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BY [Signature]
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**MONTANA FIRST JUDICIAL DISTRICT COURT
LEWIS AND CLARK COUNTY**

ASSOCIATION OF MONTANA
RETIRED PUBLIC EMPLOYEES,
RUSSELL WRIGG, MARLYS
HURLBERT, CAROLE CAREY,
I. EDWARD SONDEÑO,

Plaintiffs,

v.

STATE OF MONTANA, MONTANA
PUBLIC EMPLOYEE RETIREMENT
ADMINISTRATION, PUBLIC
EMPLOYEE RETIREMENT BOARD,
GOVERNOR STEVE BULLOCK, in
his official capacity,

Defendants.

Cause No.: DDV-2013-788

**ORDER ON MOTION FOR
SUMMARY JUDGMENT**

Plaintiffs Association of Montana Retired Public Employees and certain individual members thereof (collectively AMRPE) seek a declaratory judgment that section 5 of House Bill 454¹, which reduces the guaranteed annual benefit adjustment (GABA) for all members of the Public Employee Retirement

¹ 2013 Mont. Laws Ch 390.

1 System (PERS) defined benefit plan², is unconstitutional. AMRPE also seeks
2 a permanent injunction barring Defendants State of Montana, Montana Public
3 Employee Retirement Administration (MPERA), Public Employee Retirement
4 Board (PERB), and Governor Steve Bullock (collectively State) from
5 implementing section 5 of IIB 454. Leo Barry, Chad Adams, and Jessie L. Luther
6 represent AMRPE. Stuart Segrest represents the State.³

7 Before the Court are cross-motions for summary judgment. AMRPE
8 filed its motion on September 5, 2014. The State filed its motion on October 21,
9 2014. The parties have fully briefed both motions; the Court heard oral argument
10 on January 13, 2015. For the following reasons, the Court concludes that
11 AMRPE's motion should be granted, the State's motion should be denied, and a
12 permanent injunction should issue.

13 **FACTUAL AND PROCEDURAL BACKGROUND**

14 AMRPE consists of retired Montana public employees. Plaintiff
15 Russell Wrigg is the president of AMRPE. Plaintiffs Carole Carey, Marlys
16 Hurlbert, and I. Edward Sondeno are retired public employees who receive state
17 retirement benefits, including the GABA.

18 The Montana Legislature created the PERS in 1945. The system is
19 governed by Chapters 2 and 3 of Title 19 of the Montana Code Annotated.
20 MPERA and PERB administer PERS. With each paycheck, public employees pay
21 a percentage of their salaries into a trust fund and public employers contribute an
22 equivalent percentage of each employee's pay. When an employee retires, she is

23 ² In this order, PERS refers to the PERS defined benefit plan only, unless otherwise specified.

24 ³ Michael Black initially represented the State as co-counsel. On February 17, 2015, the State
25 filed a notice of withdrawal indicating that Black was no longer affiliated with the Office of the
Attorney General and is no longer representing the State in the matter.

1 entitled to receive monthly benefit payments calculated by a formula contained in
2 statute. Until the late 1990s, the monthly retirement benefit paid to any particular
3 retiree remained the same for the retiree's life, regardless of external economic
4 changes.

5 In 1997, recognizing that a flat retirement benefit necessarily loses
6 value over time, the Montana Legislature enacted the GABA through IIB 170,
7 1997 Mont. Laws, Ch. 287 at 1337; § 19-3-1605, MCA. Initially, the GABA was
8 a 1.5 percent increase in benefit, compounded annually. This meant that each
9 January, the amount received by an individual retiree the preceding January was
10 increased by 1.5 percent and that increased amount became the monthly benefit
11 payable for the rest of the year. The following January, the benefit would increase
12 another 1.5 percent. The GABA is not, strictly speaking, a cost-of-living
13 adjustment (COLA) because it is not dependent on the actual cost of living at the
14 time. Rather, the GABA is applied regardless of whether it is higher or lower than
15 the change in the cost of living.

16 In 2001, the Montana Legislature increased the GABA to three
17 percent. In 2007, the legislature changed the GABA to 1.5 percent for all new
18 employees who began work after July 1, 2007, but left it at three percent for
19 existing employees and retirees.

20 Leading up to the 2013 legislative session, the funding ratio of the
21 PERS was 67 percent, meaning the fund was only able to meet 67 percent of its
22 current liabilities. Facing no prospect of achieving actuarial soundness in the fund
23 without legislative action, the 2013 Montana Legislature passed HB 454 which
24 comprises a variety of reforms to the PERS. The bill allocates funds from the Coal
25 Severance Tax account to the PERS trust fund and increases the employee and

1 employer contributions to the fund. These increased contribution rates will
2 decrease once the amortization period for PERS falls below 25 years.

3 Section 5 of HB 454, the section to which AMRPE objects, decreases
4 the GABA to 1.5 percent for all PERS members, whether currently working or
5 already retired. Unlike the 2007 amendment, which applied only to new hires,
6 HB 454 decreases the GABA for everyone, including retired public employees
7 who had previously enjoyed a three percent GABA. Section 5 provides for further
8 GABA decreases if the unfunded liability of PERS falls below 90 percent.

9 Upon application of AMRPE, the Court issued a preliminary
10 injunction on December 20, 2013, enjoining the State from enforcing section 5 that
11 amended § 19-3-1605, MCA, and reduced the GABA. Because HB 454 was to
12 take effect on January 1, 2014, no decrease in the GABA has occurred.

13 STANDARD OF REVIEW

14 "Summary judgment is appropriate if the pleadings, the discovery and
15 disclosure materials on file, and any affidavits show that there is no genuine issue
16 as to any material fact and that the movant is entitled to judgment as a matter of
17 law." *Lewis & Clark County v. Hampton*, 2014 MT 207, ¶ 22, 376 Mont. 137,
18 333 P.3d 205 (citing M. R. Civ. P. 56(e)(3)).

19 The parties agree that the material facts are not in dispute and the
20 issues may be resolved as a matter of law.

21 ANALYSIS

22 AMRPE claims that HB 454 violates the contract clause of both the
23 Montana and United States Constitutions because retired public employees have
24 a contractual right to the GABA and, by unilaterally reducing the GABA, the
25 legislature has impaired that right. Article II, section 31 of the Montana

1 Constitution provides, in part, “No . . . law impairing the obligation of contracts
2 . . . shall be passed by the legislature.” Article 1, section 10 of the United States
3 Constitutions provides, in part, “No State shall . . . pass any . . . Law impairing the
4 Obligation of Contracts.”

5 **I. Level of Scrutiny**

6 The parties appear to dispute the level of scrutiny the Court must
7 apply to claims of contract clause violations. AMRPE argues that the Court must
8 apply strict scrutiny because the contract clause is found in article II of the
9 Montana Constitution and the Montana Supreme Court has “repeatedly held that
10 the rights enumerated in the Declaration of Rights (Article II) of Montana’s
11 Constitution are fundamental constitutional rights . . . that deserve the highest level
12 of court scrutiny and protection.” *Kortum-Managhan v. Herbergers NBGL*, 2009
13 MT 79, ¶ 25, 349 Mont. 475, 204 P.3d 693.

14 Without conceding the appropriateness of strict scrutiny, AMRPE
15 argues in the alternative that, if not strict scrutiny, the Court should apply the three-
16 part test for contract clause claims in *City of Billings v. County Water Dist. of*
17 *Billings Heights*, 281 Mont. 219, 935 P.2d 246 (1997). In that case, the Montana
18 Supreme Court held that the contract clauses of the Montana and United States
19 Constitutions are “interchangeable guarantees against legislation impairing the
20 obligation of contract,” and articulated a test for claims of contract clause
21 violations borrowed from the United States Supreme Court. *City of Billings*, 281
22 Mont. at 227, 935 P.2d at 251 (quoting *Carmichael v. Workers' Compens. Ct.*, 234
23 Mont. 410, 414, 763 P.2d 1122, 1125 (1988)).

24 The State notes that *Kortum-Managhan* dealt with the right to a jury
25 trial, not a contract clause issue, and thus does not support the application of strict

1 scrutiny in this case. Instead, the State argues, the Court should apply the three-
2 part contract clause test found in *Seven-Up Pete Venture v. State*, 2005 MT 146,
3 327 Mont. 306, 114 P.3d 1009. The test as articulated in *Seven-Up Pete* is
4 identical to the *City of Billings* test. See *Seven-Up Pete*, ¶ 41.

5 Both *City of Billings* and *Seven-Up Pete* trace the roots of the test used
6 to the Montana Supreme Court's decision in *Carmichael*. See *City of Billings*, 281
7 Mont. at 227, 935 P.2d at 251; *Seven-Up Pete*, ¶ 41. *Carmichael*, in turn, notes
8 that the Montana Supreme Court regularly applies the three-tiered test used by the
9 United States Supreme Court in *Energy Reserves Group, Inc. v. Kansas Power and*
10 *Light Co.*, 459 U.S. 400 (1983), which applied the test announced in *U.S. Trust Co.*
11 *of New York v. New Jersey*, 431 U.S. 1 (1977).

12 Without necessarily agreeing with the State that the general rule that
13 all rights contained in Article II of the Montana Constitution are to be analyzed
14 under strict scrutiny must give way to a more specific test applied to contract
15 clause matters in both Montana and federal law, as discussed above, the Court will
16 apply the three-part test used in *City of Billings* and *Seven-Up Pete* to determine
17 whether HB 454 violates the contract clause of the Montana and United States
18 Constitutions. *City of Billings*, *Seven-Up Pete*, *Carmichael*, *Energy Reserves*
19 *Group*, and *U.S. Trust Co.* all use the same test. AMRPE's alternative argument
20 for application of the test in *City of Billings* is not at odds with the State's position
21 that the Court should apply the *Seven-Up Pete* test, because both cases apply the
22 same test under Montana law.

23 The three-part test used in *City of Billings* and *Seven-Up Pete* to
24 analyze the contract clause of the Montana and United States Constitutions
25 requires the Court to consider: (1) Whether the state law is a substantial

1 impairment to the contractual relationship; (2) Whether the State has a significant
2 and legitimate purpose for the law; and (3) Whether the law imposes reasonable
3 conditions that are reasonably related to achieving the legitimate and public
4 purpose. *City of Billings*, 281 Mont. at 228, 935 P.2d at 251; *Seven-Up Pete*, ¶ 41.

5 **2. Scope of the Contract**

6 Before applying the test, a court must identify the contractual right
7 claimed to be impaired. *U.S. Trust Co.*, 431 U.S. at 17. Here, the Court must
8 determine whether public employees have a contractual right to the GABA.

9 It is presumed that statutes do not create contractual obligations.
10 *Wage Appeal of Mont. St. Hwy. Patrol Officers v. Bd. of Personnel Appeals*, 208
11 Mont. 33, 41, 676 P.2d 194, 199 (1984). “If contractual rights are to be created
12 by statute, the language of the statute and the circumstances must manifest a
13 legislative intent to create private rights of a contractual nature enforceable against
14 the state.” *Wage Appeal*, 208 Mont. at 41, 676 P.2d at 199. Durational or
15 contractual words are suggestive of such legislative intent. *Justus v. State*, 336
16 P.3d 202, ¶ 29 (Colo. 2014).

17 The parties agree that at least some benefits are protected by a
18 contract; the dispute is over the scope of that protection. Section 19-2-502(2),
19 MCA, provides:

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

24 AMRPE argues that the contract comprises Chapters 2 and 3 of Title
25 19 of Montana Code Annotated, including § 19-3-1605, the GABA statute.

1 AMRPE urges application of the California rule as articulated by the California
2 Supreme Court in *Betts v. Bd. of Admin. of the Pub. Employees' Ret. Sys.*, 582 P.2d
3 614 (Cal. 1978). "An employee's contractual pension expectations are measured
4 by benefits which are in effect not only when employment commences, but which
5 are thereafter conferred during the employee's subsequent tenure." *Betts*, 582 P.2d
6 at 619. AMRPE asserts the GABA, therefore, is included as part of the pension
7 benefits guaranteed to retired public employees by their contracts with the State.

8 The State argues for a significantly narrower construction. Section
9 19-2-502(2), MCA, provides that "*benefits and refunds* are payable pursuant to
10 a contract" (emphasis added). There is no mention of the GABA. Section
11 19-2-303(10)(a), MCA, defines "benefit" as "the service retirement benefit, early
12 retirement benefit, or disability retirement or survivorship benefit payment
13 provided by a defined benefit retirement plan." The GABA is not mentioned
14 in that definition. The service retirement benefit is calculated by a formula in
15 § 19-3-904, MCA, that likewise does not refer to the GABA. Similarly, the
16 formula for the early retirement, disability, and survivorship benefits do not refer
17 to the GABA. See §§ 19-3-906, 19-3-1008, 19-3-1205, MCA. The contract
18 contemplated by § 19-2-502(2), therefore, contains only the benefits defined as
19 service retirement, early retirement, or disability or survivorship, not the GABA.

20 The Montana Supreme Court has not addressed the scope of a public
21 employee's pension contract in regards to the GABA. Lacking direct precedent,
22 the State directs the Court to *Wage Appeal*, in which the Montana Supreme Court
23 held that highway patrol officers did not have a contractual right to a one percent
24 yearly salary increase. In that case, the 1975 Montana Legislature supplanted a
25 statewide pay plan that provided for one percent annual salary increases with a new

1 plan that provided for longevity increases of \$10 per month for each five years of
2 service. *Wage Appeal*, 208 Mont. at 35-36, 676 P.2d at 196. A group of highway
3 patrol officers sued, claiming the new legislation impaired their contractual right to
4 a one percent annual increase. The Montana Supreme Court rejected their
5 argument, citing “the general rule that an employee’s right to compensation vests
6 or accrues only after he or she has performed the required services for that pay
7 period.” *Wage Appeal*, 208 Mont. at 42, 676 P.2d at 199. Because the officers
8 had not yet worked and earned their salaries for future years, they were not
9 contractually entitled to future salary increases. *Wage Appeal*, 208 Mont. at 43,
10 676 P.2d at 199.

11 The State argues that *Wage Appeal* supports the position that retired
12 public employees have no contractual right to the GABA. But the GABA is
13 different from a salary increase. Retired public employees have already worked
14 their entire careers, unlike the officers in *Wage Appeal*. They have already
15 performed the services that make up their half of the contract and are thus entitled
16 to whatever compensation was promised by the State. Whether the GABA is part
17 of that promised compensation must still be determined.

18 Other states’ courts have considered whether members of a state’s
19 public pension system have contractual rights to various components of their
20 benefits. The California Supreme Court held in 1978 that a pension is an element
21 of compensation which vests upon acceptance of employment. *Betts*, 582 P.2d at
22 617. An employee does not have a right to fixed or specific benefits, but rather to
23 a “reasonable pension.” *Betts*, 582 P.2d at 617. The legislature may modify the
24 benefits prior to retirement to maintain the integrity of the pension system as a
25 whole, but if such modifications are to be reasonable, any resulting disadvantages

1 to employees must be offset by corresponding advantages. *Betts*, 582 P.2d at 617.

2 Betts was a retired state treasurer. He left office in 1967, and at that
3 time California law calculated his pension by multiplying his years of service by
4 the salary of the current treasurer.⁴ In 1974, after Betts had left office but before
5 he retired, the California Legislature changed the law so that his pension was
6 calculated by multiplying his years of service by the highest salary he earned while
7 in office. *Betts*, 582 P.2d at 615. The effect of this change was to substitute a
8 fixed benefit for a fluctuating benefit; under the prior system, pensions would
9 slowly increase as the salary of the current treasurer increased, while under the
10 new system pensions would always remain the same.

11 Switching to a fixed benefit pension is a disadvantage to employees
12 because it freezes the amount of their pensions. Because no corresponding
13 advantages were granted by the change in the pension scheme, the California
14 Supreme Court deemed the change unconstitutional as applied to Betts “because
15 the amendment withdraws benefits to which he earned a vested contractual right
16 while employed.” *Betts*, 582 P.2d at 619. Betts’ contractual right to pension
17 benefits vested the day he began employment and included those benefits in effect
18 at that time, as well as any beneficial modifications.

19 Nebraska has adopted the California rule. See *Calabro v. City of*
20 *Omaha*, 531 N.W.2d 541, 551 (Neb. 1995) (“We now adopt the California rule in

22 ⁴ Cal. Gov. Code § 9359.1(b) (1967) “The retirement allowance . . . is an annual amount equal to
23 five percent (5%) of the compensation payable at the time payments of the allowance fall due,
24 to the officer holding the office which the retired member last held prior to his retirement, or
25 five percent (5%) of the highest compensation fixed for such office during the member’s last
term or any subsequent term prior to his retirement, whichever is greater, multiplied by [years
of service credit].”

1 Nebraska and hold that a public employee's constitutionally protected right in his
2 or her pension vests upon the acceptance and commencement of employment,
3 subject to reasonable or equitable unilateral changes by the Legislature.”).

4 The Arizona Supreme Court follows a similar rule that an employee is
5 “entitled to have his retirement benefits calculated based upon the formula existing
6 when he began employment, rather than a less-favorable formula subsequently
7 adopted during his employment.” *Fields v. Elected Officials' Ret. Plan*, 320 P.3d
8 1160, ¶ 27 (Ariz. 2014) (citing *Yeazell v. Copins*, 402 P.2d 541, 545 (Ariz. 1965)).
9 Beneficial amendments automatically become part of an employee's contract
10 because acceptance of the modification is presumed, but acceptance cannot be
11 presumed when a modification is detrimental to the employee. *Thurston v. Judges'*
12 *Ret. Plan*, 876 P.2d 545, 547-548 (Ariz. 1994).

13 A key difference between Arizona and Montana, however, is that as of
14 1998 Arizona's Constitution provides that “[m]embership in a public retirement
15 system is a contractual relationship . . . and public retirement benefits shall not be
16 diminished or impaired.” Ariz. Const. art. 29, § 1. Montana's Constitution has no
17 such provision that directly addresses the contractual nature of public retirement
18 benefits.⁵

19 Other courts have determined that employees do not have contractual
20 rights to post-retirement benefit adjustments. The United States District Court for
21 the District of Maine held that “it is not clear and unmistakable that a ‘cost-of-
22 living adjustment’ falls under the umbrella of [retirement benefits due].” *Me.*

23 ⁵ Montana's constitutional provision on public employee retirement systems requires the
24 systems be actuarially sound and directs the governing board of the PERS to administer the
25 system as fiduciaries of system participants and their beneficiaries. Mont. Const. Art. VIII,
§ 15.

1 *Ass'n. of Retirees v. Bd. of Trustees. of the Me. Pub. Employees Ret. Sys.*, 954
2 F.Supp.2d 38, 53 (D. Me. 2013). The reason was that the relevant statute listed
3 certain provisions of the Maine Retirement System as “solemn contractual
4 commitments.” The COLA provision was not included in that list and, therefore,
5 the Court concluded that the legislature did not intend for COLAs to be part of the
6 employment contracts. *Me. Ass'n. of Retirees*, 954 F.Supp.2d at 53.

7 Additionally, the COLA was based on the Consumer Price Index
8 (CPI) and thus could fluctuate, leaving the possibility of a zero percent COLA.
9 “Given the potential for variations in the payment to be made, the Court cannot
10 conclude that Former Section 17801 included not-yet-determined COLAs under
11 the umbrella of ‘benefits’ that could not be reduced.” *Me. Ass'n. of Retirees*, 954
12 F.Supp.2d at 53.

13 Similarly, the Washington Supreme Court held that public employees
14 did not have a contract right to an unalterable COLA because the statute
15 authorizing the payment of COLAs explicitly reserved the legislature’s right to
16 modify or repeal it and specified that the statute did not create contractual rights.⁶
17 *Wash. Educ. Ass'n v. Dept. of Ret. Sys.*, 332 P.3d 439, ¶ 6 (Wash. 2014). The New
18 Mexico Supreme Court also found that COLAs were not contractually protected
19 retirement benefits. COLAs were defined separately from the statute that defined
20 the employee’s retirement benefits, the legislature had amended the COLA statute
21 numerous times in the past and, because the COLA was tied to the CPI and could
22 be zero percent, the COLA was “antithetical to a vested . . . right.” *Bartlett v.*
23 *Cameron*, 316 P.3d 889, ¶ 22 (N.M. 2014).

24 _____
25 ⁶ “The legislature reserves the right to amend or repeal this section in the future and no member
or beneficiary has a contractual right to receive this postretirement adjustment not granted prior
to that time.” RCW 41.32.489(6) (1995).

1 The Colorado Supreme Court found that public employees were not
2 contractually entitled to a COLA because there was “no contractual or durational
3 language stating or suggesting a clear legislative intent to bind itself, in perpetuity,
4 to paying [Public Employees’ Retirement Association] members a specific COLA
5 formula.” *Justus*, ¶ 29. The Court compared the COLA statute to other laws it had
6 previously determined created contractual rights, using words such as “entitled,”
7 “future,” and “payable for the life of the retiree,” and noted that the COLA statute
8 did not contain any such language. *Justus*, ¶ 32. Moreover, the Court noted that
9 “[b]y its very nature a statutory cost of living adjustment is a periodic exercise of
10 legislative discretion that takes account of changing economic conditions in the
11 state and/or nation.” *Justus*, ¶ 24. The COLA statute had been amended numerous
12 times over the years, switching at times between a fixed-percentage adjustment and
13 an adjustment tied to the CPI. *Justus*, ¶¶ 8-11.

14 While these cases from other states are helpful to the Court’s analysis,
15 none address an identical situation to that in the present case. The GABA is not a
16 COLA that is tied to economic factors outside the control of the legislature. It is a
17 fixed percentage that compounds annually, regardless of market performance. In
18 that sense, the GABA is unlike the COLAs in New Mexico, Maine, or Colorado
19 which were not contractually protected because, in part, they were subject to the
20 whims of the economy. See *Bartlett*, ¶ 22; *Me. Ass’n. of Retirees*, 954 F.Supp.2d
21 at 53; *Justus*, ¶¶ 8-11.

22 The State contends that *Wage Appeal* is instructive here, and shows
23 that there is no contract right to the GABA. But as noted above, *Wage Appeal* is
24 factually distinguishable. Moreover, *Wage Appeal* does not describe a meaningful
25 framework to analyze the language of a statute to determine whether it “manifest[s]

1 a legislative intent to create private [contract] rights.” *Wage Appeal*, 208 Mont. at
2 41, 676 P.2d at 199. The Montana Supreme Court simply declares the “[n]either
3 the circumstances nor the language of the statute suggest that a contractual
4 obligation was intended to be created.” *Wage Appeal* 208 Mont. at 41-42, 676
5 P.2d at 199. The Colorado Supreme Court in *Justus* suggested words such as
6 “entitled,” “future,” and “payable for the life of the retiree,” evince intent to create
7 contractual rights. *Justus*, ¶ 32.

8 The Court concludes that the GABA statute uses language suggesting
9 legislative intent to bind itself contractually. The statute provides that “the
10 permanent monthly benefit . . . must be increased.” Section 19-3-1605, MCA
11 (emphasis added). See also § 19-3-1605(3), MCA (eligible retirees “must receive
12 the minimum annual benefit adjustment . . .”). Notably, this language referring to
13 “permanent benefits” that must be increased was present in the original version of
14 the GABA statute as well as all later, amended versions. See 1997 Mt. HB 170,
15 § 19-3-1605, MCA (2011), § 19-3-1605, MCA (2014). Even the title of the
16 adjustment, the guaranteed annual benefit adjustment, suggests that the legislature
17 intended to bind itself contractually.

18 Section 19-2-502, MCA, which specifies that PERS members have a
19 contract right to benefits entered into on the first day of a member’s covered
20 employment, notes that the contract may be enhanced by the legislature. Unlike
21 the Washington statutes at issue in *Wash. Educ. Ass’n.*, which explicitly permitted
22 the Washington Legislature to modify or repeal them, the Montana statute limits
23 the ability of future legislatures to alter benefits by use of the word “enhance,”
24 which means “to increase or improve.” [http://www.merriamwebster.com/
25 dictionary/enhance](http://www.merriamwebster.com/dictionary/enhance). This is different than reserving authority to modify or repeal

1 statutory elements of the contract and is in line with the California rule and
2 Arizona cases holding that beneficial changes to an employment contract are
3 presumed to be accepted by the employee. Here, the Montana Legislature
4 enhanced the benefits payable to retirees under their employment contracts by
5 instituting the GABA. Once that enhancement was made, it became part of the
6 contract.

7 The Montana Legislature has, in other contexts, explicitly reserved
8 the right to modify retirement benefits. Section 19-3-2106, MCA, provides that
9 the provisions governing the defined contribution plan and university system
10 retirement programs are subject to amendment by the legislature. "Employees
11 choosing the defined contribution plan or university system retirement program
12 . . . do not have a contract right to the specific terms and conditions specified in
13 statute on the date the employee's choice becomes effective." *See also* section
14 19-3-1607, MCA, expressly providing that GABA does not apply to defined
15 contribution retirees. "Unless otherwise explicitly provided in this part, none of
16 the provisions of this part [GABA] apply under the defined contribution plan."
17 In contrast, neither section 19-2-502 nor section 19-3-1605, the GABA statute,
18 has such language.

19 The statement of intent accompanying HB 170, which established
20 the GABA, bolsters this interpretation that the legislature intended to bind itself
21 contractually to the GABA. "It is the intent of the legislature to guarantee a
22 minimum level of annual benefit increases for retired members and their
23 contingent annuitants or survivors under each of the statewide public employee
24 retirement systems." 1997 Mont. Session Laws, Ch. No. 287 at 1338. The
25 legislature could have described its intent in other ways that would suggest a

1 current policy choice, such as “give” a benefit increase, or “reward” retirees for
2 their work. That the legislature chose the word “guarantee” indicates a promise
3 to ensure that something will happen. Here, that something is the annual benefit
4 increase called the GABA.

5 Publications produced by MPERA and distributed or made available
6 to PERS members further support the interpretation that the GABA is part of the
7 members’ contract. A January 2007 newsletter states on the first page, “Your
8 retirement benefits are a protected contract right. Proposed benefits changes will
9 be for new members only.” A PowerPoint presentation from an employee
10 workshop put on by MPERA contains a slide titled Defined Benefit Retirement
11 Plan Guarantees and lists two things: Guaranteed lifetime retirement income and
12 the GABA. The 2001 PERS member handbook states that the “Guaranteed Annual
13 Benefit Adjustment (GABA) will increase your retirement benefit every year.”
14 Other MPERA workbooks contain statements such as “The GABA ensures a 3%
15 increase in your benefit from the previous year.” Letters sent to employees upon
16 retirement indicate that the retired employee “will receive [their] gross monthly
17 retirement benefit for [their] lifetime. This benefit will increase by 3% each
18 January . . . in accordance with the Guaranteed Annual Benefit Adjustment
19 (GABA).”

20 These publications show that public employees were told before and
21 after they retired that they could count on the GABA. Some of the publications
22 specifically describe the GABA as a contract right. They discuss benefits and
23 benefit increases in the same sentence, suggesting that the State’s interpretation
24 that “benefit” does not include the GABA is incorrect.

25 ///

1 By focusing on the definitions in § 19-2-303, MCA, the State engages
2 in a myopic analysis that misses the point of the retirement system: to provide for
3 people who have dedicated their careers to the State. It is true that § 19-2-303,
4 MCA, does not mention GABA by name, but the GABA statute is part and parcel
5 of the same title of the Montana Code Annotated. Section 19-2-502(b), MCA,
6 provides that the benefits are “payable pursuant to a contract as contained in
7 statute” without any further specification. The statutes do not limit the contract to
8 the definitions in § 19-2-303, MCA.

9 The Court cannot conclude that “contained in statute” refers to only
10 the definitions section or the section describing part of the formulae for calculating
11 benefits. When the legislature created the GABA, it enhanced the retirement
12 benefits for all PERS-eligible employees, working or retired, as § 19-2-502, MCA,
13 contemplates may happen from time to time. The legislature did not reserve the
14 right to reduce that enhancement in the future, nor did it declare that the GABA
15 was not part of the contract. The legislature knew that public employees had a
16 contractual right to retirement benefits and chose to guarantee an additional benefit
17 beyond those in existence at the time. Given the structure and language of the
18 relevant statutes, and the promises made to public employees, the Court concludes
19 that the GABA is part of the contract between public employees and the state.

20 **3. Contract Clause Analysis**

21 Having determined that retired public employees have a contractual
22 right to the GABA, the Court now proceeds to apply the three-part test for contract
23 clause claims.

24 ///

25 ///

1 **A. Substantial Impairment**

2 The first part of the test is to determine whether JTB 454 is a
3 substantial impairment of that contractual right. “Total destruction of contractual
4 expectations is not necessary, and a law which restricts a party to gains reasonably
5 expected from a contract is not a substantial impairment. Further, the extent that
6 the particular industry has been regulated in the past will modify the amount of
7 impairment, if any.” *Neel v. First Fed. Savings & Loan Ass’n. of Great Falls*, 207
8 Mont. 376, 392, 675 P.2d 96, 105 (1984) (citing *Energy Reserves Group*, 459 U.S.
9 at 411).

10 AMRPE offers examples of things that other state and federal courts
11 have found to be substantial impairments. The Ninth Circuit Court of Appeals
12 held that a one- to three-day delay in the issuing of paychecks was a substantial
13 impairment of public employees’ collective bargaining agreement with the state.⁷
14 *Univ. of Hawaii Prof’l Assembly v. Cayetano*, 183 F.3d 1096 (9th Cir. 1999). The
15 West Virginia Supreme Court of Appeals found that a reduction in the COLA—
16 part of West Virginia’s public employee retirement benefits—was a substantial
17 impairment to the contracts of current public employees who had spent sufficient
18 time in the system to have relied, to their detriment, on the expectation of the
19 higher COLA. *Booth v. Sims*, 456 S.E.2d 167 (W. Va. 1995). The Oregon

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23 ⁷ The State notes, correctly, that a collective bargaining agreement is not at issue in the present
24 case. But the Ninth Circuit’s analysis did not rest on the fact that the contract was a collective
25 bargaining agreement. Rather, the Ninth Circuit focused on the “financial embarrassment and
displacement” that could result from the employees’ delayed receipt of their paychecks. *Univ.
of Hawaii*, 183 F.3d at 1106.

1 Supreme Court found that modification of the assumed earning rate adjustment⁸
2 on public pensions, which resulted in 12 to 20 percent decrease in monthly
3 benefits, was a substantial impairment. *Strunk v. Pub. Employees Ret. Bd.*, 456
4 P.3d 1058, 1094 (Or. 2005).

5 The State focuses on the “extent of past regulation” aspect of *Neel*,
6 arguing that retirement benefits are heavily regulated and the GABA statute has
7 been amended several times since its inception. The State also argues that the
8 constitutional requirement that PERS be funded on an actuarially sound basis
9 means that AMRPE should have reasonably expected the GABA to change over
10 time.

11 The Court is persuaded that, by reducing in the GABA from three
12 percent to 1 percent, HB 454 constitutes a substantial impairment of retired public
13 employees’ contract rights. From a strictly financial point of view, the reduction in
14 the GABA would have a substantial effect on the total value of payments a retiree
15 could receive over his or her retirement—thousands of dollars in some cases. (See
16 Pl.’s State. Undisputed Facts, Ex. 2, Aff. Mike O’Connor (Oct. 20, 2014).) This
17 reduction in lifetime value of benefits payments is substantially greater than the
18 lost value caused by a short delay in payment that was found to be a substantial
19 impairment in *University of Hawaii*. There, the plaintiffs had only to wait a few
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21 ⁸ Public employees who joined Oregon’s Public Employee Retirement System before 1996 were
22 entitled to a guaranteed minimum rate of return, called the assumed earnings rate, on their
23 “regular” account, an individual account consisting of the employee’s contributions and
24 earnings from the Public Employee Retirement fund. Amounts calculated by the assumed
25 earnings rate were credited to employee accounts each year. A 2003 change prohibited the
crediting of employee according to the assumed earnings rate if doing so would cause a deficit
in the fund. The Oregon Supreme Court found this change to be a substantial impairment of
the employees’ contracts. *Strunk*, 456 P.3d at 1072.

1 days to receive their pay, while here, if the GABA reduction is allowed to stand,
2 retired public employees will never receive the money.

3 Moreover, reducing the GABA frustrates retired public employees'
4 legitimate expectations. As described above, PERB distributed literature and held
5 seminars and workshops that repeatedly assured employees that the GABA was
6 guaranteed, not subject to the whims of the market, and something on which they
7 could rely. Indeed, the named plaintiffs in this case relied on the three percent
8 GABA when deciding when to retire or whether to purchase service credits. (See
9 Pl.'s State Undisputed Facts (Oct. 20, 2014): Ex. 18, Aff. Carole Carey; Ex. 20,
10 Aff. Marlys Hurlbert; Ex. 22, Aff. E. Edward Sordeno.) This reliance was
11 reasonable, given the reassurances they received from PERB.

12 Retired public employees reasonably expected that the GABA would
13 not decrease, despite the fact that the GABA statute had been amended in the past,
14 because the GABA had never been reduced, except for new hires. Section
15 19-2-502(2), MCA, provides that the contract may be *enhanced* by the legislature.
16 An increase in the GABA percentage is exactly that— an enhancement. The past
17 modifications, then, could not give employees notice that the GABA might be
18 reduced in the future because all past modifications did only what the statute
19 permitted: enhanced their contracts.

20 In 2007, the Montana Legislature reduced the GABA to 1.5 percent
21 for employees hired after January 1, 2007. This further strengthens AMRPE's
22 reasonable expectation that the GABA, as applied to them, would not decrease.
23 The Montana Legislature decreased the GABA for new hires to help maintain
24 constitutionally-mandated actuarial soundness in PERS, but it did so without
25 modifying the GABA as applied to existing employees and retirees. This action

1 is in line with the understanding that an employee's contract entered into on the
2 first day of employment includes the GABA. Public employees have a legitimate
3 expectation that the GABA is part of their contracts with the State, and a reduction
4 in GABA substantially frustrates that expectation.

5 Because the reduction of the GABA has the effect of significantly
6 decreasing the amounts retired public employees reasonably expected to receive
7 as pension payments under their employment contracts, the Court concludes that
8 HB 454 operates as a substantial impairment to their contractual rights.

9 **B. Significant and Legitimate Purpose**

10 Part two of the test is a determination of whether there is a significant
11 and legitimate purpose for the law, and here the parties agree that HB 454 has a
12 significant and legitimate purpose. Article VIII, section 15 of the Montana
13 Constitution requires that public retirement systems be funded on an actuarially
14 sound basis, and the preamble to HB 454 states that it is an attempt to fulfill that
15 constitutional duty. Plaintiffs "do not dispute the State's obligation to ensure
16 PERS is actuarially sound is a compelling governmental interest." (Pl.'s Br.
17 Supp. Mot. S.J. at 15 (Sept. 5, 2014).)

18 **C. Reasonably Related to Achieving that Legitimate Purpose**

19 The third part of the test is whether "the law impose[s] reasonable
20 conditions which are reasonably related to achieving the legitimate and public
21 purpose." *City of Billings*, 281 Mont. at 227, 935 P.2d at 251; *Seven-Up Pete*,
22 ¶ 41. The Montana Supreme Court, the Ninth Circuit, and the United States
23 Supreme Court have all included a "necessity" component in the analysis of
24 the third prong. See *City of Billings*, 281 Mont. at 229, 935 P.2d at 252 ("an
25 impairment may be constitutional if it is reasonable and necessary to serve an

1 important public purposes.”); *Seven-Up Pete*, ¶ 40 (citing *City of Billings*); *Univ. of*
2 *Hawaii*, 183 F.3d at 1106 (“We must next determine whether . . . the impairment
3 was both reasonable and necessary to fulfill an important public purpose.”); *U.S.*
4 *Trust Co.*, 431 U.S. at 29 (“We can only sustain the repeal . . . if that impairment
5 was both reasonable and necessary to serve the admittedly important purposes
6 claimed by the State.”). The burden is on the State to prove that the impairment
7 was reasonable and necessary. *Univ. of Hawaii*, 183 F.3d at 1106.

8 The State argues that it does not need to prove necessity and refers to,
9 without citing, *Seven-Up Pete*. *Seven-Up Pete*, however, quotes *City of Billings*,
10 stating that “an impairment may be constitutional if it is reasonable and necessary
11 to serve an important public purpose.” *Seven-Up Pete*, ¶ 40 (quoting *City of*
12 *Billings*, 281 Mont. at 229, 935 P.2d at 252) (emphasis added). The language in
13 *City of Billings* in turn is a quote from *Buckman v. Montana Deaconess Hosp.*, 224
14 Mont. 318, 327, 730 P.2d 380, 385, which in turn quotes *U.S. Trust Co.*, 431 U.S.
15 at 25. The element of necessity has always been a part of modern contract clause
16 jurisprudence, and the State therefore must prove its action was necessary.

17 Though courts generally defer to the legislature’s judgment, in this
18 case “complete deference to a legislative assessment of reasonableness is not
19 appropriate because the State’s self-interest is at stake. . . . If a State could reduce
20 its financial obligations whenever it wanted to spend the money for what it
21 regarded as an important public purpose, the Contract Clause would provide no
22 protection at all.” *U.S. Trust Co.*, 431 U.S. at 26. See also *City of Billings*, 281
23 Mont. at 229, 935 P.2d at 252 (“[A] heightened level of scrutiny applies when a
24 governmental entity is party to the contract.”); *Seven-Up Pete*, ¶ 47 (“[W]e will not
25 give complete deference to a legislative assessment and will apply a heightened

1 level of scrutiny when the State is a party to the contract or if its self interest is at
2 stake.”)

3 The State argues that heightened scrutiny is not applicable here and
4 the Court should defer to the legislature’s judgment because the State is not acting
5 in its own self interest and HB 454 actually increases the State’s obligations.
6 Section 1 of HB 454 directs up to \$21 million from the Coal Tax Severance fund
7 to the PERS trust fund. Section 4 of HB 454 creates an additional employer
8 contribution to PERS. Initially set at 1.27 percent of the employee’s pay, the
9 additional amount will increase by 0.1 percent each year. The additional
10 payments, however, will terminate when the amortization period of unfunded
11 liabilities in PERS is 25 years or less. As in *Seven-Up Pete*, where the challenged
12 law prohibiting cyanide leaching in mining operations forced the State to forego
13 millions in royalties from mines, the State argues here that because HB 454
14 increases funding obligations to PERS it cannot be in the State’s self-interest.

15 Nevertheless, the cases both parties cite make clear the when the State
16 is a party to the contract that is substantially impaired, complete deference to the
17 legislature is inappropriate. And the State is clearly a party to the employment
18 contracts of public employees. The Court, therefore, will not grant complete
19 deference to the legislature and will instead apply a heightened level of scrutiny.

20 AMRPE argues that the reduction in the GABA was not reasonable
21 because it “placed the entire burden of any unfunded liability [in PERS] primarily
22 on the backs of the Retirees.” (Pl.’s Br. Supp. Mot. S.J. at 15 (Sept. 5, 2014).)
23 “[The] State is not completely free to consider impairing the obligations of its own
24 contracts on a par with other policy alternatives. Similarly, a State is not free to
25 impose a drastic impairment when an evident and more moderate course would

1 serve its purposes **equally well.**" *U.S. Trust Co.*, 431 U.S. at 30-31.

2 Reducing the GABA is not reasonable, AMRPF argues, because
3 there are numerous alternatives the legislature could have adopted to address
4 the actuarial soundness of PERS, including:

- 5 1) Extending the amortization period beyond 30 years;
- 6 2) Adopt HB 454 as initially proposed, without GABA reductions;
- 7 3) Increase employer contributions;
- 8 4) Make a one-time payment to PERS from the General Fund
9 reserves;
- 10 5) Divert money from other trust accounts, such as the Coal
11 Severance Tax trust fund, the Montana Tobacco Settlement trust fund, or
12 the Big Sky Economic Development trust fund, into PERS;
- 13 6) Increase revenue through taxes.

14 Even if alternatives might be "politically more difficult," the State is
15 limited in its ability "to abridge its contractual obligations without first pursuing
16 other alternatives." *Univ. of Hawaii*, 183 F.3d at 1107. The State offers no
17 evidence or argument that it considered alternatives, but rather simply declares
18 that "the rights and responsibilities of the parties were adjusted to ensure current
19 employees and retirees continue to receive retirement benefits," and such action
20 was "of a character appropriate to the public purpose." (Def.'s Comb. Resp. Pl.'s
21 Mot. S.J. & Br. in Supp. Mot. S.J. at 18 (citing *Energy Reserves Group*, 459 U.S.
22 at 412)).

23 There is no dispute that reducing the GABA helps make PERS
24 actuarially sound. If the GABA were decreased, PERS has to pay out less money
25 in benefits (nearly \$700 million less, in this case). In that sense, reducing the

1 GABA bears a reasonable relationship to the admittedly important purpose of
2 keeping PERS actuarially sound.

3 The test however requires “reasonable conditions” that are reasonably
4 related to the public purpose. By reducing the GABA, the State has significantly
5 decreased the benefit payments that retired public employees receive. Decreasing
6 benefits for those who have already given their entire working life to the State,
7 benefits to which they are contractually entitled, is not reasonable or necessary,
8 when other broader remedies were available.

9 The Court thus concludes that reducing the GABA was not reasonable
10 and necessary to achieve the legitimate purpose of maintaining actuarial soundness
11 in PERS. The substantial impairment of contract rights caused by Section 5 of HB
12 454, therefore, is in violation of the contract clause of both the Montana and United
13 States Constitutions. AMRPE is entitled to summary judgment and a permanent
14 injunction.

15 Because the Court concludes that AMRPE is entitled to summary
16 judgment on its contract clause claim, the Court declines to address AMRPE’s
17 takings claim.

18 4. Attorney Fees

19 AMRPE argues that it should be awarded attorney fees. The State
20 did not address fees in its briefs or at oral argument.

21 “Montana follows the general American Rule that a party in a civil
22 action is not entitled to attorney fees.” *Trustees of Ind. Univ. v. Buxbaum*, 2003
23 MT 97, ¶ 19, 315 Mont. 210, 69 P.3d 663. However, in certain circumstances, a
24 court may award attorney fees to the prevailing party. A “district court may award
25 attorney fees in a declaratory relief action under § 27-8-313, MCA, only if

1 equitable considerations support that award.” *Horace Mann Ins. Co v. Hanke*,
2 2013 MT 320, ¶ 34, 372 Mont. 350, 312 P.3d 429. “While § 27-8-313, MCA, |
3 gives district courts the discretion to award ‘further relief’ in the form of attorney
4 fees if a court determines such an award is ‘necessary and proper,’ implicit in that
5 determination is a threshold question of whether the equities support a grant of
6 attorney fees.” *United Nat’l Ins. Co. v. St. Paul Fire & Marine Ins. Co.*, 2009
7 MT 269, ¶ 38, 352 Mont. 105, 214 P.3d 1260.

8 Here, AMRPE does not provide an argument as to how the equities
9 support a grant of attorney fees. Only once has the Montana Supreme Court
10 upheld an award of attorney fees under § 27-8-313, MCA, since it first interpreted
11 the statute in *Trustees of Ind. Univ. v. Buxbaum*. In *Renville v. Farmers Ins. Exch.*,
12 2004 MT 366, 324 Mont. 509, 105 P.3d 280, the Montana Supreme Court upheld
13 an award of attorney fees because the plaintiff, who prevailed in the case, would
14 have been worse off than before she initiated the suit if the court had not awarded
15 her fees. Here, the Court issued a preliminary injunction and the reduced GABA
16 never took effect. All retired public employees have continued to receive the three
17 percent GABA, and thus they would not be worse off than before filing suit but for
18 an award of attorney fees.

19 The Court concludes that the equities do not support departure from
20 the general rule that each party is responsible for its costs and declines to award
21 attorney fees to AMRPE.

22 **IT IS ORDERED** that:

- 23 1. AMRPE’s motion for summary judgment is **GRANTED**.
- 24 2. The State’s motion for summary judgment is **DENIED**.

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