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Illinois Launches Legal Argument for Pension Reform.

CHICAGO – Illinois acted within its sovereign authority in passing pension reforms given its precarious fiscal condition and the size of its unfunded pension obligations.

That's the heart of the state's initial legal defense of the pension legislation from Illinois Attorney General Lisa Madigan.

"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" under the Illinois constitution, say filings Illinois made Thursday.

Madigan filed the defense in response to a series of lawsuits seeking to overturn the December pension legislation as a violation of the state constitution which affords pension benefits strong contractual rights that cannot be impaired or diminished.

The lawsuits have been consolidated in Sangamon County Circuit Court, home of the state capital, and are being heard by Judge John W. Belz, though the Illinois Supreme Court is expected to have the final word.

Madigan's responses to each of the lawsuits includes a response to the dozens of assertions laid out by the plaintiffs, which include the union coalition We Are One Illinois and various associations that represent state employees and retirees. In many instances, the state simply denies legal assertions made in the lawsuits.

Madigan then takes the additional step in the filings of laying out the state's defense for adopting the pension changes, arguing they were both reasonable and necessary given the state's precarious financial position, the size of its unfunded liabilities, and the need to fund critical services. "The Act's limited changes to pensions were necessary to address these circumstances," the filings contend.

The filings lay out the roots of the state's financial deterioration and integral link to the rise in its unfunded pension obligations. Beginning around 2000 and continuing over the next decade the state's underfunding of the systems "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."

The filings outline steps taken by the state to improve its balance sheet and the pension system including the 2010 passage of legislation cutting pension benefits for new employees, an overhaul of its Medicaid system, spending cuts, and the 2011 enactment of a temporary income tax hike.

Those measures proved insufficient and the state's "credit rating continued to suffer, causing it to incur still higher costs to finance its debt, thereby further reducing" revenues for critical services and to reduce unfunded liabilities.

The filings draw much of the information on the state' fiscal struggles from a lengthy preamble to the legislation included by the attorney general's father, House Speaker Michael Madigan, D-Chicago.

The legislation limits cost-of-living increases, caps pensionable salaries, and raises the retirement age for some while cutting employee contributions by 1%, shifting contribution calculations to a more actuarially sound method, and gives the pension funds enforcement rights over state payments.

Much of the expected $140 billion of savings stem from the COLA increases annuitants now receive. The state filings target the existing automatic COLA as a key driver for the rising pension burden and argue those adjustments "are not part of the core pension benefit."

The state acknowledges that in past years the General Assembly failed to contribute sufficient funds to keep the system healthy, but also chides unions saying their past efforts to push wage increases came at the expense of greater pension contributions during tough fiscal times.

The state argues that the legislation provides "consideration" for the negative changes by stabilizing the pension system. The plaintiffs argue that pension benefits are protected by the state's pension clause, that the reforms violate the contract clause, and violate the constitution's takings clause that protects private property.

Belz on Thursday granted the plaintiffs' request to stay the June 1 implementation of the pension legislation. Rating agencies have said the state's weak credit rating could stabilize if the pension changes are eventually upheld and the state shores up its budget by extending a temporary income tax.

The state's rating has sunk over the last several two years to the A-minus level, the weakest among states due to its pension and budgetary strains. Two rating agencies assign a negative outlook and Standard & Poor's a "developing" outlook. The state has $100 billion of unfunded pension obligations.

The plaintiffs did not have an immediate reaction to the state attorney general's filings.

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