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State Administration and Veterans' Affairs Interim Committee

62nd Montana Legislature

TO: State Administration and Veterans' Affairs Interim Committee

FROM: David Niss, Staff Attorney

RE: Litigation Report and Analysis

DATE: September 30, 2011

I
Introduction

On June 29, 2011, trial courts in Colorado and Minnesota issued opinions in litigation involving the constitutionality of recently passed legislation reducing the size of cost-of-living adjustments (COLA)[1] to be paid to persons receiving certain state pension benefits. In both cases, the courts ruled on a Contract Clause[2] challenge to the legislation. Because there was legislation introduced on this topic in the 62nd Montana Legislative Session[3] and because several of the Montana public employee retirement systems face large unfunded liabilities of their own caused by market declines in their investment assets (which prompted the legislation in both Colorado and Minnesota), Committee staff has prepared this litigation report and analysis of the Minnesota and Colorado trial court decisions.

[1]In the context of this Memorandum, there is no substantial difference between a cost-of-living adjustment and the guaranteed annual benefit adjustment provided for in Montana statutes.

[2]Article I, section 10, clause 1, of the U.S. Constitution prohibits the states from impairing the obligations of contracts. The constitutions of both Colorado and Minnesota also contain analogous provisions. Montana has an analogous provision in Article II, section 31, of the Montana Constitution. The Montana Supreme Court has held that it will construe the federal and Montana Contract Clauses interchangeably, relying upon United States Supreme Court opinions to test the validity of Montana legislation under both Contract Clauses. Neel v. First Fed. Savings and Loan Ass'n of Great Falls, 207 Mont. 376, 675 P.2d 96 (1984), citing Butte v. Roberts, 94 Mont. 482, 23 P.2d 243 (1933).

[3]House Bill No. 197 (Hoven) provided for a constitutional amendment to allow retirement pension contracts to be amended by the Legislature.

II
Discussion

A. The Legislation

In 2010, the Colorado Legislature enacted Senate Bill No. 10-001, and Governor Ritter signed it on February 23, 2010. The law was designed to remedy years of severe underfunding of the statutory Public Employees' Retirement Association's provision of public pensions to more than 400 government agencies and public entities for over 440,000 public employees and to address the unfunded liability caused by market declines in pension fund assets. Among other changes to the retirement systems, the legislation reduced the COLA from 3.25% or 3.5%, depending upon the subclass to which an employee belonged, to 2%.

In Minnesota, the Legislature passed a financial sustainability package in 2010 that, like the Colorado legislation, included many changes to the several retirement systems involved. Among those changes were changes to the postretirement adjustment formulas of several retirement funds, with the largest fund being subject to a change that reduced the adjustment from 2.5% to 2.0%, but returned the adjustment to 2.5% when the level of funding achieved 90%. However, other small retirement funds saw an even greater reduction.[4]

B. The Litigation Generally

Both the Colorado and Minnesota cases concern only the constitutionality of changes made to the annual COLA by the respective legislatures.

In Colorado, plaintiff Gary Justus and three other named public employee plaintiffs brought a class action civil lawsuit to have sections 19 and 20 of Senate Bill No. 10-001, modifying the COLA formula, declared unconstitutional in Justus, et al. v. Colorado, et al., District Court, City and County of Denver, Case No. 2010-CV-1589 (Justus). The complaint in Justus alleged that the legislation constituted a violation of the Contract Clauses of both the U.S. and Colorado Constitutions and included other claims based upon additional sections of the U.S. and Colorado Constitutions and under 42 U.S.C. 1983 for their Contract Clause, takings, and substantive due process violations of the U.S. Constitution.

Like the Colorado litigation, Swanson, et al. v. Minnesota, et al., Ramsey County District Court, File No. 62-CV-10-05285 (2011) (Swanson), was brought as a class action suit against the state and various retirement systems and officials of those

[4]For example, the State Patrol Plan saw a reduction in the postretirement adjustment from 2.5% to 1.5%. 2010 Minn. Laws, sec. 1345-51, ch. 359, art.1, sec. 76-81.

systems, alleging that legislation passed in 2009 and 2010 reducing the formula for the plaintiffs' postretirement COLA abrogated plaintiffs' right to a part of the adjustment in violation of the Contract Clauses and the Takings Clauses of both the U.S. and Minnesota Constitutions. Like the complaint in Justus, the complaint in Swanson also alleged that the violations of the U.S. Constitution constituted a violation of 42 U.S.C. 1983.[5]

In both Justus and Swanson, the plaintiffs claimed that they were, as a matter of contract, entitled to a specific COLA increase that vested in the plaintiffs at the time the plaintiffs either became eligible for retirement or in fact retired. Motions for summary judgment were made by both the plaintiffs and defendants to resolve the litigation, and in both cases the motions were granted for the defendants and denied to the plaintiffs.

C. The Court Decisions

In both the Justus and Swanson opinions, the trial courts issued summary judgment for the state defendants because there were no disputes as to the facts in either case. The courts held that the plaintiffs had not met their burden of proving that the legislation in question was unconstitutional beyond a reasonable doubt because the plaintiffs had not proved that a contract existed as a matter of law requiring a specific level of a COLA that vested in the plaintiffs either upon the day of retirement or the day the plaintiffs became eligible to retire.[6]

In Justus, the court concluded, without citation as to the authority for the standard applied to the plaintiffs, that the plaintiffs could not have had a "reasonable expectation" of a contract for a specific level of a COLA granted to them by statute because of the many times that the statutory COLA had been changed by the Colorado Legislature over the years. However, the court did conclude that there must be a clear and unambiguous statement by the Legislature that a statutory provision is considered to be part of a contract before the court will conclude that a contract exists and that the statute constitutes a term of that contract.[7]

Like the opinion in Justus, the court in Swanson concluded that there was no contract entitling the plaintiffs to a specific COLA. However, the court's opinion in Swanson is the more scholarly because the Swanson court followed cited precedent of the United States Supreme Court and the Minnesota Court of Appeals in making that determination. Here, with the citations omitted, are some of the statements of the

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[5]Plaintiffs in both Justus and Swanson were represented by Mr. Stephen Pincus of Stember Feinstein Doyle & Payne, Pittsburgh, Pennsylvania. Mr. Pincus also represents public employees in similar litigation in Massachusetts, New Hampshire, and South Dakota. A similar legal action is also pending in New Jersey, but Mr. Pincus does not represent the plaintiffs in New Jersey.

[6]Justus opinion p. 2; Swanson opinion, p. 14.

[7]Justus, p. 9.

Minnesota District Court in the Swanson opinion:

> The plain statutory language says nothing about a contract. Thus, there is no express contract to use only the adjustment that is in effect as of a members retirement. . . . Here, no plain and unambiguous language shows the Legislature intended to confer contract rights to a particular adjustment formula. . . . If there is no enforceable contract or promise, there is no basis for a contract impairment claim.

D. Importance of Rulings to Montana

The Justus and Swanson opinions are less important in Montana than the states in which they were decided because Montana law, both statutory and case law, is different.

In order for a court to determine whether there has been an unconstitutional interference with a retirement benefit contract, the court must first find that a contract exists.[8] In the Justus and Swanson opinions, the trial courts held that there was no statute, court decision, or fact evidencing the existence of a contract that included the disputed COLA benefits. Montana law on the existence of a contract is different. Sections 19-2-502(2), MCA, governing all of the public employee retirement systems administered by the Public Employees' Retirement Board[9] and 19-20-501(6), MCA, governing the Teachers' Retirement System (TRS), provide as follows:

> (2) Benefits and refunds to eligible recipients are payable pursuant to a contract as contained in statute. The contract is entered into on the first day of a member's covered employment and may be enhanced by the legislature. Unless specifically provided for by statute, the contract does not contain revisions to statutes after the time of retirement or termination of membership.

> (6) Benefits and refunds to eligible recipients are payable pursuant to a contract as contained in statute. Unless specifically provided for by statute, the contract does not contain revisions to statutes after the time of retirement or termination.

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[8] Baumgardner v. Public Employees' Retirement Board, First Judicial Dist., Lewis and Clark Co., Cause No. ADV-2002-450 (2007); Gulbrandson v. Carey, 272 M 494, 901 P.2d 573 (1995).

[9] In addition to the Public Employees' Retirement System, these are the Judges' Retirement System, the Highway Patrol Officers' Retirement System, the Sheriffs' Retirement System, the Game Wardens' and Peace Officers' Retirement System, the Municipal Police Officers' Retirement System, and the Firefighters' Unified Retirement System.

Under each of these provisions, the contract between the state and the retirement system member includes the guaranteed annual benefit adjustment (GABA) because the adjustment is provided for in statute.[10]

However, it is the language of the Minnesota court in Swanson, after the court concludes that there was no contract to impair, that might someday be applied in Montana. After the Swanson court concluded that there was no contract for a specific level of a COLA, the court then went on to state that even if there had been a contract between the state and the plaintiffs for the payment of a specific COLA, that contract was not unconstitutionally impaired by the Minnesota legislation reducing the COLA.[11] The court noted that both the Minnesota Supreme Court and the U.S. Supreme Court have held that a contract is not impaired unless there is a substantial, as opposed to a technical or minimal, impairment, that the base pension amount, as opposed to a COLA amount, was left undisturbed by the Legislature, that the plaintiffs were left eligible for some type of COLA, that the COLA and pension system had been subject to previous changes and underfunding, and that the challenged legislation was a reasonable and appropriate exercise of legislative authority.[12]

III
Conclusion

The decisions by the Colorado and Minnesota trial courts in the Justus and Swanson cases, holding that there was no contract between the state and the members of the retirement systems for a specific COLA, are not particularly applicable in Montana because statutes and previous decisions of the Montana Supreme Court clearly indicate that the right to a pension benefit is a contractual right in Montana. Whether other statements made by the courts in those opinions concerning the constitutional ability of a legislature to alter retirement pension contracts will apply in Montana will depend upon the outcome of any future litigation involving any similar changes enacted by the Montana Legislature.

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[10]Sections 19-3-1605, 19-5-901, 19-6-710, 19-6-711, 19-7-711, 19-8-1105, 19-9-1009, 19-9-1010, 19-9-1013, 19-13-1010, and19-13-1011.

[11]Swanson opinion, pp.21, 22.

[12]Id., pp. 22-24. There has been little evaluation of any of these matters by the Montana Supreme Court as they might apply to contracts for pension benefits. See previous memorandums on the subject of GABA modification to Senator Dave Lewis dated August 14, 2009, and August 28, 2009. Some legal scholars or advocates are likely to claim that these observations by the Swanson court constitute "dicta", or language unnecessary to the ruling of the court, and should therefore be ignored or at least given little weight.