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1st District refuses to sanction 'side letter' pension spike

The 1st District Appellate Court recently considered a dispute between the city of Countryside, its police pension board and several city pensioners. The court's opinion clarifies how certain preretirement salary increases should be factored into pension calculations for municipal police and firefighters. The case is *City of Countryside v. the City of Countryside Police Pension Board of Trustees, et al.*, 2018 IL App (1st) 171029.

The events giving rise to the court's opinion date back to 2002 when the city and the police union entered into a collective bargaining agreement which defined "longevity benefit" as a one-time payment of \$800 (increasing to \$850) for officers meeting certain conditions, including a requirement that an officer have at least 20 years of service with the city.

The bargaining agreement also contained an integration clause. During contract negotiations, the city's labor attorney signed a "side letter" with the union's attorney outlining the parties' understanding of how the longevity benefit would be factored into an officer's wage base for pension purposes.

Specifically, the side letter provided that an officer's gross wage base for pension purposes was to be calculated by multiplying the one-time longevity benefit (\$800 or \$850) by 24 pay periods. In other words, the side letter provided that the parties would, for pension purposes, treat the one-time longevity benefit payment as though it had been received by the police officer every paycheck for the prior 24 pay periods.

The result, of course, was a final salary for pension purposes which was nearly \$20,000 higher than the officer's actual final salary. Neither the bargaining agreement nor the city's

resolution approving the agreement referenced the side letter.

This calculation method prevailed for a while, but as time passed and the city's administration questioned and scrutinized the legality of the side letter differences occurred.

In 2010, both the city and pension board sought advisory opinions from the Illinois Department of Insurance concerning the treatment of longevity payments under the Pension Code and the department's regulations.

The department is authorized by law to issue regulations and guidance on issues concerning municipal police and fire pension systems, and it concluded that only the initial payment of \$800 would be pensionable.

The city filed suit in 2012 against the pension board, the union and certain pensioners alleging that the side letter computation was illegal and that the board's use of the side letter created a systemic miscalculation of benefits.

After years of litigation and procedural maneuvering, the trial court granted summary judgment in favor of the city; the defendants appealed.

On appeal, the defendants argued, among other things, that

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the city and the union were free to collectively bargain for enhanced pension benefits, which are constitutionally protected from diminution, that the side letter created a binding contract, and that the Insurance Department's regulations interpreted the Pension Code in a way that was contrary to the Pension Code itself. The appellate court

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disagreed with the defendants' arguments and affirmed the trial court.

The appellate court's analysis began with a review of the operative statutes and related Insurance Department administrative regulations. The court looked at the definition of "salary" in Section 3-125.1 of the Pension Code before turning to an analysis of Insurance Department regulations concerning longevity benefits.

The department's regulation at Section 4402.35(d) of the Illinois Administrative Code provides that when longevity pay is made in one lump sum the payment should be prorated to determine the monthly equivalent for purposes of calculating a pension.

Defendants argued that this language contradicted the statutory definition which requires that an officer's pension be pegged specifically to the salary earned on the last paycheck, annualized. The court rejected the arguments of defendants and confirmed the validity of the state regulations, noting the absurdity that would result under

the defendants' interpretation.

For example, the court explained, a municipality and its employees' union could agree that on the last paycheck an officer would receive a longevity increase of \$100 for the officer's last hour of work.

Under the defendants' interpretation, the \$100 would be multiplied by 24 hours a day, and multiplied again by 365 days in a year to get a pensionable salary of \$876,000. Such an absurd result, held the court, could not have been the intent of the legislature.

Having found the state's regulations to be valid, the court next turned the legality of the side letter and whether the city's funding of the longevity benefit was proper. In finding the side letter unenforceable, the court noted that the side letter was never approved by the corporate authorities in any manner.

Furthermore, to be considered pensionable salary, extra payments (like the longevity benefit) must be duly appropriated by ordinance. The city's legislative leaders never appropriated the longevity bonus times 24 pay periods (\$800 x 24) for any of the retirees that received the benefit. Thus, for these reasons as well the side letter was of no force and effect.

The court rejected the affirmative defenses of the defendants, including the claim that the pension protection clause of the Illinois Constitution prevents the court from correcting the side letter pension calculation.

The court had none of the argument. "A host of individuals ... constructed a fictitious calculation method ... and used that method to award pensions far higher than those permitted by law" stated the court.

"The pension protection clause does not prevent the court from imposing a remedy to bring the retirees' pensions to the correct level ..."