retirement.

B. Public Act 76-748, effective August 15, 1969, added Section 14-153.1, captioned "Automatic Increase in Service Retirement Allowance," to the Illinois Pension Code. The section provided that any employees retiring after December 31, 1969, having attained age 60, would, on January 1 next following the first full year of retirement, and each succeeding year thereafter, have the amount of his or her then fixed and payable retirement annuity increased by an additional 1.5%. annually, up to a maximum of 30% over the years. PA 76-748 also provided for an increase in SERS members' out-of-pocket monthly payroll deduction in an amount of .5% of salary effective January 1, 1970 and going forward, and it mandated that the State match the payroll deduction with an additional .5% contribution. Putting it another way, PA 76-748 mandated that future annuitants would pay for future automatic increases in their annuities through present payroll deductions, and that the State would match the employees' payroll deduction to pay for the automatic increases.

C. The national increase in the consumer price index ("CPI") in 1969 was 5.46%, far above the 1.5% annual automatic increase in annuity payments mandated by PA 76-748. In no sense did PA 76-748 attempt a "cost of living adjustment," which would have indexed the automatic increases to increases in the CPI or some other measure of inflation.

D. PA 77-292, effective July 15, 1971, eliminated the 30% cap and provided that the automatic rate of increase in the annuity—now termed an "allowance"—would be 2% per year. The national CPI increase in 1971 was 4.30%, more than double the 2% annual automatic increase mandated by PA 77-292.

E. PA 80-1408, effective August 28, 1978, amended Section 14-114 by raising the annual automatic increase—by then once again referred to as an "annuity"—to 3% annually. The national CPI increase in 1978 was 7.6%, more than two and a half times the 3% Automatic Increase.

F. Public Act 86-273, effective August 1989, provided that effective January 1, 1990, the 3% Automatic Increase would be in effect compounded. So, in 1991, an annuitant would receive 103% of 1990's payment; in 1992, 103% of 1991 's payment, etc. The national CPI increase in 1989 was 4.83%, more than one and a half times as much as the 3% Automatic Increase.

ANSWER: Defendants admit that Section 14-114 has been part of the Pension Code since 1969 and that it has been amended and renumbered several times. Defendants further admit the allegations in Paragraph 23 subsections (A), (E), and (F). Defendants deny that Public Act 76-748 "mandated that future annuitants would pay for future automatic increases in their annuities through present payroll deductions, and that the State would match the employees' payroll deduction to pay for the automatic increases," but admit the remainder of Paragraph 23 subsection (B). Defendants admit that the national increase in the consumer price index in 1969 was approximately 5.5%. Defendants further admit that Public Act 77-292 was effective July 15, 1971, that Public Act 77-292 eliminated the 30% cap, and that under Public Act 77-292 the automatic rate of increase in retiree's annuities would be 2% per year. Defendants also admit that the national increase in the consumer price index in 1971 was approximately 4.4%. Defendants deny the remainder of Paragraph 23 subsections (C) and (D). Further answering, Defendants state that the purpose of the annual automatic increases in the Pension Code was to mitigate in part the effects of increases in the cost of living, that the General Assembly has regularly changed the rate of such increases, that such changes since 1970 have been included in the Pension Code without requiring active system members to make any contributions higher than before those changes, and that the most recent changes in annual automatic increases added to the Pension Code before the Act were extended to persons who had already retired and ceased making any contributions to their retirement system.

24. While as shown by the press release, Exhibit B, Governor Quinn and certain legislators prefer to refer to the 3% Automatic Increase as a "Cost of Living Adjustment" in an effort to influence public opinion, at no time during the forty-four years since what is now Section 14-114 was added to the Pension Code in 1969 has it included any language or reference

to the Automatic Increase, whether 1.5%, 2% or 3%, being a "cost of living adjustment" or "COLA." The 3% Automatic Increase simply is not a COLA under the commonly accepted definition of the term.

ANSWER: Defendants deny the allegations in Paragraph 24.

25. All of the members of the Association, all of the Class Plaintiffs, and all of the members of the Class worked (or are the survivors of such workers) during a period when the 3% Automatic Increase mandated by Section 14-114 of the Pension Code was in effect, and retired at a time when the 3% Automatic Increase mandated by Section 14-114 of the Pension Code was in effect. They contributed the .5% of their salaries required by Section 14-114 to fund the 3% Automatic Increase.

ANSWER: Defendants deny that the 0.5% employee contributions required by Section 14-114 starting in 1970 funded later-enacted automatic annuity increases. Further answering, Defendants state that the purpose of the annual automatic increases in the Pension Code was to mitigate in part the effects of increases in the cost of living, that the General Assembly has regularly changed the rate of such increases, that such changes since 1970 have been included in the Pension Code without requiring active system members to make any contributions higher than before those changes, and that the most recent changes in annual automatic increases added to the Pension Code before the Act were extended to persons who had already retired and ceased making any contributions to their retirement system. Defendants lack knowledge sufficient to form a belief regarding the remaining allegations in Paragraph 25 and therefore deny the allegations.

26. Article XII, Section 5 of the Illinois Constitution of 1970, the Pension Protection Clause, provides 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.

ANSWER: Defendants admit the allegations in Paragraph 26.

27. There is a controversy between the Plaintiffs and the Defendants as to the Constitutional validity of Public Act 98-599, and in particular as to the new subsection (a-1) to Section 14-114 of the Illinois Pension Code. Plaintiffs contend that PA 98-599 and the new subsection (a-1) violate Article XII, Section 5 of the Illinois Constitution of 1970 by diminishing and impairing the future pension and retirement benefits of all SERS retirees, namely, by diminishing and impairing the 3% Automatic Increase. Defendants deny that such is the case, and they intend to implement PA 98-599 on its effective date.

ANSWER: Defendants admit that a controversy exists as to the constitutional validity of Public Act 98-599 and, in particular, Section 14-114(a-1) of the Illinois Pension Code. Defendants further admit that they assert in this case that Public Act 98-599 is constitutional and that they intend to implement it according to its terms unless ordered not to do so by a valid court order or judgment. The remaining allegations in Paragraph 27 consist of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

28. Plaintiffs are threatened with irreparable injury and have no adequate remedy at law.

ANSWER: Paragraph 28 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

29. In order to protect the Plaintiffs during the pendency of this litigation, this Court should order the State to establish an escrow in the amount of the difference between the amounts to which the Plaintiffs would be entitled pursuant to Section 14-114 of the Pension Code as it existed as of the date of filing of this case and through May 31, 2014, and the amounts to which they are entitled under the Pension Code as it takes effect on June 1, 2014, and thereafter.

ANSWER: Paragraph 29 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

<u>COUNT II (Equal Protection Clause)</u>

1-25. Plaintiffs reallege paragraphs 1 through 25 of Count I as and for paragraphs 1 through 25 of this Count II.

ANSWER: Defendants repeat and reincorporate their answers above.

26. Article I, Section 2 of the Illinois Constitution of 1970 states as follows:

No person shall be deprived of life, liberty or property without due process of law nor be denied the equal protection of the laws.

ANSWER: Defendants admit the allegations in Paragraph 26.

27. Prior to adoption of Public Act 98-599, the provisions of the Pension Code governing SURS, TRS, PSTPRF, GARS and the Judges' Retirement System all provided for a 3% Automatic Increase, and contained provisions similar to Section 14-114 of the Pension Code. PA 98-599 limits the 3% Automatic Increase, and contains provisions similar to those of the new subsection (a-1) of Section 14-114 of the Pension Code, with respect to all of these systems save one: the Judges' Retirement System.

ANSWER: Defendants admit the allegations in Paragraph 27.

28. Keeping the 3% Automatic Increase in full effect with respect to the Judges' Retirement System, while diminishing and impairing the 3% Automatic Increase set forth in Section 14-114 of the Pension Code and the similar 3% Automatic Increase provisions enjoyed by SURS, TRS, PSTPRF and GARS Annuitants, lacks a rational basis reasonably related to a legitimate governmental purpose.

ANSWER: Paragraph 28 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them. Further answering, Defendants allege that the General Assembly reasonably could have concluded that not including other Articles of the Pension Code within the scope of Public Act 98-599, including Article 18, is rationally related to a legitimate purpose.

29. There is a controversy between the Plaintiffs and the Defendants as to the validity of Public Act 98-599, and in particular as to the new subsection (a-1) of Section 14-114 of the Illinois Pension Code. Plaintiffs contend that the Public Act and the new subsection (a-1) violate Article I, Section 2 of the Illinois Constitution of 1970 by depriving the Plaintiffs of the equal protection of the laws vis-a-vis retired judges. Defendants deny that such is the case, and they intend to implement PA 98-599 on its effective date.

ANSWER: Defendants admit that a controversy exists as to the constitutional validity of Public Act 98-599 and, in particular, Section 14-114(a-1) of the Illinois Pension Code. Defendants further admit that they assert in this case that Public Act 98-599 is constitutional and that they intend to implement it according to its terms unless ordered not to do so by a valid court order or judgment. The remaining allegations in Paragraph 29 consist of legal conclusions that

Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

30. Plaintiffs are threatened with irreparable injury and have no adequate remedy at law.

ANSWER: Paragraph 30 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

31. In order to protect the Plaintiffs during the pendency of this litigation, this Court should order the State to establish an escrow in the amount of the difference between the amounts to which the Plaintiffs would be entitled pursuant to Section 14-114 of the Pension Code as it existed as of the date of filing of this case and through May 31, 2014, and the amounts to which they are entitled under the Pension Code as it takes effect on June 1, 2014, and thereafter.

ANSWER: Paragraph 31 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

COUNT III
(Impairment of Contracts Clause)

1-25. Plaintiffs reallege paragraphs 1 through 25 of Count I as and for paragraphs 1 through 25 of this Count III.

ANSWER: Defendants repeat and reincorporate their answers above.

26. The Constitution defines membership in SERS as an "enforceable contractual relationship." During their tenure at the State, the Plaintiffs continually paid their .5% contributions in exchange for their entitlement to the 3% Automatic Increase. Moreover, the Plaintiffs were continually reminded of the 3% Automatic Increase in numerous publications, seminars, etc. This has occurred for at least the last 40 years:

A. The 1982 Benefits Handbook, distributed to most if not all State employees at the time, is attached hereto as Exhibit C-1. It said, on page 11:

> If you retire after age 60, you will receive a 3% increase in your pension on January 1 following your first full year of retirement. Future increases of 3% of your original pension will also be made each January 1 thereafter. Future increases in your pension will not be limited by the 75% maximum.
>
> If you retire before age 60, you will receive a 3% increase in your pension on January 1 after you reach age 60 if you have been retired for one full year.
>
> If you retire with 35 or more years of credited service, you are eligible for your first increase on the January 1 following your first full year of retirement whether or not

you have then reached age 60.

B. The 1992 Benefits Handbook, distributed to most if not all State employees at the time, is attached hereto as Exhibit C-2. It said, on page 8:

> If you are a retiree of the State Employees Retirement System, you will receive a 3 % increase in your pension on January 1 following your first full year of retirement or attainment of age 60, whichever is later. If you retire with 35 or more years of service, you are eligible for your first increase on the January 1st following your first full year of retirement, whether or not you have reached age 60. Future increases of 3 % of your current pension will also be made each January 1 thereafter.

C. The 2001 Benefits Handbook, distributed to most if not all State employees at the time, is attached hereto as Exhibit C-3. It said, on page 8:

> SERS retirees receive a 3% increase in their pensions on January I following their first full year of retirement, or age 60, whichever is later. If you retire using the Rule of 85, you are eligible for your first increase on the January 1 following your first full year of retirement, even if you are not age 60. Future increases of 3% of your current pension will also be made each January 1 thereafter. Future increases are not limited by the 75% maximum. If you retired under the alternative formula, you will receive a 3% increase to your pension on January 1 following your first full year of retirement or age 55, whichever is later. Future increases are not limited by the 80% maximum.

D. The current SERS Benefits Handbook, 2011 edition, was distributed to most if not all State employees, and is posted on the SERS website. It is attached hereto as Exhibit C-4. It says, on page 19:

> If you retire under the Rule of 85, you are eligible for your first 3% increase on January 1 following your first full year of retirement, even if you are not age 60. If you retire at age 60 or older, you will receive a 3% pension increase every year on January 1, following your first full year of retirement. If you retire before age 60 with a reduced retirement benefit, you will receive a 3% pension increase every January 1 after you turn age 60 and have been retired at least one full year. These pension increases are not limited by the 75% maximum.

E. The current SERS Annual Report, Exhibit A to this Complaint, similarly describes (page 66) the 3% automatic increase for Tier 1 employees—that is, for employees hired prior to July, 2011. A similar description is contained in at least the last 10 years' SERS annual reports, all of which are and have been available on the SERS website.

ANSWER: Defendants admit that the Illinois Constitution states that membership in a public pension system is an "enforceable contractual relationship." Defendants also admit that Paragraph 26 subsections (A), (B), (C), and (D) accurately quote the SERS benefits handbooks, but deny that such handbooks may create rights greater than, or inconsistent with, the law. Defendants further admit that current and past SERS Annual Reports described the 3% automatic annual increase for Tier 1 employees. Defendants deny the remaining allegations in Paragraph 26.

27. In diminishing and limiting the 3% Automatic Increase, PA 98-599 impairs the Plaintiffs' enforceable contractual rights in violation of Article I, Section 16 of the Illinois Constitution, which provides in relevant part:

No... law impairing the obligation of contracts... shall be passed.

ANSWER: Defendants admit that Paragraph 27 accurately quotes Article I, Section 16 of the Illinois Constitution, but deny the remaining allegations in Paragraph 27.

28. There is a controversy between the Plaintiffs and the Defendants as to the validity of Public Act 98-599, and in particular as to the new subsection (a-1) to Section 14-114 of the Illinois Pension Code. Plaintiffs contend that the Public Act and the new subsection (a-1) violate Article I, Section 16 of the Illinois Constitution insofar as they diminish and impair the Plaintiffs' contractual rights. Defendants deny that such is the case, and they intend to implement PA 98-599 on its effective date.

ANSWER: Defendants admit that a controversy exists as to the constitutional validity of Public Act 98-599 and, in particular, Section 14-114(a-1) of the Illinois Pension Code. Defendants further admit that they assert in this case that Public Act 98-599 is constitutional and that they intend to implement it according to its terms unless ordered not to do so by a valid court order or judgment. The remaining allegations in Paragraph 28 consist of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

29. Plaintiffs are threatened with irreparable injury and have no adequate remedy at law.

ANSWER: Paragraph 29 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

30. In order to protect the Plaintiffs during the pendency of this litigation, this Court should order the State to establish an escrow in the amount of the difference between the amounts to which the Plaintiffs would be entitled pursuant to Section 14-114 of the Pension

Code as it existed as of the date of filing of this case and through May 31, 2014, and the amounts to which they are entitled under the Pension Code as it takes effect on June 1, 2014, and thereafter.

ANSWER: Defendants deny the allegations in Paragraph 30.

COUNT IV
(Impairment of Contract Clause—ERI Subclass)

1-25. Plaintiffs reallege the paragraphs 1 through 25 of Count I as and for paragraphs 1 through 25 of this Count IV.

ANSWER: Defendants repeat and reincorporate their answers above.

26. This Count IV is brought by Plaintiffs Hajek and Richter on behalf of the ERI Subclass and relates only to the ERI Subclass.

ANSWER: Defendants admit the allegations in Paragraph 26.

27. In 2002, the State of Illinois announced an Early Retirement Incentive Program (hereinafter "ERI Program"). The program was specifically designed to lower the personnel costs of the State of Illinois by pensioning off higher paid employees with many years of service. The Early Retirement Program provided for the purchase by eligible annuitants of additional service credits, and promised that the ERI Participants would have continued entitlement to the 3% Automatic Increase. See, e.g., the ERI website attached hereto as Exhibit D.

ANSWER: Defendants admit that the General Assembly enacted an Early Retirement Incentive Program in 2002 and that the Program provided for the purchase of additional service credits by eligible state employees who were members of the affected retirement systems. Defendants deny the remaining allegations in Paragraph 27.

28. According to a report of the Commission on Government Forecasting and Accountability attached hereto as Exhibit E, in reliance on the 2002 ERI Program, the over 10,000 members of the ERI Subclass paid the State over $128 million to purchase additional service credits and retired from State service. They thereby reduced the State's payroll costs over $2.9 billion in the years 2003-2012.

ANSWER: Defendants admit that participation in the 2002 early retirement program reduced the State's payroll expenditures in the years after it was passed and that participants in that program made payments in connection with their election to participate in the program. Defendants lack knowledge sufficient to form a belief regarding what members of the purported

ERI subclass relied upon and the accuracy of the information reported by the Commission of Government Forecasting and Accountability and therefore deny the allegations.

29. While much smaller in terms of the number of retirees involved and the fiscal impact on the State, early retirement incentive programs similar to the 2002 program were announced in 1991 and in 2005, and the persons who availed themselves of those early retirement programs are included in the ERI subclass.

ANSWER: Defendants admit that the claims asserted by the purported ERI subclass also relate to the Early Retirement Incentive Programs in 1991 and 2005. Defendants deny the remaining allegations in Paragraph 29.

30. The State's promises and the ERI Subclass's reliance thereon created implied contracts between the State and members of the ERI Subclass pursuant to the principles of promissory estoppel.

ANSWER: Paragraph 30 consists of legal conclusions to which no answer is required.

31. In eliminating the 3% Automatic Increase, Public Act 98-599 is an impairment of the contracts made between the State of Illinois and members of the ERI Subclass and as such, is an impairment of the contract in violation of Article I, Section 16 of the Illinois Constitution, which provides in relevant part:

No... law impairing the obligation of contracts... shall be passed.

ANSWER: Paragraph 31 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

32. There is a controversy between the ERI Subclass and the Defendants as to the validity of Public Act 98-599, and in particular as to the new subsection (a-1) of Section 14-114 of the Illinois Pension Code. Members of the ERI Subclass contend that the Public Act and the new subsection (a-1) violate Article I, Section 16 of the Illinois Constitution insofar as they diminish and impair the Plaintiffs' contractual rights obtained by participation in the Early Retirement Incentive programs of the State, which are in addition to the contractual rights enjoyed by them simply by being members of SERS. Defendants deny that such is the case, and they intend to implement PA 98-599 on its effective date.

ANSWER: Defendants admit the allegations in Paragraph 32.

33. Plaintiffs are threatened with irreparable injury and have no adequate remedy at law.

ANSWER: Paragraph 33 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

34. In order to protect the ERI Subclass during the pendency of this litigation, this Court should order the State to establish an escrow in the amount of the difference between the amounts to which the Plaintiffs would be entitled pursuant to Section 14-114 of the Pension Code as it existed as of the date of filing of this case and through May 31, 2014, and the amounts to which they are entitled under the Pension Code as it takes effect on July 1, 2014, and thereafter.

ANSWER: Paragraph 34 consists of legal conclusions that Defendants deny, and to the extent it contains any factual allegations, Defendants deny them.

AFFIRMATIVE MATTER IN DEFENSE OF CLAIMS ASSERTED
(Reserved Sovereign Powers)

Pursuant to Section 2-613(d) of the Code of Civil Procedure, Defendants further respond to the Amended Complaint by alleging the following affirmative matter in defense of the claims asserted by the plaintiffs in this suit:

1. All causes of action asserted in the Plaintiffs' Complaint fail to state a claim and are barred because Public Act 98-599 (the "Act") is a permissible exercise of the State of Illinois' reserved sovereign powers (sometimes referred to as the State's police powers). Plaintiffs cannot sustain their burden of establishing that Public Act 98-599 is unconstitutional.

2. Starting around 2000 and continuing through the financial crisis and deep recession that began in 2008, underfunding in the state-funded retirement systems (*i.e.*, asset levels below the actuarially required amounts needed to pay all benefits for services provided by members) contributed significantly to a severe financial crisis for the State that adversely affected the long-term financial soundness of those retirement systems, the cost of financing the State's operations and outstanding debt, and the State's ability to provide critical services to Illinois residents and businesses.

3. From fiscal year 1999 to fiscal year 2013, the unfunded actuarial liability of the four state-funded retirement system affected by Public Act 98–599 (hereinafter the "Systems"),

according to the Systems' actuarial reports for those years, increased as follows (rounded to the nearest million dollars):

	1999	2013
TRS	$10,968,000,000	$55,732,000,000
SERS	$2,012,000,000	$22,843,000,000
SURS	$1,855,000,000	$20,110,000,000
GARS	$94,000,000	$269,000,000
Total:	$14,929,000,000	$98,954,000,000

The causes of this underfunding included, but were not limited to, significant unforeseen and unanticipated events, including, among other things: (1) prolonged and unusually poor investment results and reasonable future investment return expectations due to systemic, severe market downturns, including in the wake of the worst financial crisis since the Great Depression; (2) historically low rates of inflation; (3) significant increases in life expectancy; and (4) other changes in actuarial assumptions. These events not only increased significantly the Systems' unfunded actuarial liabilities, but also led to substantial reductions in the State's revenues available to make contributions to the Systems and for other expenditures, including wages, salaries and other benefits for state employees.

4. Although the Systems have been underfunded for many years, their underfunding now greatly exceeds the State's annual budget for all categories of expenditure, including, without limitation, public education, public health and safety, medical coverage for the poor and for current and retired public employees, road construction, repair and maintenance, and all other public services provided by state employees.

5. Before passage of the Act, the Systems' unsustainable and worsening liabilities greatly contributed to higher debt financing costs for the State, which passage of the Act immediately and substantially alleviated. The Systems' unsustainable and worsening pension liabilities, which the Act was intended to address, also contributed to substantial uncertainty in the State's climate for attracting and retaining businesses that provide employment to Illinois residents, contribute to a thriving state economy, and pay taxes that support important public services and provide revenues to fund the Systems. A significant factor contributing to the magnitude of System's liabilities and corresponding underfunding is that the 3% compounded annual annuity increases, which are not part of the core pension benefit, have in recent years substantially exceeded actual inflation and were not matched with higher employee contributions.

6. Before enacting Public Act 98-599, the General Assembly took multiple other steps to address the State's financial crisis, including the increasingly urgent problem presented by the Systems' underfunding. Those steps included, among other things, enacting a separate program of less generous pension benefits for persons who became system members after 2010 (identified as "Tier II" members); significantly reducing public spending on other programs, including support for public education, Medicaid, health insurance benefits for current and retired state employees, and other social services for Illinois residents; raising income taxes; and deferring billions of dollars in payments owed to state vendors and other creditors. These measures proved insufficient to adequately address the State's financial crisis, and its credit rating continued to suffer, causing it to incur still higher costs to finance its debt, thereby further reducing the revenues that could be devoted to providing critical services to Illinois residents and reducing the Systems' unfunded liabilities.

7. Only after taking these other measures to promote the actuarial soundness of the Systems and address the State's financial crisis resulting from this underfunding problem did the General Assembly pass the Act, which includes a schedule for actuarially prescribed, automatic state contributions to the Systems that will progressively eliminate their underfunding, a mechanism for enforcing those contributions, reductions in contributions to the Systems by their active members, and for persons who became members of the Systems before 2011 (referred to as "Tier I" members), modifications to future pension increases for active and retired members.

8. The pension modifications provided in the Act include prospective reductions in future increases in annual annuity adjustments (often referred to as cost-of-living adjustments, or COLAs) that are designed to have the least impact on members with the lowest salaries on which their pensions are calculated, on members who put in the most years of public service, and on members who retired before July 1, 2014.

9. The pension modifications provided in the Act also include increases in the retirement age at which active members below the age of 46 are entitled to receive a pension. Those increases, up to a maximum of five years, are lowest for the oldest active members and are progressively greater for younger active members.

10. The pension modifications provided in the Act further include a cap on the pensionable salary of active members with a salary presently above about $110,000, and a change in the method for determining the "effective rate of interest" used to calculate pensions for members under the money-purchase formulas included in Articles 15 and 16 of the Pension Code.

11. In light of the above-described unanticipated exigencies contributing to the Systems' unsound financial condition and the State's related fiscal crisis, the Act represented a

reasonable response to these circumstances. In light of the measures already taken by the General Assembly to address the Systems' financial condition and the State's fiscal crisis, and in light of the serious negative effects of other alternatives, the Act's limited changes to pensions were necessary to address these circumstances.

12. The legislative findings in the Act include the following:

> 1. a. "Illinois has both atypically large debts and structural budgetary imbalances that will, unless addressed by the General Assembly, lead to even greater and rapidly growing debts and deficits. Already, Illinois has the lowest credit rating of any state, and it faces the prospect of future credit downgrades that will further increase the high cost of borrowing."
> 2. b. "The State has taken significant action to address these fiscal troubles, including, but not limited to, increasing the income tax and reducing pension benefits for future employees. Further, the State has enacted a series of budgets over the last several fiscal years that resulted in deep cuts to important discretionary programs that are essential to the people of Illinois."
> 3. c. "[T]he State's retirement systems have unfunded actuarially accrued liabilities of approximately $100 billion."
> 4. d. "[W]ithout significant pension reform, the unfunded liability and the State's pension contribution will continue to grow, and further burden the fiscal stability of both the State and its retirement systems."
> 5. e. "Having considered other alternatives that would not involve changes to the retirement systems, the General Assembly has determined that the fiscal problems facing the State and its retirement systems cannot be solved without making some changes to the structure of the retirement systems. As a result, this amendatory Act requires more fiscal responsibility of the State, while minimizing the impact on current and retired State employees."

13. These legislative findings are reasonable and justified. They confirm and establish that the Act represents a reasonable and necessary means by the General Assembly to achieve an important public purpose.

14. The Act is presumed constitutional. The Act's presumption of constitutionality includes the reasonableness and necessity for its provisions in light of the circumstances faced by the State and the General Assembly when it was enacted.

15. In light of the magnitude of the pension problem and all of the other efforts the State has made to date, the Act represents a valid exercise of the State's reserved sovereign

powers to modify contractual rights and obligations, including contractual obligations of the State established under Article I, Section 16 and Article XII, Section 5 of the Illinois Constitution.

WHEREFORE, Defendants pray for entry of judgment in their favor and against the plaintiffs on all of their claims, and for such further relief as is warranted in the circumstances.

Date: May 15, 2014

Respectfully Submitted,

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IN THE CIRCUIT COURT FOR THE SEVENTH JUDICIAL CIRCUIT,
SANGAMON COUNTY, ILLINOIS

IN RE: PENSION REFORM LITIGATION	)	No. 2014 MR 1
	)	Hon. John W. Belz

This document relates to:	)	
	)	
RETIRED STATE EMPLOYEES ASSOCIATION,	)	
an Illinois not-for-profit corporation, and	)	
LAWRENCE WORT, GLADYS HAJEK,	)	
LINDA GUELDENER and MAURINE RICHTER,	)	
for themselves and on behalf of a class of persons	)	
similarly situated,	)	Originally Filed as
Plaintiffs,	)	Sangamon County Case
	)	
v.	)	
PATRICK QUINN, in his capacity of the Governor	)	No. 2014 MR 1
of the State of Illinois, JUDY BAAR TOPINKA,	)	
Comptroller of the State of Illinois,	)	
DAN RUTHERFORD, Treasurer of the State of	)	
Illinois, and the BOARD OF TRUSTEES OF THE	)	
STATE EMPLOYEES RETIREMENT SYSTEM,	)	
Defendants.	)	

NOTICE OF FILING

To: See attached Certificate of Service

PLEASE TAKE NOTICE that on the 15th day of May, 2014, the attached **ANSWER AND DEFENSES** was filed with the Clerk of the Circuit Court for the Seventh Judicial Circuit, Sangamon County, Illinois, at the Sangamon County Courthouse, 200 South Ninth Street, Springfield, Illinois 62701.

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CERTIFICATE OF SERVICE

I, Joshua Ratz, an attorney, hereby certify that on May 15, 2014, true and correct copies of the foregoing Answer and Defenses were served by email; and United States Mail, first class postage prepaid, upon all counsel of record as follows:

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