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

	)
In the Matter of:	)
	)
Mary Adams	)
	)
Petitioner	)

RECOMMENDED DECISION OF THE CLAIMS HEARING COMMITTEE IN THE ADMINISTRATIVE REVIEW OF MARY ADAMS

I. Introduction

Pursuant to 80 Ill. Adm. Code 1650.640(e), Petitioner Mary Adams (Adams) agreed with the Teachers' Retirement System of the State of Illinois (TRS or the System) that her request for administrative review would be presented to the Claims Hearing Committee of the TRS Board of Trustees solely upon the record agreed to by the parties. The Claims Hearing Committee met on August 12, 2009 at TRS Springfield offices. Present were Committee Chairman Cynthia O'Neill, Committee members Jan Cleveland and Janice Reedus and Ralph H. Loewenstein, as presiding hearing officer. Adams was represented by Shari Rhode of Rhode & Jackson, P.C. The System was represented by Scott Spooner of Heyl, Royster, Volker & Allen.

Adams filed this administrative review to challenge the TRS staff determination that creditable earnings for Adams serving as Director of Project Echo with the Franklin-Williamson Regional Office of Education should be reduced by the amount of kickbacks that Adams paid to Regional Superintendent Barry Kohl for appointing her to the Director's position.

After considering the pleadings of the parties and the agreed-upon exhibits and stipulations contained in the Claims Hearing Packet, the Committee finds that none of the earnings received by Adams for serving as Director of Project Echo are creditable for TRS retirement benefit purposes.

II. Stipulated Facts

1. Petitioner Mary Ann Adams (Adams) was employed at the Franklin-Williamson Regional Office of Education (Regional Office) between 1991 and 2005.

2. Between September 1999 and August 2004, Barry Kohl (Kohl) was the Superintendent of the Regional Office.

3. In the summer of 1999, Adams' annual salary from her employment at the Regional Office was between $50,000 and $55,000.

4. In the summer of 1999, Adams asked Kohl for a pay raise.

5. Kohl agreed to Adams' request for a pay raise, on the condition that she pay over to him one half of the net (i.e. after-tax proceeds of her pay raise) on a monthly basis.

6. Between September 15, 1999 and June 15, 2004, Adams received the salary she had previously been paid for her employment at the Regional Office, together with the pay raise she requested and received from Kohl.

7. Between September 15, 1999 and June 15, 2004 (a period 58 months, or four years 10 months), Adams cashed one of the two paychecks she received as a raise and delivered the proceeds to Kohl.

8. On two occasions, Adams handed the agreed monthly payment to Kohl's wife, Janine Kohl.

9. Between September 15, 1999 and June 15, 2004, Adams was the Director of Project Echo.

10. Between September 15, 1999 and June 15, 2004, Judy Davis (Davis) was the Assistant Director of Project Echo.

11. On an unspecified date either in calendar year 2002 or calendar year 2003, Adams spoke with Kohl about Davis' need for additional money.

12. Kohl responded by asking Adams to talk with Davis about an arrangement similar to the kickback arrangement with Adams.

13. Adams spoke to Davis about Kohl's proposal and Davis agreed.

14. Davis made monthly payments to Kohl on the 30^{th} day of each month by placing the cashed proceeds of one of two paychecks she received as a raise beneath the blotter of her desk at the Project Echo headquarters in Johnston City, Illinois.

15. On two occasions, Davis gave Adams an envelope to give to Kohl as part of Davis' payments to Kohl.

16. Adams stopped making payments to Kohl in June 2004.

17. Between September 1999 and June 2004, Adams never reported to law enforcement personnel her payments to Kohl.

18. Between September 1999 and June 2004, Adams understood she was a public employee of the Regional Office.

19. Between September 1999 and June 2004, Adams understood that the salaried compensation she received for her public employment was funded by and with public monies.

20. Adams claims she was given additional duties on or before the time she asked for a pay raise.

21. TRS has no evidence that Adams did not perform additional duties for the pay raises she received in any year.

22. TRS has no information that Adams was convicted of a felony.

23. TRS has no information that Adams was convicted of a misdemeanor.

24. TRS has no information that Adams was charged with any official misconduct related to her employment with the Regional Office.

25. TRS has no information that Adams was convicted regarding misconduct related to her employment with Regional Office.

26. TRS's August 19, 2008 letter to Ms. Adams signed by Lori Dour explains the basis on which TRS adjusted Adams' monthly annuity and the claimed overpayment for the period May 26, 2005 through July 31, 2008.

27. Adams' last day of work was May 25, 2005.

28. Barry and Janine Kohl were convicted of felonies related to their employment with the Regional Office.

29. Barry Kohl was convicted of a felony related to official misconduct concerning his employment with the Regional Office.

30. TRS invoked the felony forfeiture provision of its governing law to terminate Kohl's retirement annuity following his felony conviction.

III. <u>Analysis</u>

The first issue the Claims Hearing Committee must resolve is whether the earnings Adams received as Director of Project Echo, qualify as "salary" for TRS pension purposes. As stated in 40 ILCS 5/16-121:

> *"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.)

As stated in pertinent part in TRS rule 80 ILAC 1650.450(a):

> *"Salary" means any form of creditable compensation received by a member* ***in consideration of services rendered as a teacher…*** (Emphasis added.)

By her own admission in Stipulated Fact 5, in her testimony before the grand jury, and her deposition of March 31, 2009, Adams was paid extra compensation, not for services rendered as Director of Project Echo, but in consideration for the kickbacks she agreed to pay to Regional Superintendent Kohl. Adams has the burden of proof in this administrative review. She failed to prove that she actually assumed additional duties or that even if she did, the consideration for the pay raise was for anything other than the kickbacks she agreed to pay to Kohl.

Adams' assertion that an auditor of the Auditor General's Office told her in 2003 that he would not do her job for what she was being paid, is legally irrelevant and unsupported by any evidence. Even assuming, *arguendo,* that such a statement was made, Adams failed to advise the auditor of her kickback arrangement with Kohl. There is no reason to believe that the auditor would have made such a statement if he had known the true circumstances of the compensation arrangement.

Adams makes several additional arguments why the compensation she received for her work as director of the Echo project should be considered to be "salary". First, she argues that she is entitled to spend her income as she saw fit whether it was to place illegal bets, buy illegal drugs or pay a portion of her income to Kohl. The problem with this argument is that it was not how she spent the money that caused it not to be "salary", it is how she came to earn the compensation. She was paid the additional stipend not because she assumed extra duties, but because she agreed to pay a kickback to Mr. Kohl.

Her second argument that she earned the salary by being a good employee and performing her duties satisfactorily fails for the same reason. She was not paid the additional compensation for her work or for assuming extra duties. She was paid this compensation because of the kickback scheme she entered into with Mr. Kohl.

Her third argument is that there was no evidence that her employer lacked the authority to pay her a salary increase. While under most circumstances this might be true, he did lack the authority to pay a salary increase in exchange for Adams paying a portion of that increase back to him. Ultimately, he pled guilty to this arrangement further emphasizing just how much he lacked the authority to do what he did.

Finally, Adams maintains that she was entitled to count the income as creditable earnings because she paid taxes on the earnings. Payment of taxes on ill-gotten gains does not convert it to salary. Salary for TRS purposes is not synonymous with taxable income.

Based upon the foregoing, the Committee finds that all compensation made to Adams over and above her regular salary while she was paying kickbacks to

Kohl is not "salary" under 40 ILCS 5/16-121 and TRS Rule 1650.450, because the consideration for Adams' earnings as Director of Project Echo were not for the services she rendered, but the kickbacks she paid to Kohl.

The second issue is whether a constructive trust should be imposed to prevent Adams from benefiting from the increase in her retirement annuity resulting from her kickback scheme. A constructive trust is an equitable remedy to keep a person from being unjustly enriched from a breach of fiduciary duty, Tarpoff v. Karandjeff, 51 Ill.App.2d 454, 201 N.E.2d 549 (1964).

The constructive trust doctrine was first imposed in a public corruption case in County of Cook v. Barrett, 36 Ill.App.3d 623, 344 N.E.2d 540 (1975). Barrett was the Clerk of Cook County. While serving in this capacity he took bribes to rent voting machines from and place insurance with certain vendors. The County sought to impose a constructive trust and recover the amount of the bribes.

The Court found that Barrett, as a public official owed a duty of loyalty and good faith to the public. If the agent (in this case Barrett) received a bribe from a party with whom he transacted business on behalf of the County, the County had a right to recover those profits. It was not necessary for the County to prove any actual loss to make a recovery or impose a constructive trust.

The Court quoted with approval from the Supreme Court case of United States v. Carter, 217 US 286 (1910),

'It is immaterial…whether the complaint was able to show any specific abuse of discretion, or whether it was able to show that it had suffered any actual loss by fraud or otherwise***…It would be a dangerous precedent to lay down as law that unless some affirmative fraud or loss can be shown, the agent may hold on to any secret benefit he may be able to make out of his agency. The larger interests of public justice will not tolerate, under any circumstances, that a public official shall retain any profit or advantage which he may realize through the acquirement of an interest in conflict with his fidelity as an agent'…The absence of an allegation of damages is immaterial.*** A constructive trust is not an action for 'recovery' or compensation under any theory of contract or tort. It is a strict equitable doctrine applied to cure a fiduciary's breach of is duty of loyalty by erasing the source of is conflict of interest, and transferring it to the innocent beneficiary. Bad faith is not an essential element of disloyalty [citation] and good faith is no defense to the charge. ***Courts are not interested in a fiduciary's particular motive for accepting a payment or gift but rather with the general***

effect of actual damage to the beneficiary. [Citation.] (Emphasis added.), 36 Ill.App.3d at 631-2.

The constructive trust doctrine involving public corruption was expanded beyond a person who held public office in Village of Wheeling v. Stavros, 89 Ill.App.3d 450, 411 N.E.2d 1067 (1980). Stavros took money from a construction company to obtain building permits and zoning changes from the Village. He then used his influence with certain Village officials and employees to obtain favorable rulings, even though he was not himself a public official or employee.

The Village sued to impose a constructive trust and recover the payments. The Court held that it was not necessary to prove the existence of a fiduciary duty or relationship to impose a constructive trust,

> "Stavros is incorrect in assuming that a constructive trust may only be imposed when there is fraud or the breach of a fiduciary relationship. A constructive trust is by no means restricted to those grounds. (citation omitted) The particular circumstances in which equity will impress a constructive trust are as numerous as the modes by which property may be obtained through bad faith and unconscionable acts. (citation omitted) A constructive trust is imposed by a court because the person holding title to property would profit by a wrong or would be unjustly enriched if he were permitted to keep the property.", 89 Ill.App.3d at 454.

The imposition of the constructive trust and recovery of funds is not limited to the person who committed the offense. In County of Cook v. Warren Motors, Inc., 114 Ill2d 305, 500 N.E.2d 22 (1986), the Supreme Court approved the application of the constructive trust argument regarding a party who paid bribes for the reduction of property taxes. The fact that the defendant colluded with a public official to induce the public official to breach his fiduciary duty was sufficient. Also see City of Chicago v. Keane, 64 Ill.2d 559, 357 N.E.2d 452 (1976); Chicago Park District v. Kenroy, Inc., 107 Ill.App.3d 222, 437 N.E.2d 783 (1982).

Adams was a public employee who breached her fiduciary duty to the public by participating in a kickback scheme with Kohl. In 2002, Adams also began participating in a separate kickback scheme involving her co-worker Judy Davis, a further breach of fiduciary duty. Adams was unjustly enriched by her kickback arrangement for which she received earnings she would not otherwise have received (see Stipulated Fact 5), and further unjustly enriched by her attempt to have those earnings count toward her TRS pension.

The fact that Adams did not have a direct fiduciary relationship with TRS does not prevent imposition of a constructive trust, as established by case law cited above. While it is up to the Regional Office of Education to decide whether to seek repayment of the earnings in question, it is the responsibility of the System to recoup the annuity payments to which Adams was not entitled, and to cease further annuity payments resulting from her unjust enrichment.

For these reasons, constructive trust should be imposed to prevent Adams from increasing her retirement annuity as a result of her participation in a kickback scheme.

IV. Conclusion

The Committee finds that, but for her kickbacks to Kohl, Adams would not have received the salary raise and enhanced pension benefits.

Based on the foregoing, the Committee recommends that the staff determination disallowing the following amounts as creditable earnings to Adams be upheld. Associated TRS contributions are included in each annual reduction.

1999-00	$24,175.82
2000-02	$24,175.82
2001-02	$24,175.82
2002-03	$24,175.82
2003-04	$26,813.19

The Claims Hearing Committee recommends that the staff reduce Adam's monthly annuity from $5,426.66 to $4,175.14. It is further recommended that, pursuant to 40 ILCS 5/16-172 and 80 Ill. Adm. 1650.595, staff recover all overpayments to Adams.

V. 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 TRS Board of Trustees after it has considered the Claims Hearing Committee's Recommended Decision and any exceptions filed by the Petitioner.