

## Death of Illinois pension reform may breathe life into budget talks

By Andrew Scurria and Gunjan Banerji  
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Illinois is no longer trying to salvage a pension overhaul deemed unconstitutional by the state's highest court, something that may help jumpstart FY16 budget talks, according to public finance experts.

Illinois Attorney General Lisa Madigan had previously signaled a possible appeal to the US Supreme Court over the 2012 pension fix, which the Illinois Supreme Court struck down in May as a violation of the state constitution's pension protections. But her office confirmed late Wednesday (9 September), without explaining why, that it had elected not to file a writ petition.

The 10 September deadline for filing the papers fell in the midst of an epic budget stalemate between Governor Bruce Rauner (R) and the Democratic legislature.

"There's a lot to be said" for dropping the Supreme Court appeal, according to Mark Davis of O'Keefe Lyons & Hynes, who said it removes one big variable from the negotiating calculus. With compromise still elusive on labor reform, municipal bankruptcy and other issues, the standoff has raised the specter of a USD 8.5bn backlog of unpaid bills by the end of the calendar year, as reported.

"The Attorney General probably deserved a lot of credit for making a very responsible decision and accelerating the ability of all the other actors to act," Davis said. "That includes the people who are working on the budgets."

Waiting until late autumn to see if the Supreme Court granted review "would just complicate things," added Ronald Kramer, a labor attorney with Seyfarth Shaw.

"Somebody had to step back and say, if we're going to try to bridge any gaps politically here, we can't be going after the appeal," said Karol Denniston of Squire Patton Boggs. "There's only so much energy, so much time and so many fights that you can wage."

Illinois bonds did not move much. A USD 260m tranche of Series 2013 general obligation bonds issued by the state last traded yesterday (10 September) at 103.8 yielding 4.59%, slightly up from 103.1 yielding 5%, according to Electronic Municipal Market Access.

"I don't think this decision changed anything at all," said Illinois Senator Daniel Biss (D). "The State Supreme Court's ruling was very clear."

The Illinois Supreme Court is the ultimate interpreter of the Illinois constitution and deemed the pension clause as trumping police powers. While it was a worthwhile argument for the state to make, it may have been difficult, according to John Schomberg of Clark Hill, who said that the lack of an appeal may mean that lawmakers evaluate alternatives sooner rather than later. The state has a USD 111bn unfunded pension liability among its five state-funded retirement systems; they are 39.3% funded.

## **Legal finality clears the decks**

The pension litigation is unfolding against a budget impasse that has led to unevenness in state-supported programs; the human services sector is bearing the brunt, Biss said at an Illinois Senate committee hearing earlier this week. Meanwhile, pensions and debt service payments will automatically continue to be made, Biss said. Much of the state's expenditures are being made through consent decrees, court orders, or appropriation bills.

State Comptroller Leslie Geissler Munger said yesterday that without a balanced budget, Illinois' backlog of unpaid bills to schools, hospitals, businesses, social services, and other vendors will exceed USD 8.5bn by December and could be as high as USD 12.8bn.

This is an "unbelievable trifecta of tragedy," Biss said. "There is more money going out the door than is coming in." The parties making spending decisions are unelected and not designated to make budgetary decisions, Biss said.

A prolonged budget impasse reduces the state's flexibility in the long run, Schomberg and Biss said. Illinois currently has 80 consent decrees on the books, added Donovan Borvan, associate general counsel to the governor, at the hearing.

"Consent decrees don't go away; they tie the hands of the agencies going forward," Borvan said.

As more appropriations and consent decrees are enacted, room for the legislature to make cuts shrinks, Schomberg said. The state is now two months into the budget year, and any additional revenue the state may have tapped for FY16 to cover the year's expenses is already lost.

Spending is currently based on FY15 levels, while revenue is based on FY16 levels, which took a hit after the sunset of the temporary tax increase in January. Reducing spending quickly could mean closing facilities or laying off employees, which could spark lawsuits down the road, Schomberg said.

## **Pension jurisprudence still evolving**

Meanwhile, legal wrangling over the Illinois pension clause continues, with the state justices having agreed to consider the legality of the 2013 retirement overhaul enacted under Chicago Mayor Rahm Emanuel. Cook County Circuit Court Judge Rita Novak voided the city's reform in July. The strong jurisprudence against benefit impairments for midcareer workers also hangs over a pension proposal floated by Cook County. As in Chicago, holdouts to that negotiated agreement are threatening to sue.

In procedural papers filed with the Supreme Court, Madigan's office previewed her potential arguments around the so-called reserved powers doctrine. This refers to the idea that the US Constitution provides certain sovereign powers to the states and prohibits an interpretation of the Illinois pension clause that excludes those policing authorities, Davis said.

The decision's harsh indictment of the Illinois legislature's chronic pension underfunding was another reason not to seek Supreme Court review, said Peter Mixon of K&L Gates. The state justices found the current pension crisis to be one of the legislature's own making that could not justify the invocation of emergency police powers.

"An appeal might only serve to reinforce the decision," Mixon said.