

**BEFORE THE BOARD OF TRUSTEES
TEACHERS' RETIREMENT SYSTEM OF THE STATE OF ILLINOIS**

In the Matter of:)
)
)
Gary Lester)
and Thornton Township)
High School Dist. No 205)
)
Petitioners)

RECOMMENDED DECISION OF THE CLAIMS HEARING COMMITTEE
IN THE ADMINISTRATIVE REVIEW OF
GARY LESTER AND THORNTON TOWNSHIP
HIGH SCHOOL DIST. NO 205

Introduction

Pursuant to 80 Ill. Adm. Code 1650.640(e), Petitioners Gary Lester (Lester) and Thornton Township High School Dist. No 205 (Thornton) agreed with the Teachers' Retirement System of the State of Illinois (TRS or the System) that their request for administrative review would be presented to the TRS Board of Trustees Claims Hearing Committee solely upon the record agreed to by the parties. The Claims Hearing Committee met on August 12, 2009 at TRS headquarters in Springfield. Present were Committee Chairman Cynthia O'Neill and Committee members Jan Cleveland and Janice Reedus. Lester and Thornton were represented by Andrew Malahowski of Franczek Radelet & Rose. The System was represented by Thomas Gray, its General Counsel.

Petitioners Lester and Thornton filed the instant administrative review to challenge the TRS staff determination that Thornton's \$59,735 check dated June 29, 2006, \$19, 503 of which was payable to Lester's 403(b) tax-sheltered annuity provider, AXA Equitable, was properly reportable to TRS as creditable earnings to Lester in the 2005-06 school year, and not in the 2006-07 school year. The

System's position is that the \$19,503 paid to Lester's 403(b) account was properly reportable to TRS as creditable earnings in the 2005-06 school year, not the 2006-07 school year. Under the Pension Code and TRS administrative rule governing the reporting of "salary" for TRS purposes, the check date of a lump sum payment determines the school year of creditable earnings reporting. Petitioners take the position that the date a check is cashed, i.e., the date of receipt, governs the school year of reporting.

After considering the pleadings of the parties and the agreed upon exhibits and stipulations contained in the Claims Hearing Packet, it is the Committee's recommendation to uphold the TRS staff determination that the \$19,503 paid by Thornton into Lester's 403(b) account was properly reportable as creditable earnings to Lester in the 2005-06 school year.

Findings

The parties stipulated to the following:

- a) TRS annuitant Gary Lester's TRS retirement date was July 1, 2008.
- b) Thornton, Lester's former employer, processed a check in the amount of \$59,755 to AXA Equitable, on June 29, 2006.
- c) Included within the \$59,755 payment was a \$19,503 contribution to Lester's AXA Equitable 403(b) account.
- d) Thornton made the \$19,503 contribution to Lester's 403(b) account in addition to the base salary that Lester received from Thornton.
- e) The \$59,755 payment, which included the \$19,503 contribution to Lester's 403(b) account, was paid out of Thornton's 2005-06 school year budget.
- f) Thornton originally reported the \$19,503 as "salary" to Lester in the 2005-06 school year.
- g) Thornton later filed with TRS an adjustment to earnings report dated July 14, 2008, seeking to have the \$19,503 re-allocated as "salary" to Lester in the 2006-07 school year.

- h) TRS denied Thornton's request to adjust Lester's "salary" in the 2006-07 school year, by letter dated November 21, 2008.
- i) Lester served as a principal in the Thornton School District through June 30, 2008. Lester was employed pursuant to a 2004-2008 Administrative Contract dated June 14, 2004 (the Contract). Lester received certain retirement benefits pursuant to the Contract, which incorporated a Retirement Package for Administrators dated April 21, 1999 (the Retirement Package).
- j) Pursuant to the Contract and Retirement Package, Lester was permitted to receive retirement incentive adjustments, and was further permitted to spread these retirement adjustments over a period of three years. Lester announced his retirement from the Thornton School District on June 7, 2004.
- k) The total amount of retirement adjustments due Lester under the Contract and Retirement Package was \$63,003. Lester announced his retirement early enough that he was permitted to spread the retirement adjustments over three years.
- l) \$18,000 in retirement adjustments was paid to Lester on or about December 22, 2005, and was properly reported to TRS for the 2005-2006 school year.
- m) \$19,503 in retirement adjustments were delivered to Lester's 403(b) provider the first week of July, 2006, and the check was cashed and deposited in Lester's 403(b) account on July 12, 2006.
- n) The final \$25,500 in retirement adjustments was paid to Lester on or about July 2, 2007, and was properly reported to TRS for the 2007-2008 school year.
- o) While the \$19,503 check intended for Lester's 403(b) account was processed by Thornton on June 29, 2006, it was retained in District offices and not delivered to either Lester or his 403(b) provider until after July 1, 2006.

- p) TRS stated in its November 21, 2008 letter to Thornton that the “date of the check” is the presumed date of payment but that this presumption can be rebutted.

Decision of the Claims Hearing Committee

The sole issue to be determined by the Claims Hearing Committee is whether to attribute the \$19,503 employer contribution to Lester’s 403(b) account as creditable earnings to Lester in the 2005-06 school year, or in the 2006-07 school year.

Thornton originally reported the \$19,503 contribution as TRS creditable earnings to Lester in the 2005-06 school year. Thereafter, Thornton filed an adjustment to earnings to re-report the \$19,503 in the 2006-07 school year.

40 ILCS 5/16-121 governs the reporting of “salary” for TRS purposes:

*“Salary”: The actual compensation received by a teacher during any school year and **recognized by the system in accordance with rules of the board.** For purposes of this Section, “school year” includes the regular school term plus any additional period for which a teacher is compensated and such compensation is **recognized by the rules of the board.** (Emphasis added).*

To interpret and effectuate 40 ILCS 5/16-121, the TRS Board of Trustees promulgated TRS Administrative Rule 1650.450. As far back as 1991, TRS Rule 1650.450 defined “salary” as:

*Any recognized emolument of value that is received, actually or **constructively**, by a member in consideration for services rendered as a teacher. (Emphasis added.)*

The current version of TRS Rule 1650.450(a) provides:

"Salary" means any form of creditable compensation received by a member in consideration of services rendered as a teacher, subject to all applicable limits and restrictions imposed on qualified plans under the Internal Revenue Code. "Salary"

*directly related to specific work performed during a school year is recognized on an accrual basis. Other creditable compensation is recognized on a cash basis. **The System reserves the right to determine the year of salary recognition.*** (Emphasis added.)

TRS administrative rules have the full force and effect of statute and must be interpreted in accordance with 40 ILCS 5/1-102, which provides:

Continuation of prior statutes. The provisions of this Code insofar as they are the same or substantially the same as those of any prior statute, shall be construed as a continuation of such prior statute and not as a new enactment.

Since the 1990's, staff has determined the proper reporting of lump sum payments is determined by the date the check is issued, not the date it is cashed (i.e. constructive receipt). The question, therefore, is whether Lester constructively received the \$19,503 from Thornton in the 2005-06 school year. For the following reasons, the Committee finds in the affirmative.

Lester's Contract contained the following relevant provisions:

Fringe Benefits include...

10. *An administrative Retirement Plan, as defined in the Board of Education action of April 15, 1999.*
11. *Administrator may elect that a portion of his compensation be used to purchase tax annuity of his own selection. It is understood and agreed that the cost of the purchase of said annuity shall not require an expenditure of funds by the Board above the amount paid to the Principal in the form of salary.*

As further stated in the Retirement Package:

1. *Final Year Salary* – *in their final year of service, a retiring administrator should receive a 1% increase in base salary for every year of service to the district; however, in no case will the increase be less than 20%. (Please remember that a retiring teacher receives a 20% increase, and therefore, the increase for administrators should not be less.)*

...

7. *The retirement increases could be spread over two years if the employee announced their retirement early enough and if they elected this option.*

Based upon the above contractual provisions, it is clear to the Committee that Thornton paid the \$19,503 to Lester's 403(b) account out of its 2005-06 school year budget. Lester was entitled to the \$19,503 at any time after he gave notice to retire by virtue of the Contract and the Retirement Plan. He directed the funds to AXA Equitable. Once the check was cut on June 29, 2006, it became Lester's money in that it was set apart for him. Therefore, Lester was in constructive receipt at that point, which was still in the 2005-06 School Year.

There is good reason for TRS to look to the check date to determine the school year in which lump sum payments are creditable. Unfortunately, salary reporting manipulation is a very real concern for TRS. Looking to the check date to determine the school year in which lump sum payments are creditable provides an objective standard which prevents such reporting manipulation.

Petitioners cite two cases for the proposition that Lester did not "receive" the funds until the June 29, 2006 check was cashed by AXA Equitable on July 12, 2007. The Committee finds neither case to be relevant or persuasive.

Consolidated Freightways v. Industrial Com., 48 Ill.2d 221 (1971), dealt with a claim for workers compensation benefits and whether the claimant timely filed his claim within the time period prescribed by law. While the court used the receipt date of the employer-paid benefit check to determine when the claim filing deadline ran out, the court's analysis is not relevant nor on point with respect to the TRS salary rule constructive receipt issue as to when earnings are creditable for TRS earnings credit purposes.

The Committee finds *Gillespie v. Riley Management Corp.*, 59 Ill.2d 211 (1974), to be distinguishable as well. In *Gillespie*, the court found that ownership of a cashiers check remains with the purchaser until delivery. However, *Gillespie* dealt with cashiers check ownership governed by the Uniform Commercial Code (UCC), which has absolutely no bearing on TRS creditable earnings. This matter presents a creditable earnings issue governed by the Illinois Pension Code. The *Gillespie* analysis of cashiers check ownership under the UCC is entirely irrelevant in this administrative review matter.

Petitioners also invoke 40 ILCS 5/16-192, Correction of Errors. As stated therein:

Should any change or error in the records result in any member, annuitant or beneficiary receiving from the system more or less than he or she would have been entitled to receive had the records been correct, the board shall correct such error, and, as far as practicable, shall adjust the payments in such a manner that the actuarial equivalent of the benefit to which such member, annuitant or beneficiary was entitled shall be paid; however, in no event shall the system be required to change the records of any member, annuitant or beneficiary if, at the time of discovery of the error, more than 4 fiscal years have elapsed since the fiscal year in which the error occurred.

However, the Correction of Errors provision is irrelevant in Lester's case, because there was no error in reporting. Thornton properly reported the \$19,503 in the 2005-06 school year. All that has been established by Thornton is that Lester would have received a higher pension benefit if Thornton were allowed to re-report the \$19,503 in the 2006-07 school year. Such manipulation of creditable earnings to maximize a retirement benefit does not qualify as "correction of errors" and is simply not permissible under the law.

Conclusion

The Committee finds that the \$19,503 payment made by Thornton on behalf of Lester to AXA Equitable by check dated June 30, 2006, was properly reportable in the 2005-06 school year. Accordingly, the Committee upholds the TRS staff determination in this matter.

Notice of Right to File Exceptions

Exceptions to the Claims Hearing Committee's Recommended Decision must be filed within 15 days of receipt by the Petitioner. A Final Decision will be issued by the Board of Trustees after it has considered the Claims Hearing Committee's Recommended Decision and any exceptions filed by the Petitioner.