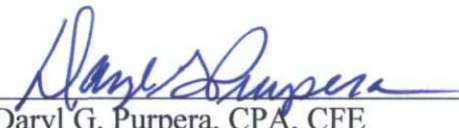




LOUISIANA LEGISLATIVE AUDITOR
DARYL G. PURPERA, CPA, CFE

In accord with my constitutional and statutory responsibilities, I requested that the attached legal analysis be done to assist me in the preparation of actuarial notes for pension bills being considered this 2012 Regular Legislative Session.



Daryl G. Purpera, CPA, CFE
Legislative Auditor
March 28, 2012

Strasburger

ATTORNEYS AT LAW

Memorandum

	Date March 26, 2012
To Office of the Louisiana Legislative Auditor Jenifer Schaye	From Gary B. Lawson A.D. (Gus) Fields
Re Likelihood of Litigation Resulting from Proposed Legislation Affecting Public Pension Benefits	

I. EXECUTIVE SUMMARY

This memorandum addresses potential legal and constitutional challenges facing public pension system bills currently pending in the Louisiana House and Senate.¹ As currently drafted, these bills propose to (1) increase the minimum retirement age, (2) increase employee contributions, (3) increase the number of years used to calculate final employee average compensation, and (4) merge two independent public retirement systems. We present our assessment of the likelihood that certain anticipated challenges addressed herein would succeed. We base our assessment upon relevant Louisiana court decisions, where applicable, as well as case law from other jurisdictions that have experienced similar challenges to public pension legislation.

The proposed legislation poses issues under both the United States and Louisiana Constitutions. Litigation would likely ensue in state as opposed to federal court due to Eleventh Amendment restrictions upon suing states in federal courts. But exceptions to the Eleventh Amendment restrictions could allow plaintiffs to bring suit in federal court under certain circumstances.

The challenges would most likely allege violations under: (1) Article X, § 29 of the Louisiana Constitution, which protects public pension benefits, (2) the Contract Clause within both the Louisiana and U.S. Constitutions² (claiming contract impairment due to diminished benefits); (3) the Takings Clause of both the Louisiana and U.S. Constitutions³ (for divesting public employee benefits without just compensation); (4) the Due Process Clauses of both the Louisiana Constitution⁴ and the Fifth Amendment to the U.S. Constitution (for depriving employees' of property rights without due

¹ The bills, discussed further in Part II B, are HB 53/SB 51, HB 56/SB 52, HB 55/SB 42, 47, HB 60/SB 46, 56)

² LA CONST Art I, § 23, U.S. CONST Art I, § 10

³ LA CONST Art I, § 4, cal 2, U.S CONST AMEND V

⁴ LA CONST Art I, § 2

Strasburger & Price, LLP

process); and (5) 42 U.S.C. § 1983 against public officials for enforcing unconstitutional laws.

The pending public pension bills are most vulnerable to both U.S. and Louisiana constitutional Contract Clause scrutiny, though the other potential challenges have significant merit as well. As currently drafted, each bill, except the one merging two pension systems, retroactively impairs or diminishes accrued pension benefits contrary to the guarantees in Article X, § 29. Courts must determine whether the proposed changes affect plan members and retirees retroactively or only impact future benefits. Case law from other jurisdictions demonstrates that changes to members' retirement age, contribution rate, and final average compensation formula retroactively affect members who have accrued and vested benefits based on their past service. Consequently, a reasonable likelihood exists that these bills as currently drafted will not survive constitutional scrutiny.

The bills proposing to merge two differently funded pension systems⁵ at this point seek only a merger of administrative functions and thus do not in our opinion pose any immediate constitutional risks. These bills do, however, contain a directive to study a future merger of plan assets, suggesting the legislature's intent to merge the funding aspects of the two systems in the not too distant future. Any such merger attempt could, in contrast, raise the likelihood of being challenged as unconstitutional. This would have a negative effect on the actuarial soundness of the disparately funded system, which is guaranteed by Article X, § 29.

Therefore, we conclude that House Bills 53, 55, 56, and Senate Bills 51, 52, 42, and 47, in their current form, face a likelihood of being challenged in the courts. If such challenges occur, we think it more likely than not that a court will rule such then-adopted bills as unconstitutional to the degree such bills affect the accrued benefits of current members and retirees.

II. POTENTIAL CONSTITUTIONAL CHALLENGES

1. THRESHOLD JURISDICTIONAL DECISION: FEDERAL OR STATE COURT?

A potential plaintiff must first determine where to file suit. Constitutional limitations on suing states in federal court often lead plaintiffs to file such suits in state court. But depending on the nature of the action and relief sought, a plaintiff could sue in federal court.

A. Effect of the Eleventh Amendment on Potential Lawsuits

Plaintiffs have challenged prior pension legislation in both state and federal court. But pension plaintiffs face certain limitations in federal court because the Eleventh

⁵ HB 60, SBs 46, 56

Amendment provides states with sovereign immunity from suit in federal court, subject to certain exceptions. This effectively limits a federal court's subject matter jurisdiction over claims by citizens against states, except in certain situations. *E.g.*, *Atascadero State Hosp. v. Scanlon*, 473 U.S. 234, 238 (1985); *Myers v. Tex.*, 410 F.3d 236, 240 (5th Cir. 2005).

Eleventh Amendment immunity from suit generally protects the state and any governmental entity considered to be an "arm of the state." *Vogt v. Bd. of Comm'rs*, 294 F.3d 684, 692-93 (5th Cir. 2002). Whether a governmental entity is an "arm of the state" for Eleventh Amendment purposes involves a multi-factor analysis, but usually does not include municipalities and distinct political subdivisions that operate with some degree of autonomy and are not significantly reliant on state funding. *See id.*

If applicable, Eleventh Amendment immunity generally prohibits federal court actions against a state in which a plaintiff seeks relief that is retroactive in nature. *Edelman v. Jordan*, 415 U.S. 651, 678 (1974). Eleventh Amendment immunity may be waived (1) by Congress under its exercise of power to enforce the Fourteenth Amendment or (2) by voluntary consent by the state. *E.g.*, *Myers v. Tex.*, 410 F.3d 236, 240 (5th Cir. 2005).

An exception to Eleventh Amendment immunity also exists under the U.S. Supreme Court's opinion in *Ex Parte Young*, which allowed a federal court suit action against state officials to proceed because the plaintiffs sought purely prospective injunctive relief. *Ex Parte Young*, 209 U.S. 123, 168 (1908); *Myers*, 410 F.3d at 240. In particular, the *Ex Parte Young* exception allows a federal court, consistent with the Eleventh Amendment, to "enjoin state officials to conform their future conduct to the requirements of federal law, even though such an injunction may have an ancillary effect on the state treasury." *Quern v. Jordan*, 440 U.S. 332, 337 (1979).

In suits seeking to have a state statute declared unconstitutional or to enjoin its enforcement, the officer of a state, including its governor, may be an appropriate defendant provided he has some connection with the act's enforcement. *Shell Oil Co. v. Noel*, 608 F.2d 208, 211 (1st Cir. 1979) (citing *Ex Parte Young*). In one case, the U.S. Supreme Court found the governor and secretary of state were proper federal court defendants because of their "general supervision" over the allegedly unconstitutional state actions. *Papasan v. Allain*, 478 U.S. 265, 282 n.14 (1986). Some past challenges to pension legislation have successfully proceeded in federal court. *See, e.g.*, *Parker v. Wakelin*, 123 F.3d 1 (1st Cir. 1997); *Professional Firefighters of Mass. v. Patrick*, No. 09-CV-11137 (D. Mass. 2009); *Marvel v. Dannemann*, 490 F. Supp. 170, 177 (D. Del. 1980).

Recently, however, a New Jersey federal district court was reluctant to hear claims against the state that involved public pension system changes, even though the plaintiffs sought prospective injunctive relief. The plaintiffs challenged legislation that suspended cost of living adjustments (COLA) and increased employee contribution

rates. *N.J. Ed. Ass'n v. State*, No. 11-5024 (March 5, 2012) (ECF No. 37). Plaintiffs claimed that Eleventh Amendment immunity did not apply because they sought only prospective injunctive relief to stop state officials from enforcing the pension legislation.

The court, however, disagreed and dismissed plaintiffs' claims. While the court noted it was a difficult decision, it ultimately concluded that the suit sought retroactive relief, because the enactment of legislation suspending COLA benefits for current and future retirees was a "single act" with "continuing ill-effects," and not a continuous violation of plaintiff's constitutional rights (for which a plaintiff can seek federal court relief under *Ex Parte Young*). The court found that plaintiff's claims were "nothing more than an indirect way of making the state abide by its obligations as they existed prior to the enactment of the [new legislation]." Thus, the court held that the Eleventh Amendment barred the requested relief because plaintiffs sought specific performance of the contract that existed *prior* to the new legislation; and not purely prospective relief.

B. Conclusion

This recent New Jersey opinion might lead a plaintiff to hesitate before challenging legislative changes to pension benefits in Louisiana federal district court, and to instead look to the state courts for relief. However, the New Jersey court admitted that the decision was a close one. Previous cases that found an *Ex Parte Young* exception plaintiffs may believe that they have a reasonable chance at securing jurisdiction in federal court if they only seek injunctive relief.

2. POTENTIAL LEGAL CHALLENGES TO PROPOSED LEGISLATION

A. Constitutional Issues Raised by the Proposed Legislation

The proposed bills pending before the Louisiana House and Senate that affect public pension benefits face potential legal challenges under both the Louisiana Constitution and the U.S. Constitution, with particular scrutiny arising under the "Contract Clause" in both Constitutions. LA. CONST. ART. 1, § 23; U.S. CONST. ART. I, § 10.

i. Louisiana Constitution, Article X, Section 29

Louisiana Constitution Article X, Section 29(B) makes membership in a state retirement system a contract between the members and the employer:

Membership in any retirement system of the state or of a political subdivision thereof shall be a contractual relationship between employee and employer, and the state shall guarantee benefits payable to a member of a state retirement system or retiree or to his lawful beneficiary upon his death.

The specific terms of that contract determine the scope of the constitutional protection. State statutes and the state constitution provide that an employee's pension and the

state's contribution to that pension are part of his compensation for employment services rendered. See *Groves v Bd. of Trustees*, 324 So. 2d 587, 596 (La. App. 1 Cir. 1976). Article X, Section 29(E)(5) also provides:

The accrued benefits of members of any state or statewide public retirement system shall not be diminished or impaired.

Article X, Section 29 creates grounds for challenging legislation affecting "accrued benefits" primarily under the Contract Clause of the state and U.S. Constitutions,⁶ but also under the state and federal Takings Clause,⁷ the Due Process Clause of the Fifth Amendment to the U.S. Constitution, and 42 U.S.C. § 1983.

ii. Violation of the State and Federal Contract Clauses

Louisiana's Constitution Article I, Section 23, follows the provisions of U.S. Constitution Article I, Section 10 by prohibiting any law that impairs the obligation of contracts, providing:

No bill of attainder, ex post facto law, or law impairing the obligation of contracts shall be enacted.

Louisiana clearly distinguishes impairment of private rights from those actions impairing governmental rights. The state may lawfully impair its own contractual rights as long as it does not infringe upon private rights. *Rousselle v. Plaquemines Parish Sch. Bd*, 633 So. 2d 1235 (La. 1994).

Louisiana courts employ a four part test to determine whether a contract violates the state and U.S. constitutional prohibitions on impairing the obligations of contracts:

- (1) the reviewing court must determine whether the state law would, in fact, impair a contractual relationship;
- (2) if the court finds impairment, it must determine whether the impairment is of constitutional dimensions;
- (3) if the state regulation constitutes a substantial impairment, the court must determine whether a significant and legitimate public purpose justifies the regulation; and finally,
- (4) if a significant and legitimate public purpose exists, the court then determines whether the adjustment to the rights and responsibilities of the contracting parties is based upon reasonable conditions and is of a

⁶ LA CONST. Art. 1, § 23, U S CONST Art. I, § 10.

⁷ LA. CONST. Art I, § 4, cal. 2, U S CONST Amend V

character appropriate to the public purpose justifying the legislation's adoption.

Segura v. Frank, 630 So. 2d 714, 728-29 (La. 1994); *Bd. of Comm'rs of Orleans Levee Dist v. Dept. of Natural Res.*, 496 So. 2d 281 (La. 1986).

Courts will defer to the Legislature when dealing with economic regulation between private parties. However, such complete deference is not appropriate when the state is a party to a contract because its own self-interest is at stake, as are its obligations of contract under Article X, Section 29. *Id.* at 293. This approach is consistent with the U.S. Supreme Court jurisprudence interpreting the federal non-impairment of contracts provision. In *U.S. Trust v. New Jersey*, 97 S.Ct. 1505 (1976), the Supreme Court held that if contract rights are taken for some public benefit, there must be just compensation paid. Legislation will be treated as a contract when its plain language evinces an intent to create privately enforceable rights. "A state may not refuse to meet its legitimate financial obligations simply because it would prefer to spend the money to promote the public good rather than the private welfare of its creditors." *Id.* at 1521.

Based upon the high value that the framers of both the state and U.S. Constitutions placed on the enforceability of contracts—as evidenced in Supreme Court opinions such as *U.S. Trust and Allied Structural Steel v. Spannaus*, 438 U.S. 234, 249-50. (1978)—the state must overcome a significant burden to justify drastic changes in contractual pension benefits. Simple presumptions of reasonableness or necessity, which are the core of legislative deference, cannot stand. See *Spannaus*, 438 U.S. at 249-50. Further, under Louisiana law, retroactive application of new legislation is constitutionally permissible *only* if it does not result in the impairment of the obligation of contracts or the divestiture of vested rights. 2 A. N. Yiannopoulos, *Louisiana Civil Law Treatise*, Section 10 (3d ed. 1991), cited with approval in *Bourgeois v. A. P. Green Indus., Inc.*, 783 So. 2d 1252 (La. 2001).

iii. Violation of the State and Federal Takings Clauses

The "Takings" clauses of the United States and Louisiana Constitutions state as follows, respectively:

...[N]or shall private property be taken for public use, without just compensation. U.S. CONST. Amend. V.

Property shall not be taken or damaged by the state or its political subdivisions except for public purposes and with just compensation paid to the owner or into court for his benefit LA. CONST. Art 1, § 4(B)(1).

In order to establish a cognizable takings claim, plaintiffs must establish that they have a protectable property interest in pension benefits, which, for purposes of the Takings Clause, includes a valid contract. See e.g., *Ruckelshaus v. Monsanto Co.*, 467 U.S.

986, 1003 (1984). Louisiana courts have held that one's right to retirement funds constitutes a property right. *Hare v. Hodgins*, 586 So. 2d 118 (La. 1991); *Parochial Employees' Retirement System v. Caddo Parish Commission*, 676 So. 2d 105 (La. App. 1 Cir. 1996). A cut in government retirement benefits may constitute an abridgement of a property right. See *Phillips v. Wash. Legal Found.*, 524 U.S. 156 (1998).

The constitutional prohibition against governmental expropriation of private property applies only when the property has been taken for a public purpose. See generally L. Tribe, *American Constitutional Law*, § 9-2 (1978). When pension plan changes are enacted for the purpose of maintaining the plan's actuarial integrity, some courts hold that the action benefits the plan contributors, and not the public, within the meaning of the constitution. See *Steven v. Bd. of Trustees of the Police Pen. Fund of Shreveport*, 3790 So. 2d 528, 531 (La. 1979). We do not think a court would likely sustain an argument that the proposed pension changes in the bills discussed herein as currently drafted would meet the express standard mentioned above.

iv. Violation of the State and Federal Due Process Clauses

The Fifth Amendment to the U.S. Constitution provides, in pertinent part:

No person shall ... be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation. U.S. CONST. AMEND V.

The Fourteenth Amendment makes the protections afforded by the Fifth Amendment applicable to the states by providing:

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws. U.S. CONST. AMEND XIV, § 1.

Louisiana Constitution Article I, § 2 similarly provides:

no person shall be deprived of life, liberty, or property, except by due process of law.

Louisiana courts have interpreted this state protection as consistent with the Fifth Amendment. See *Hare v. Hodgins*, 586 So. 2d 118 (La. 1991); *Parochial Emp.s' Ret. Sys. v. Caddo Parish Comm'n*, 676 So. 2d 105 (La. App. 1 Cir. 1996).

Plaintiffs may assert that legislation affecting pension benefits violates procedural due process by showing that the legislation has affected their property interests without any

rational basis or rational relationship to its stated purpose. See *Parker v. Wakelin*, 882 F. Supp. 1131 (D. Me. 1995). This claim usually depends upon showing a non-forfeitable contractual right. *Bd. of Regents v. Roth*, 408 U.S. 564 (1972).

v. Violation of 42 U.S.C. § 1983

Parties may pursue claims under 42 U.S.C. § 1983 against an official (for enforcing unconstitutional laws) particularly when seeking injunctive relief. 42 U.S.C. § 1983 provides:

Every person who, under color of any statute, ordinance, regulation, custom, or usage of any State...subjects, or causes to be subjected, any citizen of the United States...to the deprivation of any rights privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law, suit in equity, or other proper proceeding for redress...

Plaintiffs often include constitutional claims against the public officials responsible for the act in question, when suing to restore public pensions. However, the sovereign immunity doctrine precludes Section 1983 claims against the state itself. Moreover, monetary damages may not be recovered as to any defendant sued in an "official capacity." See *Will v. Mich. Dep't of State Police*, 491 U.S. 58, 71, 109 S. Ct. 2304 (1989). Accordingly, prospective injunctive relief is often the only remedy in a Section 1983 action. However, since a successful plaintiff may recover statutory attorneys' fees in such a Section 1983 action upon obtaining injunctive relief, such claims are often included. See 42 U.S. § 1988; *Pulliam v. Allen*, 466 U.S. 522, 543-44 (1984).

**B. Specific Challenges to Individual Pension Bills Currently Pending
Before the Louisiana Legislature**

The following discussion addresses potential legal challenges to the specific pension-related bills currently pending before the Louisiana House and Senate. Because the specific language within these bills may change, the discussion focuses topically on the proposed revisions.

A potential question exists regarding when retirement system member benefits "accrue" or "vest" under Article X, § 29(E). Louisiana law on this issue is not yet well developed. Some Louisiana cases (e.g., *Smith v. Board of Trustees of LASERS*, 851 So. 2d 1000 (La. 2003)) have summarily touched on this issue, and we will address these cases below in Part II.C. Cases from other jurisdictions addressing "accrued" and/or "vested" benefits particular to those states are discussed below in Part III.

i. Change in Retirement Age (HB 53/SB 51)

HB 53 and SB 51 seek to increase the minimum retirement age to 67 for new members and actuarially reduce the benefits of any current members who retire before age 67. There is no constitutional prohibition to increasing the minimum retirement age for new workers hired for the first time on or after the statute's effective date. Current employees, however, will likely challenge the constitutionality of any retirement age increases since it has the direct effect of reducing the benefits they receive if they retire before the newly proposed unreduced benefit at age 67.

Louisiana courts have not addressed whether increasing the retirement age is constitutional under Article X of the Louisiana constitution or any other state or federal constitutional provisions. However, case law that predates the current Louisiana constitutional provisions upheld such a retirement age increase as to those employees that had not yet attained retirement eligibility. See, e.g., *Bowen v. Board of Trustees Police Pension Fund*, 706 So. 2d 430 (La. 1954). Those seeking to distinguish *Bowen* and its progeny will not only point to the significant constitutional changes in the interim, but also to significant shift in how courts view pension benefits. The former notion that pension benefits were a voluntary gift from the employer (and thus subject to revision or termination at the employer's sole discretion) has since yielded to an understanding that pension benefits comprise an essential component of public employee compensation and that public employees have a significant contractual interest in these benefits. Recent cases from other jurisdictions that have indirectly addressed the issue strongly suggest that changes to retirement age affect constitutionally protected vested rights, and are thus subject to judicial challenge and potential invalidation. The actuarial reduction will necessarily mean that these people receive a smaller benefit than they have already earned under the terms of their plan.

The Minnesota Supreme Court held that retroactively imposing a minimum retirement age upon an employee who had already retired after completing the required 10 years of service amounted to an unconstitutional impairment of contract. *Christensen v Minneapolis Mun. Emps. Ret. Bd.*, 331 N.W.2d 740, 742 (Minn. 1983). In *Christensen*, a public official retired at age 38 after attaining the 10-year minimum service eligibility threshold. Four years later, the legislature added a minimum-age requirement of 60 and suspended the official's benefits until he reached 60. He contended that the statute was unconstitutional as applied to him since it impaired his employment contract with the city, "the performance of which he had completed." *Id.* at 743. Although Minnesota does not define pension benefits as contracts or provide express constitutional protection, the Minnesota Supreme Court concluded that the official had a vested contractual right in his retirement allowance. Accordingly, any modification of that contract by the state must be reasonable. Under the circumstances, the court concluded: "We do not think that the need for a minimum age requirement is so compelling, or is such a reasonable condition appropriate to the public purpose claimed as to justify impairment of the state's obligation." *Id.* at 751.

A Colorado Court of Appeals has suggested that “benefits based on age and/or service requirements” were vested rights not subject to divestment, and thus any legislative interference with those retirement age and/or service requirements amounted to unconstitutional contractual impairment. *Kilbourn v. Fire and Police Pension Ass’n*, 971 P.2d 284, 287 (Colo. 2008).

In a recent Rhode Island case, *Rhode Island Council 94 v. Carcleri*, No. PC 10-2859 (R.I. Super. Ct. Sept. 13, 2011), plaintiffs sought a declaration that the state’s public pension system created a contract with employees who had at least ten years service, even though Rhode Island does not have constitutional language declaring that such relationships are contractual. The court held that a ten-year veteran had implied unilateral contract rights pertaining to retirement allowances and COLA benefits that are not subject to collective bargaining. The state has filed an appeal, which is currently pending. This ruling implies, however, that recent state legislative changes increasing the minimum retirement age and reducing other pension benefits for public employees with years of service will likely be found to impair the employees’ contractual rights under the state and federal Contract Clause.

Finally, in a similar but broader finding, the Tennessee Supreme Court has stated: “public policy demands that there be a right on the part of the public employer to make reasonable modifications in an existing plan if necessary to create or safeguard actuarial stability, *provided that no then accrued or vested rights of members or beneficiaries are thereby impaired.*” *Blackwell v. Quarterly Cnty. Ct. of Shelby Cnty*, 622 S.W.2d 535, 541 (Tenn. 1981). Such a declaration can be reasonably interpreted to mean that an employee’s right to retire at a certain age cannot be extended as this would impair that employee’s accrued time towards retirement.

ii. Increased Rate of Employee Contribution (HB 56/SB 52)

HB 56 and SB 52 seek to increase almost all employees’ contributions to the various state retirement plans by 3% of pay. The 3% contribution increase for employees may result in a potential employer contribution rate decrease (*i.e.*, for the state).

a). Threshold Issue—Is Legislation Requiring an Increase in Public Employee Contribution Rates Revenue-Raising?

In addition to Contract and Takings Clause scrutiny, HB 56 and SB 52 face an initial potential state constitutional challenge as tax bills. Article III, Section (2)(A) (3)(b) of the Louisiana Constitution prohibits the Louisiana Legislature from enacting tax bills during a regular session convened in even-numbered years. These bills seeking to increase employee contribution rates may be characterized as “tax” bills—a “tax” being defined as a monetary charge imposed by government on persons and others to yield public revenue. *Rachal, ex. rel. Regan v. State*, 29 So. 3d 595 (La. 1 Cir. 2009); *State v. Lanclos*, 980 So. 2d 643 (La. 2008) (distinguishing between a court cost and a tax)—depending on where the funds from the increased contributions are deposited.

If the state deposits funds from increased employee contributions in the state general fund, a stronger argument exists that they yield public revenue and thus that the legislation constitutes a “tax” bill prohibited in the 2012 session. Placing revenues from increased employee contributions into the State’s general fund may also violate IRS rules for qualified benefit plans. If the funds are deposited in the pension systems, the “tax” argument may be attenuated but by no means eliminated. The outcome of such a challenge thus remains uncertain and dependent on the specific language of the bill.

b) Potential Constitutional Challenges

Any legislative attempt to increase employee contribution rates faces almost certain litigation and a reasonable likelihood of being held unconstitutional (at least as applied to employees whose benefits have accrued under the systems). No Louisiana cases address this specific issue under similar facts, but numerous other jurisdictions have addressed the issue. The cases discussed in this section arise from jurisdictions that protect pension benefits as Louisiana does. We provide an even broader case law analysis below in Part III. These cases—in their number and holdings—make clear that any attempts to increase a vested employee’s rate of contribution will likely face a significant challenge strengthened by case law from many other jurisdictions.

In jurisdictions where pension benefits are contractual rights protected either by statute, constitution or court decision, the court will more likely find an increase in employee contribution rate a substantial impairment that violates the employees’ constitutionally protected rights in their vested benefits. In at least one case, a court has ordered that any funds collected under the unconstitutional provision be refunded to the employees.

In early March 2012, a Florida circuit court held that a statutory mandate requiring employees to deduct three percent of their gross compensation for contribution to their previously noncontributory employee retirement benefits plan was an unconstitutional impairment of the Plaintiffs’ contract, an unconstitutional taking of private property without full compensation, and an abridgment of the rights of public employees to collectively bargain over conditions of employment. *Williams v. Scott*, No. 2011 CA 1584, 3 (Fla. Ct. App. 2nd Cir. March 6, 2012). Although controlling precedent did not preclude the legislature from “altering benefits which accrue for future state service,” the court determined that the changes at issue were “qualitative changes to the plan, not changes to individual components of future accruals within the plan.” *Id.* at 6 (*citing, Florida Sheriffs Association v. Dept of Administration*, 408 So. 2d 1033 (Fla. 1981)). Accordingly, following the language of §121.011(3)(d), the court found that the challenged changes “plainly abridge the plaintiffs’ unconditional contract rights....” The Court went further, articulating a two-part test for determining when a contractual impairment is unconstitutional; that is, when the impairment is (1) substantial and (2) not reasonable and necessary to serve an important public purpose. *Id.*

In another 2012 decision, the Superior Court of Arizona for Maricopa County held that “an increase in Plaintiffs’ proportionate share of the contribution payment to their

[Arizona State Retirement System ("ASRS")] pension benefits plan is a breach of that contract and infringes upon the Plaintiffs' contractual relationship with the State." *Barnes v. Ariz. State Ret. Sys., et al.*, CV 2011-011638 (Super. Ct. Ariz. Feb. 1, 2012). The legislation effectively increased the employee contribution rate by 3% by changing the contribution formula that had been in place since the inception of the ASRS from 50% employer and 50% employee to 47% employer and 53% employee. *Id.* at 2. The court noted that the percentage change had "no effect on the actual solvency of the ASRS." *Id.* Citing a 2003 Arizona Supreme Court decision, the court stated that the Arizona Supreme Court recognizes a "special contractual relationship surrounding pension benefits." *Id.* (quoting *Proska v. Ariz. State Sch. for the Deaf and the Blind*, 205 Ariz. 627, 74 P.3d 939 (Ariz. 2003)). Under this "contract theory of retirement benefits," the state may not impair or abrogate an employee's contractual benefits without offering consideration and obtaining the employee's consent. *Id.*; see also *Yeazell v. Copins*, 98 Ariz. 109, 402 P.2d 541 (Ariz. 1965).

The Arizona court found that the legislation "as applied to these Plaintiffs, existing members of ASRS at the time [the bill] was enacted, diminishes Plaintiffs' public retirement benefits." *Id.* at 3. The court stated that "Increasing an employee's proportionate share of payment toward pension benefits necessarily operates to reduce the overall value of that benefit to the employee Plaintiffs are forced to pay additional consideration for a benefit which has remained the same." *Id.* Thus, under Art 29, § 1 of the Arizona Constitution, which expressly protects public employee pension benefits, the increase in employee contribution resulted in "diminution or impairment of Plaintiffs' existing public retirement benefits" and was therefore unconstitutional. *Id.* at 3-4.

Similarly, in *Marvel v. Dannemann*, 490 F. Supp.170, 177 (1980), a Delaware federal district court held that legislation increasing the required employee pension fund contributions from 1% to 4.3% violated the Contract Clause. The court concluded that the state and pension plan members had entered into a unilateral contract that became binding and irrevocable when the members had either fully performed under the contract by fulfilling their age and service requirements or had at least substantially performed under the contract before the law was amended to increase the contribution rates. *Id.* at 174-75. The court found that increasing in the contribution rate to 4.3% from 1% was "very substantial" and thus unreasonable under the Contract Clause. The court rejected the state's policy argument that such increases were necessary due to the "public interest in the fiscal integrity of the fund." *Id.* at 176-77. The court noted that while the fund was indeed in trouble, employee contributions were never intended to support the entire fund; rather, the plan was designed to be funded by the state, if necessary, to meet its commitments. Consequently, the court held that the amendment increasing the employee's contribution rate did not have the effect of increasing the fiscal integrity of the fund, but rather, only "provided that public funds will bear substantially less of the costs of [public] pensions and that the [employees] will pay a correspondingly greater proportion of that cost." *Id.* at 177. Thus, the increase remained an unconstitutional contractual impairment.

Likewise, the Kansas Supreme Court held that "the State or a municipality may make reasonable changes or modification in pension plans in which employees hold a vested interest, but changes which result in disadvantages to employees must be accompanied by offsetting or counterbalancing advantages." *Int'l Assoc. of Firefighters, Local No 64 v. City of Kan. City*, 954 P.2d 1079 (Kan. 1998); see also *Galindo v. City of Coffeyville*, 885 P.2d 1246 (1994); *Singer v. City of Topeka*, 607 P.2d 467 (1980). In *Singer v. City of Topeka*, the state increased the contribution amount required by employees. The supreme court held that this increase constituted an unconstitutional impairment of the employees' contract rights because the disadvantageous modification in the pension plan was not accompanied by any counterbalancing advantage to the employee. As a result, the court ordered that any amounts collected that exceeded the original contribution rate be refunded to the plan members.

iii. Readjustment of Final Average Compensation Formula (HB 55/SB 42, 47)

HB 55, SB 42, and SB 47 all seek to expand from three years to five years the number of years of earned compensation taken into account to compute an employee's "final average compensation," regardless of the employee's date of hire. Such changes often effectively dilute employee's accrued benefits by reducing the final average compensation number used in formulating an employee's total accrued benefit. These bills would also effectively reduce the employee's rate of accrual. Consequently, these bills could face significant constitutional challenges.

No Louisiana courts have addressed this issue directly, but courts from other jurisdictions have found that legislation affecting a public employee's final average compensation unconstitutionally violates vested employee's contractual rights. A reasonable likelihood that a court would find that increasing the number of years factored into the equation would unconstitutionally impair vested contractual rights, because altering the formula could affect benefits that have already accrued, for those employees who are eligible to retire, as well perhaps as those who have attained some accrued benefits.

In *Felt v. Board of Trustees*, 481 N.E.2d 698 (Ill. 1985), the Illinois Supreme Court held that legislation changing the number used to determine employee pension amount (from the salary on the last day of service to an average of the last year of service) violated the constitutional pension clause and Contract clause because it constituted a retroactive diminution and impairment of benefits to current plan participants. The court relied on *Kleinfeldt v. New York City Employees' Retirement System*, 324 N.E.2d 865, (N.Y. 1975), which similarly held unconstitutional a law limiting salary increases in the years considered in determining final average salary for pension purposes. Illinois' constitution provides similar protections to pension benefits as does Louisiana and New York.

In *Kraus v. Board of Trustees*, 390 N.E.2d 1281 (Ill. Ct. App. 1979), a police officer placed on disability challenged a statute that changed which year's salary was used to calculate his pension amount. When the officer entered the system, the law permitted him to retire at 50% of the salary of his retirement year. Before the officer became eligible to retire, however, the pension code was changed to instead use the salary year he was placed on disability in calculating his pension. Relying on the state's constitutional pension protection language, and New York court decisions interpreting similar constitutional language, the court found that the right to pension benefits vests upon enrollment, reiterating that "[t]he purpose of the amendment was to fix the rights of the employee at the time he became a member of the system." The court held that Illinois' Constitution "prohibits legislative action which directly diminishes the benefits to be received by those who became members of the pension system prior to the enactment of the legislation, though they are not yet eligible to retire." In addition, the court noted that nothing in the constitutional history suggested that the legislature retained a "reasonable power of modification, even to diminish benefits to be received by prior members of the pension system." Subsequent Illinois Supreme Court decisions in *Felt v. Board of Trustees*, 481 N.E.2d 698 (Ill. 1985) and *Buddel v. Board of Trustees*, 514 N.E.2d 184, 188 (1987), expressly approved this holding in *Kraus*.⁸

In Pennsylvania, legislation freezing the retirement base salary used to calculate employees' final average salary and pension benefits was held to violate the state's contract clause because it diminished the vested pension rights that employees would receive under their retirement contract. *McKenna v. Commonwealth, State Employees Ret. Bd.*, 421 A.2d 1236 (Pa. Commw. Ct. 1980), *affirmed* 433 A.2d 871 (Pa. 1981). The court relied upon earlier state supreme court decisions finding that that "an employee who has complied with all the conditions of eligibility to receive a pension cannot have his contract of retirement adversely affected by subsequent legislation, not even for purposes of actuarial soundness." *Id.* (citing *Harvey v. Allegheny County Retirement Board*, 141 A.2d 197 (1958)).

Likewise, the Washington state attorney general concluded that a bill altering the formula for employees' average final compensation constituted an unconstitutional impairment of contract because it disadvantaged employees with no accompanying advantage. Att'y Gen. Op. AGLO 1982 No. 5 (March 5, 1982). In particular, the legislation proposed to amend the method for calculating retirement allowances for certain employees who had earned credit for elective service and "other" service by essentially splitting what had been a single, combined allowance into two allowances. The calculation amendment would have resulted in significantly reducing the employees' retirement allowances. Relying on *Bakenhaus v. Seattle*, 296 P.2d 536

⁸ See also Eric M. Madiar, Chief Legal Counsel to Illinois Senate President John J. Cullerton, *Is Welching on Public Pension Promises an Option for Illinois? An Analysis of Article XIII, Section 5 of the Illinois Constitution* (March 1, 2011), available at <http://ssrn.com/abstract=1774163>, Donald R. Tyer, "The Constitutionality of Illinois Public Pension Reform", *Legal Insights for Pension Boards*, Vol. 18, No. 3 (Fall 2011) (concluding that pension changes that decrease benefits for current employees would "undoubtedly" face legal challenge).

(Wash. 1956), the attorney general found that the change in the final average compensation formula constituted an unconstitutional contractual impairment.

In addition, *Rhode Island Council 94 v. Carcieri*, No. PC 10-2859 (R.I. Super. Ct. Sept. 13, 2011), discussed above, suggests that recent state legislative changes in Rhode Island reducing the percentage allowances for public employees with at least ten years of service likely impairs the employees' contractual rights under the state and federal Contract Clause.

iv. Merger of TRSL and LSERS Systems (HB 60/SB 46, 56)

HB 60, SB 46 and SB 56 propose to merge the administrative functions of the Louisiana School Employees' Retirement System (LSERS) into the Teachers Retirement System of Louisiana (TRSL). At this point these bills seek only a merger of administrative functions, which does not present any legal or constitutional issues. However, the proposed bills do state the legislature's future intent to merge the funding aspects of the two systems.⁹ Since the funding of these plans is done in a significantly different manner, any attempt to combine the systems for actuarial purposes would raise a likelihood of being challenged under Article X, § 29 of the Louisiana Constitution. This is because the merger of two differently funded systems has the effect of negatively impacting the actuarial soundness of the disparately funded system, the soundness of which is guaranteed under Article X, § 29.

One Louisiana case indirectly addresses the effect of a merger of municipal retirement systems on an employee's retirement benefits, but constitutional issues were not raised and thus the case would appear to be of less precedential value. *Coutee v. Municipal Police Employees' Retirement Sys*, 921 So. 2d 1147 (La. Ct. App. 3d Cir. 2006). In *Coutee*, legislation required municipalities to merge its active members of one system with the Municipal Police Employees' Retirement System (MPERS), which had different eligibility requirements and lower benefits. Plaintiffs filed suit, claiming that the merger divested them of their vested rights and that the city had breached its "no loss" agreements, but alleged no constitutional violations. The court relying on *Smith v. Board of Trustees of Louisiana State Employees' Retirement Sys.*, 851 So. 2d 1100, 1107-08 (La. 2003), simply held that the employees did not have a vested right and the legislature was free to change benefits. The court also found there was no evidence of any contractual agreement between the city and its employees guaranteeing pension benefits.

⁹ See HB 60, Subpart E, § 116, Section 7 ("The board of trustees, as defined in this Act, shall present a strategy to the Public Retirement Systems' Actuarial Committee by December 31, 2012, for the consolidation of the plans, assets, experience accounts, and investment policies of both plans within the system and shall include estimates for the savings resulting from such consolidation. Such strategy shall provide for consolidation of the plans within one calendar year. The Public Retirement Systems' Actuarial Committee shall consider the strategy and report its findings to the legislature by February 28, 2013.")

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Case law from other jurisdictions is limited, but there may be some grounds for a reasonable challenge based on the fact that merging of the two systems would affect the actuarial soundness of the individual systems in such a manner as may violate the state's constitutional guarantee to maintain the plan's actuarial soundness.

For instance, in *Anchorage v. Gallion*, the Alaska Supreme Court held that a city ordinance affecting three related but distinct city-created defined benefit plans violated the Alaska constitution because it disturbed the actuarial soundness of two of the plans by transferring excess funds from those two fully-funded plans to the third plan, which was not fully funded. 994 P.2d 436, 443-45 (Alaska 1997). The court found that the constitutional violation stemmed from a violation of the plan members' vested rights to have the actuarial soundness of their plans evaluated and maintained separately from other plans. By combining the plans, the court reasoned that the vested rights of the employees' were being diminished. It is important to note that the language of the Alaska Constitution's pension protection provision (Article XII, § 7 provides: "Membership in employee retirement systems of the State or its political subdivisions shall constitute a contractual relationship. Accrued benefits of these systems shall not be diminished or impaired"), is almost identical that in the Louisiana Constitution, Article X, § 29(B), (E)(5), which provides that "accrued benefits" shall not be "diminished or impaired."

The Alaska case can be contrasted with and distinguished from a West Virginia case reaching the opposite conclusion because West Virginia lacks the specific constitutional protections found in the Alaska and Louisiana constitutions. *State ex rel. Dadisman v. Caperton*, 186 W. Va. 627, 413 S.E.2d 684 (W. Va. 1991). The West Virginia case involved two retirement plans, one fully funded and the other underfunded, within a single system. The monies of both plans had been accounted for on a system-wide basis and collectively invested. However, a subsequently enacted statute allowed the two plans to be actuarially valued as one system to determine the amount of employer contributions required. This resulted in the suspension of contributions because the system as a whole was actuarially sound as the funds from the over-funded plan were diverted to cover losses in the underfunded plan. Members of the over-funded plan alleged that the surplus in their plan belonged to them, and could not be diverted to cover liabilities in the other plan. The court rejected this argument, finding that so long as the system remained actuarially sound there was no violation.

Therefore, under these cases, a plaintiff may make the argument that the Louisiana Constitution protects the actuarial soundness of the individual systems, such that any merger could potentially affect the soundness of the other plan and be challenged as unconstitutional under Article X, § 29.

C. Louisiana Cases

Some will argue that a line of Louisiana court decisions¹⁰ provide legal support for the constitutionality of the proposed bills discussed above. These cases are open to likely and reasonable attack by potential plaintiffs as they are factually distinguishable and in some cases predate the enactment of Article X, § 29 in 1988 or rely upon outdated pension jurisprudence.

In the most recent such case, *Smith*, the court addressed the vesting of re-employment benefits of retired, rehired state employees. The court held that re-employment benefits can be modified prior to the time the rehired worker attains eligibility for those benefits. While some contend that this case justifies legislation altering forward looking changes in retirement benefits for vested workers, *Smith* is, by the court's own recognition, limited to the issue of re-employment benefits, which are not the same as retirement benefits. Re-employment benefits are simply not part of the "contract" protected by Article X, Section 29.

Two dissenting justices in *Smith*, both who still sit on the Louisiana Supreme Court, criticized the majority for relying on outdated approaches to pension benefits and case law decided prior to the enactment of Article X, § 29 in 1988, expressly recognizing the contractual nature of pension benefits. *Id.* at 1111-13. Legal scholars have likewise criticized the *Smith* opinion for similar reasons. See Michael A. Cancienne, *Smith v. LASERS, The Louisiana Supreme Court Adjusts a Legislative Miscalculation*, 65 La. L. Rev. 881 (Winter 2005); Rebecca B. Hall, *A Wolf in Sheep's Clothing: Dressing Up Substantive Legislation to Trigger the Interpretive Exception to Retroactivity Violates Constitutional Principles*, 67 La L. Rev. 599 (Winter 2007). Further, *Smith* glosses over the issue of when an employee "accrues" certain pension rights. Read literally, some might contend that *Smith* would permit the legislature to impose significant reductions to pension benefits even upon employees just one day short of retirement eligibility as of the effective date. Such a holding conflicts with modern pension benefit jurisprudence.

It is our opinion that *Smith* and the line of cases it relies on (beginning with *Bowen*), are inadequate to support an argument for the constitutionality of the proposed bills discussed above. Rather, the cases from other jurisdictions cited herein provide a more reliable basis to analyze constitutionality. These cases involve the same or very similar issues as the proposed bills and adopt the modern approach toward pension law as a contractual right encompassed by Article X, § 29.

¹⁰ *E.g.*, *Smith v. Board of Trustees*, 851 So. 2d 110 (2003), *Louisiana State Troopers Ass'n v. Louisiana State Police Retirement Board*, 417 So. 2d 440 (La. Ct. App. 1st Cir. 1982), *Young v. Dep't of Highways*, 160 So. 2d 391 (La. Ct. App. 1st Cir. 1964); *Bowen v. Bd. of Trustees of the Policy Pension Fund*, 76 So. 2d 430 (La. Ct. App. 1st Cir. 1954).

III.

STATE BY STATE ANALYSIS OF SIMILAR PENSION ISSUES

The following discussion provides a non-exhaustive survey of case law from multiple jurisdictions that have addressed pension changes similar to those proposed by the bills pending before the Louisiana legislature. Because the law regarding the contractual status and protection of public-employee pension benefits can vary greatly from state to state, the discussion includes a brief synopsis of each state's law governing public pension benefits before turning to the particular issues of importance in assessing any potential legal challenges facing the proposed Louisiana legislation. Some of the cases discussed below were treated in the discussion above, where they were often discussed in a more abbreviated form.

It is critical to note that some of the decisions cited below do not (or did not) recognize that public pension legislation creates a contractual right between the public employee and the state. Louisiana, like a number of other states, expressly recognizes in Article X, § 29 that its pension laws are contractual rights, which are enforceable under the state and federal Contract Clauses and subject to other causes of action. Accordingly, opinions finding no contractual violations because there was no contractual protection are readily and easily distinguishable from current Louisiana law.

1. ALASKA

A. Governing Law

Alaska Constitution Article XII, § 7 provides: "Membership in employee retirement systems of the State or its political subdivisions shall constitute a contractual relationship. Accrued benefits of these systems shall not be diminished or impaired." This language is almost identical to that in the Louisiana Constitution, Article X, § 29(B), (E)(5), which provides that "accrued benefits" shall not be "diminished or impaired."

B. Issues

i. Definition of "Accrued Benefits"

The Alaska Supreme Court has interpreted the term "accrued rights" to be the same as "vested rights." *Anchorage v. Gallion*, 944 P.2d 436, 441 n.7 (Alaska 1997); *Hammond v. Hoffbeck*, 627 P.2d 1052, 1055 n.4 (Alaska 1981). Under Alaska law, the rights of employees vest and thus accrue when they enroll in the retirement system, rather than when they become eligible to receive the benefits. *Duncan v. Retired Pub. Employees of Alaska, Inc.*, 71 P.3d 882, 889 (Alaska 2003) (finding that health benefits are included in "accrued benefits"); *Hoffbeck*, 627 P.2d at 1056-57. Thus, any changes in the system that diminish or impair vested rights must be reasonable in that they are offset by comparable new advantages to avoid running afoul of article XII of the Alaska Constitution. *Hoffbeck*, 627 P.2d at 1056-57.

ii. Merger of Differently Funded Plans

In *Anchorage v. Gallion*, 994 P.2d 436, 443-45 (Alaska 1997), the Alaska Supreme Court held that a city ordinance affecting three related but distinct city-created defined benefit plans violated the Alaska constitution because it disturbed the actuarial soundness of two of the plans by transferring excess funds from those fully-funded plans to the third plan, which was not fully funded. The court found that the constitutional violation stemmed from a violation of the plan members vested rights to have the actuarial soundness of their plans evaluated and maintained separately from other plans.

2. ARIZONA

A. Governing Law

The Arizona Constitution Article 29, § 1 provides that, "Membership in a public retirement system is a contractual relationship that is subject to Article II, § 25, and public retirement system benefits shall not be diminished or impaired."

Article II, § 25 states, "No bill of attainder, ex-post-facto law or law impairing the obligation of contract, shall ever be enacted."

B. Issues

i. Increased Rate of Employee Contribution

In an "Under Advisement Ruling," the Superior Court of Arizona for Maricopa County held that "an increase in Plaintiffs' proportionate share of the contribution payment to their [Arizona State Retirement System] pension benefits plan is a breach of that contract and infringes upon the Plaintiffs' contractual relationship with the State." *Barnes v. Ariz. State Ret. Sys., et al.*, CV 2011-011638 (Super. Ct. Ariz. Feb. 1, 2012).

The bill in question, Senate Bill 1614, changed the contribution formula that had been in place since the inception of the Arizona State Retirement System (ASRS) in which the proportionate share of annual contributions paid between an employer and its employees had been set at 50% employer and 50% employee. Senate Bill 1614 changed that formula to provide a 47% proportionate share contributed by employers and a 53% proportionate share contributed by employees. *Id.* at 2. The court likewise noted that the percentage change had "no effect on the actual solvency of the ASRS." *Id.*

Citing a 2003 Arizona Supreme Court decision, the court in *Barnes* stated that the Arizona Supreme Court recognizes a "special contractual relationship surrounding pension benefits. *Id.* (quoting *Proska v. Ariz. State Sch. for the Deaf and the Blind*, 205 Ariz. 627, 74 P.3d 939 (Ariz. 2003) "[Cases] have adopted what we have characterized as 'the contract theory of retirement benefits.' Under that theory, the State's promise to

pay retirement benefits is part of its contract with the employee; by accepting the job and continuing to work, the employee has accepted the State's offer of retirement benefits, and the State may not impair or abrogate that contract without offering consideration and obtaining the consent of the employee.")); see also *Yeazell v. Copins*, 98 Ariz. 109, 402 P.2d 541 (Ariz. 1965).

The court found that "Senate Bill 1614 as applied to these Plaintiffs, existing members of ASRS at the time [the bill] was enacted, diminishes Plaintiffs' public retirement benefits." *Id.* at 3. The court stated that "Increasing an employee's proportionate share of payment toward pension benefits necessarily operates to reduce the overall value of that benefit to the employee...Plaintiffs are forced to pay additional consideration for a benefit which has remained the same." *Id.* Thus, the court found that Art 29, § 1 of the Constitution results in "the type of diminution or impairment of Plaintiffs' existing public retirement benefits" and is therefore unconstitutional. *Id.* at 3-4.

3. COLORADO

A. Governing Law

Article II, Section 11 of the Colorado Constitution provides that, "No ex post facto law, nor law impairing the obligation of contracts, or retrospective in its operation, or making any irrevocable grant of special privileges, franchises or immunities, shall be passed by the general assembly."

Colorado case law has established that "Rights which accrue under a pension plan are contractual obligations protected under Colo. art. II, §11, and the U.S. CONST. art. 1, § 10." See e.g. *Colo. Springs Fire Fighters Ass'n v. Colo. Springs*, 784 P.2d 766 (Colo. 1989); *Knuckey v. Pub. Employees' Ret. Ass'n*, 851 P.2d 178, 180 (Colo. App. 1992). However, some courts have held that "Only vested contractual rights are constitutionally protected from statutory impairment." *Kilbourn v. Fire and Police Pension Ass'n*, 971 P.2d 284, 287 (Colo. App. 1998); see also *Changes to PERA Retirement Benefits and Contributions*, Op. Att'y Gen. Colo., No. 04-4 (Nov. 18, 2004.).

B. Issues

i. Distinctions between "Accrued Benefits," "Vested Benefit," and "Partially Vested Benefits"

Multiple Colorado Supreme Court and Court of Appeals opinions have grappled with the definition of "accrued," "vested" and "partially vested benefits." Under Colorado case law, "Only vested contractual rights are constitutionally protected from statutory impairment." *Kilbourn v. Fire and Police Pension Ass'n*, 971 P.2d 284, 287 (Colo. App. 1998).

A majority of Colorado cases have held that "Retirement pay becomes a vested right when an employee has complied with the conditions imposed entitling him to the receipt

of retirement benefits.” *Knuckey v. Pub. Employees’ Ret. Assn.*, 851 P.2d at 180 (citing *Police Pension & Relief Bd v. Bills*, 366 P.2d 581 (Colo. 1961) (vesting of pension rights occurs at retirement); *Peterson v. Fire and Police Pension Ass’n*, 759 P.2d 720 (Colo. 1988)(surviving spouse benefits vest when the statutory conditions are met including that the member dies while in active service and with a surviving spouse or child.) However, in Colorado, “[T]here can be a limited vesting of pension rights prior to actual retirement and also even prior to eligibility to retire.” *Id.*; see also *McInerney v Pub Employees’ Ret Ass’n*, 976 P.2d 348 (Colo. App. 1998). In that situation, “Until benefits fully vest, a pension plan can be changed.” However, with limited vesting, “any adverse change must be balanced by a corresponding change of a beneficial nature, a change that is actuarially necessary, or a change that strengthens or improves the pension plan.” *Id.*

The *Kilbourn* court complicated and/or confused this precedent somewhat in 1998 when it stated that, “[T]here are no bright line tests to determine what constitutes a vested right or when that right accrues. And, in determining whether a statute impairs vested rights, we must consider, *inter alia*, whether it defeats the reasonable expectations of affected persons or surprises persons who have long relied on a contrary state of the law.” *Id.* (citing *Kuhn v. State*, 924 P.2d 1053 (Colo. 1996)). The *Kilbourn* court specifically held that “unlike pension benefits based on age and/or service requirements,” the Plaintiff’s occupational disability benefits were “vested but subject to divestment in the event his occupational disability ceased to exist.”

ii. Definition of “Actuarially Necessary”

In *Peterson v. Fire and Police Pension Association*, the Colorado Supreme Court held that in order to justify a monetary loss for pension holders with limited or partial vesting, “any adverse change must be balanced by a corresponding change of a beneficial nature, a change that is actuarially necessary, or a change that strengthens or improves the pension plan.” 759 P.2d 720, at 725. The Court stated that “A pension fund is said to be actuarially sound if there are no unfounded accrued liabilities and the current cost of pension benefits attributable to active members is being paid on the annual basis.” *Id.* at 726 (citing *City of Colo Springs v. State*, 626 P.2d 1122, 1125 (Colo. 1981)).

The court held that the legislative change related to survivor benefits was constitutional because “the financial loss experienced by the petitioners is offset by the creation of a fund that will ensure that the petitioners’ future benefits are funded by a stable and actuarially sound pension fund.” *Id.* The legislature had responded to a crisis in funding and the plan resulted in “beneficial changes because it improved funding so that money would be available in the future to pay pension.” *Id.*

iii. Cost Of Living Adjustments (COLA)

Most recently, a Colorado court held that although Plaintiffs unarguably had a contractual right to the PERA pension, they did not have a contractual right to the specific cost of living adjustment (“COLA”) formula in place at the time of their

respective retirement. *Justus v. Pub. Employees' Ret. Ass'n of Colo.*, No. 2010 cv 1589, Dist. Ct. Denver (June 29, 2011). Relying in large part on the Court's analysis in *In re Estate of DeWitt*, the Court in *Justus* refused to grant a contract right to a particular COLA where Plaintiffs "could have no reasonable expectation to a COLA for life." *Id.* at 9 (citing *Dewitt*, 54 P.3d 849 (Colo. 2002)).

iv. Increased Rate of Employee Contribution

Applying the courts definitions (above) in a "Formal Opinion," the Attorney General of Colorado stated that:

The rate and amount of retirement benefits may qualify as a partially vested pension right protected by the contract clause of the constitution. An adverse change to a partially vested pension right is lawful only if it is balanced by a corresponding change of a beneficial nature, a change that is actuarially necessary, or a change that strengthens or improves the pension plan. Once a PERA member fulfills all the statutory requirements for a pension benefit, retires and begins receiving a pension, the member's fully vested pension right cannot be reduced by the General Assembly.

Changes to PERA Retirement Benefits and Contributions, Atty. Gen. Colo. Op., No. 04-4 (Nov. 18, 2004).

With regard to percentage contributions specifically, the Attorney General's opinion stated that "If the rate of employee contributions is in fact a protected contractual right, any increase by the General Assembly would be an adverse change to a partially vested pension right and would be lawful only if the change is balanced by a corresponding change of a beneficial nature, is actuarially necessary, or strengthens or improves the pension plan." *Id.* at *2. Accordingly, the Attorney General determined that a legal conclusion regarding whether a change in the rate of employee contributions would infringe on a protected right would rest upon the specific facts of each proposed change. *Id.* at *5.

v. Change in Retirement Age

Although no Colorado cases or Attorney General opinions that specifically address the constitutionality of changing the retirement age for pension plan members were located, at least one Colorado case addressed the issue in dicta. In *Kilbourn*, a Colorado Court of Appeals considered whether the discontinuation of occupational disability benefits constituted a breach of the member's contractual rights. The court held that it did not, at least in part of the grounds that the benefit was contingent upon a "continued incapacity to perform," and was therefore not a vested right. See *Kilbourn v. Fire and Police Pension Ass'n*, 971 P.2d 284, 287 (Colo. 1008). However, in holding that the disability benefits were "vested" but "subject to divestment" the court specifically differentiated occupational disability benefits from "benefits based on age and/or service

requirements,” apparently on the basis that the latter benefits are vested, not subject to divestment. See *id*

4. DELAWARE

A. Governing Law

Delaware’s Constitution, Article 15, § 4, provides limited protection for pension benefits: “No law shall extend the term of any public officer or diminish the salary or emoluments after his or her election or appointment. The term ‘salary or emoluments’ as used herein refers to the actual salary or emoluments being provided an officer at any time during his or her tenure in office and shall not be construed to mean increases in salary or emoluments scheduled by statute for a future date and not yet received by the officer.”

B. Issues

i. Increased Rate of Employee Contribution

In *Marvel v Dannemann*, 490 F. Supp. 170, 177 (D. Del. 1980), a Delaware federal district court held that legislation increasing the required pension fund contributions by its members from 1% to 4.3% was unconstitutional under the Constitution’s Contract Clause. Using contract law as its basis for analysis, the court concluded that the state and pension plan members had entered into a unilateral contract that became binding and irrevocable when the members had either fully performed under the contract by fulfilling their age and service requirements or had at least substantially performed under the contract before the law was amended to increase the contribution rates. *Id.* at 174-75.

The court next found that an increase in the contribution rate to 4.3% from 1% was “very substantial” and thus unreasonable under the Contract Clause. The court rejected the state’s policy argument that such increases were necessary due the “public interest in the fiscal integrity of the fund.” *Id.* at 176-77. The court, however, noted that while the fund was indeed in trouble, employee contributions were never intended to support the entire fund; rather, the plan was designed to be funded by the state, if necessary, to meet its commitments. Consequently, the court held that the amendment increasing the employee’s contribution rate did not have the effect of increasing the fiscal integrity of the fund, but rather, only “provided that public funds will bear substantially less of the costs of [public] pensions and that the [employees] will pay a correspondingly greater proportion of that cost.” *Id.* at 177. Thus, the increase remained an unconstitutional contractual impairment.

5. FLORIDA

A. Governing Law

Article I, Section 10 of the Florida Constitution states that, "No bill of attainder, ex post facto law or law impairing the obligation of contracts shall be passed." FLA. CONST. ART. I, § 10.

In 1974, the Florida legislature created a mandatory pension plan for state employees and, in doing so, enacted a "preservation of rights provision," which provides that: "The rights of members of the retirement system established by this chapter shall not be impaired by virtue of the conversion of the Florida Retirement System to an employee noncontributory system. As of July 1, 1974, the rights of members of the retirement system established by this chapter are declared to be of a contractual nature, entered into between the member and the state, and such rights shall be legally enforceable as valid contract rights and shall not be abridged in any way." FLA. STAT. § 121.011(3)(d).

B. Issues

i. Increased Rate of Employee Contribution

On March 6 of this year, a Florida circuit court held that a statutory mandate requiring employees to deduct three percent of their gross compensation for contribution to their noncontributory employee retirement benefits plan was an unconstitutional impairment of the Plaintiffs' contract, an unconstitutional taking of private property without full compensation, and an abridgment of the rights of public employees to collectively bargain over conditions of employment. *Williams v. Scott*, Cir. Ct. (2nd) Fla., No. 2011 CA 1584, 3 (March 6, 2012).

Although the controlling precedent in Florida, *Florida Sheriffs Association v. Department of Administration*, did not preclude the legislature from "altering benefits which accrue for future state service," the court in *Williams* determined that the changes at issue were "qualitative changes to the plan, not changes to individual components of future accruals within the plan." *Id.* at 6 (citing *Sheriffs*, 408 So. 2d 1033 (Fla. 1981)). Accordingly, following the language of § 121.011(3)(d), the court found that the challenged changes "plainly abridge the plaintiffs' unconditional contract rights..."

The Court went further, articulating a two part test for determining when a contractual impairment is unconstitutional. The court stated that an impairment will be unconstitutional if it is: (1) Substantial; and (2) Is not reasonable and necessary to serve an important public purpose. *Id.*

6. HAWAII

A. Governing Law

Article XVI, Section 2 of the Hawaii Constitution provides: "Membership in any employees' retirement system of the State or any political subdivision thereof shall be a contractual relationship, the accrued benefits of which shall not be diminished or impaired." This language is almost identical that in the Louisiana Constitution, Article X,

§ 29(B), (E)(5), which provides that “accrued benefits” shall not be “diminished or impaired.”

B. Issues

i. Definition of “Accrued Benefits”

Hawaii expressly modeled its constitutional pension protection system after New York’s, as did Alaska, whose system is very similar to Hawaii’s. *Everson v. State*, 228 P.2d 282, 290-291 (Haw. 2010) (citing *Kaho’ohanohano v State*, 162 P.3d 696, 734-35 (Haw. 2007). Under Hawaii law, as determined from the legislative history, “accrued benefits” under Article XVI, Section 2 are protected in that “the legislature could reduce benefits as to (1) new entrants into a retirement system, or (2) as to person already in the system in so far as their future services were concerned. It could not, however, reduce the benefits attributable to past services.” *Everson*, 228 P.2d at 290.

7. ILLINOIS

A. Governing Law

Article XIII, section 5 of the 1970 Illinois Constitution provides: “Membership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.” This section is expressly modeled on New York’s constitutional pension provision. *Kraus v. Board of Trustees*, 390 N.E.2d 1281, 1289-90 (Ill. Ct. App. 1979).

B. Issues

i. Change in Retirement Age

In *Peters v Springfield*, 311 N.E.2d 107 (Ill. 1974), the Illinois Supreme Court addressed the question of whether a city ordinance that reduced the mandatory retirement age for firefighters from 63 to 60 violated the pension protection provision of the Illinois constitution. Relying on the constitutional debates and New York case law, the court upheld the city ordinance reducing the mandatory retirement age. Specifically, the court recognized that any change in the retirement age indirectly affected the amount of the pension, but nonetheless concluded: “[T]he purpose and intent of the constitutional provision was to insure that pension rights of public employees which had been earned should not be ‘diminished or impaired’ but that it was not intended, and did not serve, to prevent the defendant City from reducing the maximum retirement age, even though the reduction might affect the pensions which plaintiffs would ultimately have received.”

ii. Readjustment of Final Average Compensation Formula

In *Felt v. Board of Trustees*, 481 N.E.2d 698 (Ill. 1985), the Illinois Supreme Court held that legislation changing the salary formula for determination of the employee's pension amount from the last day of service to the an average of the last year of service violated the constitutional pension clause and Contract clause because it was constituted a retroactive diminution and impairment of benefits to current plan participants. In reaching this conclusion, the court relied on *Kleinfeldt v. New York City Employees' Retirement System*, 324 N.E.2d 865, (N.Y. 1975), which had reached a similar conclusion in finding unconstitutional a law limiting salary increases in the years which could be considered in determining final average salary for pension purposes.

In *Kraus v. Board of Trustees*, 390 N.E.2d 1281 (Ill. Ct. App. 1979), a police officer who had been placed on disability challenged a statute that changed which year's salary was used to calculate his pension amount. When the officer entered the system, the law permitted him to retire at 50% of the salary of the year he chose to retire. Before the officer met the retirement requirements, however, the pension code was changed to use the year he was placed on disability as the year on which his pension salary was based. Relying on the state's constitutional pension protection language and New York court decisions interpreting similar constitutional language, the court found that the right to pension benefits vests upon enrollment, reiterating that that "[t]he purpose of the amendment was to fix the rights of the employee at the time he became a member of the system." The court held that the Illinois' Constitution "prohibits legislative action which directly diminishes the benefits to be received by those who became members of the pension system prior to the enactment of the legislation, though they are not yet eligible to retire." In addition, the court noted that nothing in the constitutional history suggested that the legislature retained a "reasonable power of modification, even to diminish benefits to be received by prior members of the pension system." Finally, the court distinguished *Peters v. Springfield*, 311 N.E.2d 107 (Ill. 1974), which found that a change in the mandatory retirement age was permissible, on grounds that such a change only *indirectly* affected the pensions in question. Subsequent Illinois Supreme Court decisions in *Felt v. Board of Trustees*, 481 N.E.2d 698 (Ill. 1985) and *Buddel v. Board of Trustees*, 514 N.E.2d 184, 188 (1987), expressly approved of the holding in *Kraus*.¹¹

8. KANSAS

A. Issues

i. Increased Rate of Employee Contribution

¹¹ See also Eric M. Madiar, Chief Legal Counsel to Illinois Senate President John J. Cullerton, *Is Welching on Public Pension Promises an Option for Illinois? An Analysis of Article XIII, Section 5 of the Illinois Constitution* (March 1, 2011), available at <http://ssrn.com/abstract=1774163>, Donald R. Tyer, "The Constitutionality of Illinois Public Pension Reform", *Legal Insights for Pension Boards*, Vol. 18, No. 3 (Fall 2011) (concluding that pension changes that decrease benefits for current employees would "undoubtedly" face legal challenge).

In Kansas, "the State or a municipality may make reasonable changes or modification in pension plans in which employees hold a vested interest, but changes which result in disadvantages to employees must be accompanied by offsetting or counterbalancing advantages." *Int'l Assoc. of Firefighters, Local No. 64 v. City of Kansas City*, 954 P.2d 1079 (Kan. 1998); see also *Galindo v. City of Coffeyville*, 885 P.2d 1246 (1994); *Singer v. City of Topeka*, 607 P.2d 467 (1980). In *Singer v. City of Topeka*, the state increased the amount of contribution required by employees. The supreme court held that this increase constituted an unconstitutional impairment of the employees' contract rights because the disadvantageous modification in the pension plan was not accompanied by any counterbalancing advantage to the employee. As a result, the court ordered that any amounts collected in excess of the original contribution rate be refunded to the plan members.

9. MAINE

A. Governing Law

Maine does not have any state constitutional protection of pension benefits but does have statutory protections as defined in 5 MAINE REV. STAT. § 17801, which expressly state that as of October 1, 1999, pension benefits are "solemn contractual commitments" protected by the Contract Clause. Section 17801 also has a provision permitted the state to increase an employee's contribution rate under certain circumstances.

B. Issues

i. Change in Retirement Age

In *Parker v. Wakelin*, 123 F.3d 1 (1st Cir. 1997), the First Circuit Court of Appeals held that legislation increased the retirement age by two years for employees who had been with the system for less than ten years did not amount to an illegal taking or a violation of the Contract Clause. At the time, Maine law provided that "no amendment . . . may cause any reduction in the amount of benefits which would be due a member . . . on the date immediately preceding the effective date of the amendment." In the First Circuit's view, the word "due" could easily have meant payments that were *immediately due* to a retiree, not the *mere prospect* of future payments. Thus, the court held that the Maine statute had not "unmistakably" given current workers a contractual right to avoid any increased contributions or other changes to their future pensions. *Id.* at 8-9. Therefore, any changes to the pension system were constitutionally permissible for any employee except those actually in retirement. In 1999, however, Maine enacted a statutory recognition of pension benefits as contractual rights. 5 Maine Rev. Stat. § 17801.

ii. Increased Rate of Employee Contribution

In *Parker v. Wakelin*, 123 F.3d 1 (1st Cir. 1997), the First Circuit Court of Appeals held that legislation increasing the employee's rate of contribution from 6.5% to 7.65% did

not amount to an illegal taking or a violation of the Contract Clause. At the time, Maine law provided that “no amendment . . . may cause any reduction in the amount of benefits which would be due a member . . . on the date immediately preceding the effective date of the amendment.” In the First Circuit’s view, the word “due” could easily have meant payments that were *immediately due* to a retiree, not the *mere prospect* of future payments. Thus, the court held that the Maine statute had not “unmistakably” given current workers a contractual right to avoid any increased contributions or other changes to their future pensions. *Id.* at 8-9. Therefore, any changes to the pension system were constitutionally permissible for any employee except those actually in retirement. In 1999, however, Maine enacted a statutory recognition of pension benefits as contractual rights. 5 Maine Rev. Stat. § 17801.

iii. Readjustment of Final Average Compensation Formula

In *Parker v. Wakelin*, 123 F.3d 1 (1st Cir. 1997), the First Circuit Court of Appeals held that legislation capping salary increases that may be used for purposes of calculating an employee’s final average salary did not amount to an illegal taking or a violation of the Contract Clause. At the time, Maine law provided that “no amendment . . . may cause any reduction in the amount of benefits which would be due a member . . . on the date immediately preceding the effective date of the amendment.” In the First Circuit’s view, the word “due” could easily have meant payments that were *immediately due* to a retiree, not the *mere prospect* of future payments. Thus, the court held that the Maine statute had not “unmistakably” given current workers a contractual right to avoid any increased contributions or other changes to their future pensions. *Id.* at 8-9. Therefore, any changes to the pension system were constitutionally permissible for any employee except those actually in retirement. In 1999, however, Maine enacted a statutory recognition of pension benefits as contractual rights. 5 Maine Rev. Stat. § 17801.

10. MASSACHUSETTS

i. Increased Rate of Employee Contribution

In *Opinion of the Justices to the House of Representatives*, the Massachusetts Supreme Judicial Court addressed whether a proposed amendment to the state pension plan raising the rate of contribution from 5% to 7% would be constitutional. 303 N.E.2d 320, 330 (Oct. 30, 1973). The court ruled that such an increase without a corresponding increase in benefits would be “presumptively invalid” as an impairment of contract, though it recognized that such a modification might be permissible under the police power if “proof of a catastrophic condition of the public finances” were presented.

11. MICHIGAN

A. Governing Law

Article 9, § 24 of the Michigan Constitution states that, “The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall

be a contractual obligation thereof which shall not be diminished or impaired thereby.” MICH. CONST. ART. 9, § 24 (1963). The provision further provides that, “Financial benefits arising on account of service rendered in each fiscal year shall be funded during that year and such funding shall not be used for financing unfunded accrued liabilities.” *Id.*

The Michigan Supreme Court has held that this provision of the Constitution provided a contractual right to the accrued financial benefits of pension plans for the state and its subdivisions in place of the common law rule that such public pension benefits were gratuitous allowances which were subject to revocation at will. *Reasonableness of Imposition of New Mandatory Contributions Upon Employee Members of Certain State Retirement Systems*, 1985-86 Op. Att’y Gen. Mich. 67 at *2-3 (citing *Advisory Opinion re Constitutionality of 1972 PA 258*, 389 Mich. 659 (Mich. 1973)).

B. Issues

i. Increased Rate of Employee Contribution

In 1985, Michigan legislative representatives requested an Attorney General opinion regarding proposed legislation that would require a payroll deduction of 3% of annual salary during the first year of employment and 5% of annual salary for each year thereafter. See *Reasonableness of Imposition of New Mandatory Contributions Upon Employee Members of Certain State Retirement Systems*, 1985-86 Op. Att’y Gen. Mich. 67, *1-2 (1985). Neither retirement system in Michigan had previously required any contributions from employee members. *Id.* The former Attorney General of Michigan, Frank Kelley, responded, finding that the proposed mandatory contributions would create an average obligation of \$1,200.00 per year without any commensurate advantage to the employee. As such, the Attorney General held that the change would be “unreasonable and, hence, subversive to the rights of the current employee members protected by Const. 1963, art. 9, § 24...” *Id.* at *1.

The Michigan Supreme Court had provided a standard for the state in a comparable situation in *Advisory Opinion on Constitutionality of 1972 PA 258*, published in 1973:

Under this Constitutional limitation the legislature cannot diminish or impair accrued financial benefits, but we think it may properly attach new conditions for earning financial benefits which have not yet accrued. Even though compliance with the new conditions may be necessary in order to obtain the financial benefits which have accrued, we would not regard this as a diminishment or impairment of such accrued benefits unless the new conditions were unreasonable and hence subversive of the constitutional protection.

209 N.W.2d 200, 389 Mich. 659, 663-664 (1973). Despite the fact that the Supreme Court went on to find that an \$84 increase in the contributions to be paid by some

employees (in order to equalize their contributions with those of other employees) did not subvert the constitutional provision because it was a “reasonable” condition, the Attorney General determined that a \$1,200 per year contribution was unreasonable and thus violated Michigan’s constitutional protections. See *Reasonableness of Imposition*, 1985-86 Op. Att’y Gen. Mich. 67, *13-14 (1985).

ii. Definition of “Accrued Financial Benefits”

In 2005, the Michigan Supreme Court held that health care benefits paid to public school retirees are not “accrued financial benefits” subject to protection from diminishment or impairment by Article 9, § 24 of the Michigan Constitution (1963). *Studier v. Mich. Pub. Sch. Emp. Ret. Sys.*, 698 N.W.2d 350, 353 (Mich. 2005). Although the opinion provided little guidance for the questions at issue in Louisiana, it did provide extensive analysis regarding the definition and proper usage and application of the term “accrued financial benefits.”

The court focused their analysis on how the term would have been commonly understood when the constitution was ratified, and stated that, “[T]he ratifiers of our Constitution would have commonly understood “accrued” benefits to be benefits of the type that increase or grow over time—such as a pension payment or retirement allowance that increases in amount along with the number of years of service a public school employee has completed.” *Id.* at 358; see also *In re Request for Advisory Opinion Regarding Constitutionality of 201 PA 38*, 806 N.W.2d 683, 694-96 (Mich. 2011). The court determined that health care benefits do not accrue in this manner. Similarly, the court held that they are not “financial” benefits as the term is understood. *Id.*

12. MINNESOTA

A. Governing Law

The Minnesota Statutes specifically address the rights of members of the Public Employees Retirement Association (PERA), and state that,

Nothing done under the terms of this chapter and acts amendatory thereof shall create or give any contract rights to any person, except the right to receive back upon withdrawal from the association through separation from the public services, the accumulated deductions, as by law defined, standing on his credit on the books of the association.

MINN. STAT. § 353.38 (1982). Similar “restrictive statutory provision exist with regard to most of the state’s other major public retirement funds.” *AFSCME Councils v Sundquist*, 338 N.W.2d 560, 567 (Minn. 1983); see e.g. MINN. STAT. §§ 354.07, *subd. 8* (teacher’s retirement fund), 352.022(1982 (state retirement fund); see also MINN. STAT. § 645.27 (1982) (state not bound by statute unless statute expressly provides.

B. Issues

i. Change in Retirement Age

In *Christensen v Minneapolis Municipal Employees Retirement Board*, the Supreme Court of Minnesota held that the retroactive application of an amendment to the retirement age for an employee who had already retired was an unconstitutional impairment of contract. 331 N.W.2d 740, 742 (Minn. 1983). When Christensen retired in 1974 (at the age of 38) he was entitled to pension benefits under a 1969 provision of the Minneapolis Municipal Employees Retirement Fund (MMERF) that provided pension benefits for elected officials who served a minimum of 10 years. See *id.* at 742. In 1980, the Minnesota legislature amended that provision and suspended further benefits to Christensen until he attained the age of 60, as required under the revised MINN. STAT. § 422A.156 (1982). Christensen contended that the statute was unconstitutional as applied to him as it impaired his contract of employment with the city of Minneapolis, "the performance of which he had completed." *Id.* at 743.

Applying a former Minnesota statute that protected the vested rights of employees and considering the issue under both the doctrine of promissory estoppel as well as contract impairment, the Minnesota Supreme Court agreed that the retroactive application of the provision was unconstitutional. *Id.* at 752. The *Christensen* court cited a former Minnesota Statute provision Section 422A.25, which provided that:

Nothing contained in sections 422A.01 to 422A.25 shall be construed as diminishing, limiting or modifying any *vested right* of an employee, annuitant or beneficiary to a retirement allowance, annuity or pension acquired under the law existing prior to May 1, 1975.

Id. at 746. Considering this provision, and applying the doctrine of promissory estoppel, the court found that "Christensen had a protectable pension entitlement and that the state's promise of a pension to be paid when he retired ... [was] binding on the state." *Id.* at 749. However, like any contract analysis (including those analyzed under promissory estoppel), there remained an implied condition that the terms of the contract were subject to modification under the state's police power. *Id.* Accordingly, the court applied a three part test for determining when a contract modification is unconstitutional:

(1) The law operates as a substantial impairment of a contractual obligation; (2) There is not a significant and legitimate public purpose behind the legislation; and (3) The adjustment of rights is not based upon reasonable conditions and/or is not of "a character appropriate to the public purpose justifying the legislature's adoption.

Energy Reserves Group v. Kansas Power and Light, 459 U.S. 400, 103 S. Ct. 697, 750-51 ("The reasonableness and necessity of legislative action affecting pension benefits requires a balance or adjustment of the competing interests involved").

Applying this test, the court stated that “We do not think that the need for a minimum age requirement is so compelling, or is such a reasonable condition appropriate to the public purpose claimed as to justify impairment of the state’s obligation.” *Id.* at 751.

ii. Increased Rate of Employee Contribution

In 1982, the Minnesota Legislature, in the wake of an “imminent, and very serious financial crisis facing the government of the State,” passed an Act that impacted the terms of public employees’ pension contributions. More specifically, the Act required that:

[B]eginning with the first full pay period after December 28, 1982, various state, county and municipal employees are required to pay an additional 2% of their salaries into their respective pension funds. This increase in employee contributions is limited in duration to the last pay period before January 1, 1984; then the preexisting formula returns. The Act also requires that, beginning with the first full pay period after December 28, 1982, and continuing until the last full pay period before July 1, 1983, employer contributions to the pension funds equal to 4% of salary are to be either diverted from the pension funds and credited to the general fund, or deferred altogether and not paid to the funds.

Afscme Councils 6 v. Sundquist, 338 N.W.2d at 565. The Act also contained provisions which raised federal tax issues, the most important of which was a provision to “reduce the federal adjusted gross income of public employees by the amount of their employee contributions.” *Id.* According to the court in *Sundquist*, this provision created a tax benefit for employees because the “entire employee pension contribution [would be] ‘picked-up’ by the employer and thereby treated for tax purposes as an employer contribution.” *Id.*

Appellants in *Sundquist* challenged the legislation arguing that it (1) unconstitutionally impaired contract obligations between public employers and employees regarding the level of employee contributions; (2) violated federal and state guarantees of equal protection, and (3) constituted a taking of property without just compensation and a violation of the employees due process rights. *Id.*

Addressing the issue of contractual obligations, the court turned to its recent opinion in *Christensen v. Minneapolis Municipal Employees Retirement Board*, in which the court held that a public employee’s interest in their pension is “best characterized in terms of promissory estoppel.” 331 N.W.2d 740, 747 (Minn. 1983). Under *Christensen*, public employees could challenge changes affecting their interests in a public pension fund under the contract clause by “establishing their right to the maintenance of the preexisting terms or conditions as a matter of either express contract, implied-in-fact contract, or promissory estoppel.” *Sundquist*, 338 N.W.2d at 566.

The court affirmed the trial court's holding that nothing in the record evidenced an express or an implied-in-fact contract designating rates at which employees must contribute. Citing the restrictive statutory provisions outlined above, the court stated: "These statutes clearly support the trial court's conclusion that the legislature did not intend to enter into a contractual obligation with public employees..." *Id.* at 567.

Moreover, the court in *Sundquist* found that, with regard to the application of promissory estoppel, the legislature made no promise regarding "fixed employee pension contribution levels, and that even if such a promise had been made, the appellants did not establish the essential element of detrimental reliance." *Id.* at 568 (stating that "[T]he state had varied contribution levels in the past and ...appellants were unable to produce a single witness to testify to any reliance on a fixed, unchanging level of employee contributions). In contrast to the court's finding in *Christensen*, in which the court held that the retroactive application of a change in the retirement age violated the principals of promissory estoppel for appellants, the court in *Sundquist* found that the Act did not affect appellants expectations concerning the benefits available to them upon leaving public employment. *Id.* at 569.

Finally, with regard to appellants' contention that the 1982 Act constituted a taking of property for a public use without just compensation, the court conceded that salary is a protected property and that "net salaries of affected public employees will be temporarily reduced by 2%" *Id.* at 572. However, the court determined that (1) the change would operate long-term to provide public employees with more disposable income and (2) the action benefited the contributors themselves, not the public (as required by the "public use" provision of the proscription). *Id.* ("the constitutional prohibition against governmental expropriation of private property applies only when it is demonstrated that the property has been taken for public purposes.")

The dissent, however, in *Afscme Councils 6 v. Sundquist*, 338 N.W.2d 560 (Minn. 1983), disagreed, stating that "the legislature has passed far over the line on what is permissible and what is not" in increasing public employees' contribution rates. The court cited other jurisdictions also holding that "increases in public employee pension contributions without counterbalancing increased benefit to the employee constitute impairments of contract rights." *Id.* (citing *Allen v. City of Long Beach*, 45 Cal. 2d 128, 287 P.2d 765 (1955); *Marvel v. Dannemann*, 490 F. Supp. 170 (D. Del. 1980); *Singer v. City of Topeka*, 227 Kan. 356, 607 P.2d 467 (1980); *Opinion of the Justices*, 364 Mass. 847, 303 N.E.2d 320 (1973).

13. NEW HAMPSHIRE

A. Governing Law

Unlike Louisiana, New Hampshire does not have specific constitutional provisions expressly declaring that pension benefits are contractual obligations or providing for protection of pension benefits. The state's supreme court, however, has recognized that in certain cases pension benefits may qualify for protection based on impairment of

contract principles. *E.g.*, *State Employees' Ass'n of N.H., Inc v Belknap County*, 448 A.2d 969 (N.H. 1982).

B. Issues

i. Increased Rate of Employee Contribution

In *Professional Firefighters of New Hampshire v. The State of New Jersey*, No. 217-2011-CV-385 (N.H. Super. Ct. Jan. 6, 2012), the trial court addressed whether recently enacted legislation that raised the employee contribution rate from 2% to 2.5% violated certain provisions of the New Hampshire constitution and the U.S. Constitution's Contract clause.¹² Because New Hampshire does not expressly declare by statute or constitution that employee pension benefits are contractual rights, the court first analyzed this issue. The court concluded that while pension benefits were contractual rights, contrary to earlier supreme court opinions finding that employee benefit rights vest immediately upon employment, those rights did not vest for purposes of the Contract clause until the time expressly stated in the enacting legislation. See *Gillman v. Cheshire County*, 493 A.2d 485 (N.H. 1985) (benefits vest at time of permanent employment); *State Employees' Ass'n of N.H., Inc v Belknap County*, 448 A.2d 969 (N.H. 1982) (same).

For rights that had vested, however, the court found that under a Contract clause analysis a .5% increase in the contribution rate was a substantial impairment of the employee's contract for those employee's who had met the requisite service and age requirements. Citing *Opinion of the Justices*, 3030 N.E.2d 320, 327 (Mass. 1973). Such an increase, the court concluded, was an impairment since it required employees to pay additional amounts without receiving any additional benefits. And this impairment could not be justified by the state's financial necessity. Citing *Opinion of the Justices* (Furlough), 135 N.H. 625, 635 (1992). The court, however, dismissed the plaintiffs' claims because they failed to allege that they were "vested employees" entitled to any contractual protections. The plaintiffs, however, have amended their petition and the matter is still before the court.

14. PENNSYLVANIA

A. Governing Law

Pennsylvania has no explicit constitutional protection for public pension benefits, but courts provide protection for contractual pension rights based on impairment of contract principles. For instance, one court held that the retirement code is in the nature of a contract for pension benefits and unilateral modifications may not be adverse to a member who has met retirement eligibility requirements. *Kelley v. State Employees' Retirement Bd.*, 890 A.2d 1173 (Pa. Cmwlth. 2006); see also *Assoc. of Pa. State Coll.*

¹² The bill also raised the retirement age for new hires and redefined "earnable compensation" to exclude certain forms of income with the effect of decreasing an employee's average final compensation.

Faculties v. State Sys. of Higher Educ, 479 A.2d 962 (1984) (unilateral modifications in the retirement system may not be adverse to a member who has met retirement eligibility requirements).

B. Issues

i. Increased Rate of Employee Contribution

In *Association of Pennsylvania State College and University Faculties v. Pennsylvania*, 479 A.2d 962 (Penn. 1984), the Pennsylvania Supreme Court held it was violation of the state and federal Contract Clause for the state to increase the contribution rate to the state's pension plan by 1.25% for those employees who were members of the system prior to the amendment's effective date without increasing benefits in return. Specifically, the court found that by increasing the employees' contribution rate, the contribution rate of the state would be decreased by 1%, and none of these funds saved would be returned to the pension system. In other words, the employee rate increase only served to save the state 1% of its budgeted payroll. The court found that such an increase was unconstitutional as to both those employees who had vested rights and those who did not. The court concluded: "Accepting the principle that the state's duty to maintain the fiscal integrity of the retirement fund through actuarial soundness is a valid basis for *some changes in a retirement system*, nevertheless, the state's unilateral reduction of retirement benefits arising from the employment contracts cannot pass constitutional muster and must fall." In short, the court rejected any changes that merely shifted some of the financial burden from the employer to the employees.

ii. Readjustment of Final Average Compensation Formula

In *McKenna v. Commonwealth, State Employees' Retirement Board*, 421 A.2d 1236, (Pa. Commw. Ct. 1980), *affirmed* 433 A.2d 871 (Pa. 1981), the court held that legislation freezing the retirement base salary used to calculate the employees' final average salary upon which benefits are computed violated the state's Contract Clause because it diminished the employees' vested pension rights that they would have received under their contract of retirement. In reaching this decision, the court relied on earlier state supreme court decisions finding that "an employee who has complied with all the conditions of eligibility to receive a pension cannot have his contract of retirement adversely affected by subsequent legislation, not even for purposes of actuarial soundness." Citing *Harvey v. Allegheny County Retirement Board*, 141 A.2d 197 (1958).

15. RHODE ISLAND

A. Governing Law

Rhode Island has no constitutional or statutory protection of pension plans or declaration that pension benefits constitute contracts between the employees and the state.

B. Issues

i. Change in Retirement Age

In a recent case, *Rhode Island Council 94 v. Carcieri*, No. PC 10-2859 (R.I. Super. Ct. Sept. 13, 2011), plaintiffs sought a declaration as to whether the state's public pension system created a contract with its employees who had at least ten years of service. Rhode Island does not have any constitutional language declaring that such relationships were contractual. The court agreed with the public employees, finding that a ten-year veteran had implied unilateral contract rights pertaining to retirement allowances and COLA benefits that are not subject to collective bargaining. The state has filed an appeal, which is currently pending. But the implication of this ruling is that recent state legislative changes increasing the minimum retirement age and reducing the percentage allowances for public employees with at least ten years of service will likely be found to impair the employees' contractual rights under the state and federal Contract Clause.

ii. Readjustment of Final Average Compensation Formula

In a recent case, *Rhode Island Council 94 v. Carcieri*, No. PC 10-2859 (R.I. Super. Ct. Sept. 13, 2011), plaintiffs sought a declaration as to whether the state's public pension system created a contract with its employees who had at least ten years service. Rhode Island does not have an constitutional language declaring that such relationships are contractual. The court agreed with the public employees, finding that a ten-year veteran had implied unilateral contract rights pertaining to retirement allowances and COLA benefits that are not subject to collective bargaining. The state has filed an appeal, which is currently pending. But the implication of this ruling is that recent state legislative changes increasing the minimum retirement age and reducing the percentage allowances for public employees with at least ten years of service will likely be found to impair the employees' contractual rights under the state and federal Contract Clause.

16. TENNESSEE

i. Changes to Accrued or Vested Benefits Equals Impairment

In *Blackwell v. Quarterly County Court of Shelby County*, the Tennessee Supreme Court stated: "While we agree with the implicit holding of the courts below that a public employer may from time to time offer additional benefits which employees may accept expressly or by acquiescence, nevertheless we are not convinced that a plan is 'frozen' against detrimental changes or modifications the moment an employee begins to participate in it, where such changes are necessary to preserve the fiscal and actuarial integrity of the plan as a whole. It seems to us that public policy demands that there be a right on the part of the public employer to make reasonable modifications in an existing plan if necessary to create or safeguard actuarial stability, provided that no then

accrued or vested rights of members or beneficiaries are thereby impaired." 622 S.W.2d 535, 541 (Tenn. 1981).

17. WASHINGTON

A. Governing Law

Washington does not have any express constitutional protection for pension plans, but does recognize the contract rule of pensions. See *Bakenhus v Seattle*, 296 P.2d 536 (Wash. 1956). Under this rule, a public employee's pension law creates a contract. Therefore, a legislative amendment causing a significant reduction in the level of benefits without any corresponding advantage (such as a correlative reduction in employees' contributions) results in an unconstitutional impairment of the contractual rights of those members who are disadvantageously affected by the amendment.

B. Issues

i. Readjustment of Final Average Compensation Formula

In Washington, the state attorney general found that a bill altering the formula for employees' average final compensation constituted an unconstitutional impairment of contract when it resulted in a disadvantage to employees with no accompanying advantage. In particular, legislation proposed to amend the method for calculating retirement allowances for certain employees who had earned credit for elective service and "other" service by essentially splitting what had been a single, combined allowance into two allowances. The calculation amendment would result in a significant reduction of the employees' retirement allowances as compared to the original calculation method. Relying on the ruling in the *Bakenhaus* case, *Bakenhus v Seattle*, 296 P.2d 536 (Wash. 1956), the attorney general found that the change in final average compensation formula was disadvantageous to the employees without any offsetting advantage and thus constituted an unconstitutional contractual impairment.

18. WEST VIRGINIA

A. Governing Law

West Virginia has no express constitutional protection for public pension benefits, but does protect against the impairment of contracts. See *State ex rel. Dadisman v. Caperton*, 186 W. Va. 627, 413 S.E.2d 684 (W. Va. 1991).

B. Issues

i. Merger of Plans

State ex rel. Dadisman v. Caperton involved two retirement plans, one fully funded and the other underfunded, within a single system. 186 W. Va. 627, 413 S.E.2d 684 (W. Va.

1991). The monies of both plans had been accounted for on a system-wide basis and collectively invested. However, a subsequently enacted statute allowed the two plans to be actuarially valued as one system to determine the amount of employer contributions required, which resulted in contributions to be suspended because the system as a whole was actuarially sound since the funds from the over-funded plan were diverted to cover losses in the underfunded plan. Members of the over-funded plan alleged that the surplus in their plan belonged to them, and could not be diverted to cover liabilities in the other plan. The court rejected this argument, finding that so long as the system remained actuarially sound there was no violation.