

TIMOTHY C. FOX  
 Montana Attorney General  
 MICHAEL G. BLACK  
 J. STUART SEGREST  
 Assistant Attorneys General  
 215 North Sanders  
 P.O. Box 201401  
 Helena, MT 59620-1401  
 mblack2@mt.gov  
 ssegrest@mt.gov  
 Phone: (406) 444-2026, Fax: (406) 444-3549

COUNSEL FOR DEFENDANTS

MONTANA FIRST JUDICIAL DISTRICT COURT  
 LEWIS AND CLARK COUNTY

ASSOCIATION OF MONTANA RETIRED	)	Cause No. CDV-2013-788
PUBLIC EMPLOYEES, RUSSELL WRIGG,	)	
MARLYS HURLBERT, CAROLE CAREY,	)	<b>DEFENDANTS' REPLY IN</b>
I. EDWARD SONDENO,	)	<b>SUPPORT OF MOTION FOR</b>
	)	<b>SUMMARY JUDGMENT</b>
Plaintiffs,	)	
v.	)	
STATE OF MONTANA, MONTANA PUBLIC	)	
EMPLOYEE RETIREMENT	)	
ADMINISTRATION, PUBLIC EMPLOYEE	)	
RETIREMENT BOARD, GOVERNOR	)	
STEVE BULLOCK, in his official capacity,	)	
	)	
Defendants.	)	

**INTRODUCTION**

Plaintiffs ask this Court to determine that the GABA is fixed at a three percent compounded annual increase “for the rest of their lives without change,” a position recently rejected by the Colorado Supreme Court. *Justus v. Colorado*, 2014 CO 74, ¶ 2, 2014 Colo. LEXIS 944. Plaintiffs fail to overcome, or even acknowledge, the presumption that a legislature, by enacting a law, “did not intend to bind itself contractually.” *Justus*, 2014 CO

74, ¶ 20 (citing *National R.R. Passenger v. Atchison, Topeka & Santa Fe Ry.*, 470 U.S. 451, 465-66 (1985)). Overcoming this presumption, and thereby binding future legislatures, requires that the “words of contract” be “clearly and unequivocally expressed.” *Id.* (quoting *National R.R. Passenger*). The only such unequivocal expression in Montana law is the obligation to pay a retiree’s base benefit--not an annual adjustment that has changed several times in the past. As such Defendants are entitled to summary judgment as a matter of law.

### ARGUMENT

#### **I. PLAINTIFFS ADVOCATE FOR THE WRONG CONSTITUTIONAL STANDARD OF REVIEW.**

Despite the Montana Supreme Court having defined the level of scrutiny for Contract Clause claims involving the State, *see Seven Up Pete Venture v. State*, 2005 MT 146, ¶ 41, 327 Mont. 306, 114 P.3d 1009, Plaintiffs claim that strict scrutiny should apply solely because the Clause is found in Article II of the Montana Constitution. Pls.’ Reply and Resp. at 3 (Doc. 50) (Pls.’ Resp.) (citing *Kortum-Managhan v. Herbergers NBGL*, 2009 MT 79, ¶ 25, 349 Mont. 475, 204 P.3d 693). Plaintiffs attempt to distinguish the controlling Montana Contract Clause cases, like *Seven Up Pete*, by noting that they “predate the *Kotrum-Managhan* holding.” But as early as 1986, the Supreme Court determined that rights found in the Declaration of Rights are fundamental under Montana’s Constitution. *Butte Community Union v. Lewis*, 219 Mont. 426, 430, 712 P.2d 1309, 1311 (1986); *see also Kortum-Managhan* (noting the Court has “repeatedly held” the rights in Article II are fundamental and citing cases back to 1997). Contrary to Plaintiffs’ implication, the law did not change.

The Supreme Court specifically follows the federal three-part test when analyzing a Contract Clause claim. *Seven Up Pete*, ¶ 41. The specific Contract Clause holdings control over the general “fundamental rights” discussion in cases such as *Kortum-Managhan*. Mont. Code Ann. § 1-3-225. And the Court has made clear that it is reversible error for a court to apply a strict scrutiny standard when that standard is not warranted. *Montana Cannabis Industry Ass’n v. State*, 2012 MT 201, ¶ 32, 366 Mont. 224, 286 P.3d 1161.

This Court should reject Plaintiffs’ invitation to apply the wrong standard and instead simply apply the Montana Supreme Court’s settled three-part Contract Clause test: (1) is the state law a substantial impairment to the contractual relationship; (2) is there a significant and legitimate purpose for the law; and (3) does the law impose reasonable conditions that reasonably relate to achieving the legitimate and public purpose? *Seven Up Pete*, ¶ 41. Under this standard, the State is entitled to summary judgment.

## **II. THE PLAIN LANGUAGE OF THE LAW DID NOT ESTABLISH A “CONTRACTUAL RELATIONSHIP” REGARDING THE PERPETUAL RECEIPT OF AN UNALTERABLE GABA.**

The first step in analyzing the substantial-impairment prong is to determine whether a contractual relationship exists at all. *General Motors v. Romein*, 503 U.S. 181, 186 (1992). In its opening brief, Defendants showed that, under the plain language of the statutes, the “contract” for retirement benefits includes the base retirement benefit, but not the GABA. Doc. 47 at 9-10. In response, Plaintiffs assert that this “is a distinction without a difference.” Pls.’ Resp. at 5. Plaintiffs then summarily conclude that the GABA is an enhancement to the contract, which in their view includes every word within Title 19, chapters 2 and 3, and

if “the Montana Legislature intended GABA not be protected by the contract right, it could have simply said so.”

Plaintiffs’ proposal to place the burden on the Legislature to “opt out” of a contract turns the presumption against laws creating contracts on its head. The presumption, in Montana and federally, is that statutes do not create contractual rights unless the obligation is “clearly and unequivocally expressed.” *In re Wage Appeal of Montana State Highway Patrol Officers v. Board of Personnel Appeals (Wage Appeal)*, 208 Mont. 33, 41, 676 P.2d 194, 199 (1984); *Justus*, 2014 CO 74, ¶ 20 (quoting *National R.R. Passenger*, 470 U.S. at 465-66).

The reason that “statutory enactments do not of their own force create a contract relationship with those whom the statute benefits [is] because the potential constraint on subsequent legislatures is significant.” *Justus*, 2014 CO 74, ¶ 21 (citing *Parella v. Retirement Bd. of the R.I. Employees’ Retirement Sys.*, 173 F.3d 46, 60 (1st Cir. 1999)). The ability of subsequent legislatures to amend Montana’s public retirement system is especially important considering the Constitution’s requirement of actuarial soundness. Mont. Const. Art. VIII, § 15(1).

The Supreme Court has also made clear that it will not hold statutes unconstitutional based on an “unreasonable interpretation and dissection” of a statute. *Broers v. Montana Dep’t of Revenue*, 237 Mont. 367, 371, 773 P.2d 320, 323 (1989); *State v. Brendal*, 2009 MT 236, ¶ 18, 351 Mont. 395, 213 P.3d 448 (a court should attempt to harmonize statutes on the same subject). The requirement to read statutes together as opposed to “dissecting” them individually has nothing to do with severability, as Plaintiffs mistakenly

assume, *see* Pls.' Resp. at 14-15, but is instead a cornerstone of statutory interpretation. Severability applies once a Court has determined a particular section is unconstitutional, but it is not an interpretative tool.

Plaintiffs, ignoring the Supreme Court's admonition to harmonize statutes, reference unrelated legislative provisions specifying that members of the defined contribution plan and university system retirement programs "do not have a contract right to the specific terms and conditions specified in statute." Mont. Code Ann. § 19-3-2106; Pls.' Resp. at 5. Plaintiffs ask this Court to assume this disclaimer, relating to defined contribution plans, is relevant to whether the GABA was intended to be part of the contract relating to defined benefit plans.

A contract disclaimer, however, is necessary for defined contribution plans because the retirement "benefit" available to members of these plans is the amount of money in their account at retirement, as opposed to a specific monthly benefit. Mont. Code Ann. §§ 19-3-2116, -2123. The "benefit" therefore is not "defined" or guaranteed. But a similar disclaimer is unnecessary for the GABA statute, because it is not the base retirement benefit but instead a yearly adjustment to the benefit, and the contract provision (§ 19-2-502(2)) thus does not apply to the GABA by definition. To "dissect" these statutes with the goal of implying a contractual right to a perpetual receipt of a three percent GABA is not only "unreasonable," but out of sync with the presumption against statutes creating contracts.

The plain language of Mont. Code Ann. § 19-2-502(2) unequivocally expresses that the contract applies only to "benefits and refunds," and "benefit," which is defined at Mont. Code Ann. § 19-2-303(10), is the base retirement benefit, not the GABA. *See also* Mont. Code Ann. § 19-2-303(48) ("Service retirement benefit' means the retirement benefit that

the member may receive at normal retirement age.”). In order to determine that the GABA is nevertheless a part of the contractual relationship, this Court would have to read “benefits” as used in Mont. Code Ann. § 19-2-502(2) more broadly than the definition of “benefit” at § 19-2-303(10), something that both the presumption against the creation of contractual rights and the rules of statutory interpretation prohibit. Additionally, while the GABA statute (Mont. Code Ann. § 19-3-1605(1) (2011)) states that the benefit “must be increased,” this mandatory language “is directed at the PERA administrator, not the legislature,” and therefore does not indicate legislative “intent to bind itself to an unchangeable [GABA] formula fixed for a retiree without change.” *Justus*, 2014 CO 75, ¶ 31. As a result the GABA is not part of the “contractual relationship,” and this Court should grant summary judgment for Defendants.

### **III. WAGE APPEAL IS APPLICABLE AND CONTROLLING AND IS SUPPORTED BY THE RECENT *JUSTUS* DECISION BY THE COLORADO SUPREME COURT.**

Plaintiffs fail to meaningfully distinguish *Wage Appeal*. Ignoring the fact that the GABA statute explicitly states the postretirement benefit adjustment applies “on January 1 of each year,” Mont. Code Ann. § 19-3-1605(1), Plaintiffs argue that the right to receive a GABA “has already accrued,” unlike the wage increases in *Wage Appeal*. Pls.’ Resp. at 6-7. Plaintiffs assert that they “worked their entire careers and paid contributions to PERS, part of which went to pay the cost of their GABA.” *Id.* at 7. First, Plaintiffs’ contributions do not directly fund their retirement benefits because retirement benefits are not based on the amount of contributions a member pays, but on a statutory formula based on the member’s

length of employment and salary. Mont. Code Ann. § 19-3-904. In any case, this argument is based on a reliance theory, not a Contract Clause claim. *Hays v. Port of Seattle*, 251 U.S. 233, 237 (1920) (distinguishing between unconstitutional impairment of contracts and ordinary breach of contract); *Horwitz-Matthews v. City of Chicago*, 78 F.3d 1248, 1250 (7th Cir. 1996). Plaintiffs' expectations based on having contributed to PERS during their employment do not affect whether the obligation to permanently fund a fixed-rate GABA is "clearly and unequivocally expressed" in the law.

Plaintiffs likewise reference Mont. Code Ann. § 19-3-901(3)(b) which states that a member who is eligible for service retirement "has a nonforfeitable right to the service retirement benefit . . . ." The "service retirement benefit," however, as explained above and in the State's opening brief, is the base retirement benefit calculated based on longevity and salary. Mont. Code Ann. §§ 19-2-303(48), 19-3-904. These provisions do not include, or even mention, the GABA. In fact, this language creating an "obligation" as to the service retirement benefit serves to prove Defendants' point--it is the base benefit only which is subject to the contract. The GABA, on the other hand, does not contain obligatory language and instead makes clear that the adjustment accrues each year on January 1. As such, the Legislature may adjust the GABA amounts going forward. *Wage Appeal*, 208 Mont. at 43, 676 P.2d at 200.

Defendants' position (and that of the Montana Supreme Court in *Wage Appeal*) is buttressed by the recent *Justus* decision, issued by the Colorado Supreme Court on October 20, 2014, the same day Defendants filed their opening brief (Doc. 47). *Justus* concludes

there is no contract right to perpetually receive a specific formula for postretirement benefit adjustments.

Colorado public pension law, from 2001 to 2009, prescribed a “3.5% compounded” statutory adjustment to the base retirement benefit for public employees. *Justus*, 2014 CO 75, ¶¶ 7, 9. Though referred to by the court as a “COLA,” the adjustment was fixed at 3.5% and did not vary based on inflation or any other cost of living metric. The Colorado adjustment is therefore identical in function to the three percent adjustment under the prior version of Mont. Code Ann. § 19-3-1605. *Id.*, ¶ 9. The Colorado Legislature, in response to “severe underfunding” of the public retirement system, reduced the benefit adjustment formula and tied it to inflation. *Id.*, ¶ 10. The retiree plaintiffs then sued, claiming, like Plaintiffs here, that they were “contractually entitled to receive” the 3.5% adjustment “for life without change,” and that the change in the law was “in violation of the contract clause,” as well as the Takings and Due Process clauses of the U.S. Constitution. *Id.*, ¶ 12.

The Colorado Supreme Court looked to the language of the prior “COLA” statute and determined it, like the prior GABA statute here, did not include “words creating an unmistakable vested contractual right.” *Id.*, ¶ 23. Specifically it did not include “contractual or durational language stating or suggesting a clear legislative intent to bind itself, in perpetuity, to paying PERA members a specific COLA formula.” *Id.*, ¶ 29. In contrast, the base retirement benefit under Colorado law did contain contractual language specifying an “entitlement” to the base benefit “for the life of the retiree.” *Id.*, ¶ 32; *compare to* Mont. Code Ann. § 19-3-901(3)(b) (“nonforfeitable right” to base retirement benefit); § 19-2-502(2) (“benefits . . . are payable pursuant to a contract”). Because the language of the

COLA statute did not offer any “clear indication” of the “legislature’s intent to be bound to provide” a fixed COLA, there was no contract, and thus the court’s inquiry was at an end. *Id.*, ¶ 37. Similarly here, because the GABA statute lacks clear indication of an intent to be permanently bound, and because Mont. Code Ann. § 19-2-502(2) creates a contract only as to base retirement “benefits,” there is no contract for the GABA.

Plaintiffs also fail to counter the persuasive authority from other courts that have wrestled with similar issues. The best Plaintiffs can offer is that *Bartlett v. Cameron*, 316 P.3d 889 (N.M. 2014), involved a COLA, not a GABA, and that Montana’s postretirement adjustment was not variable but fixed. *See* Pls.’ Resp. at 8. But Plaintiffs miss the point. The question in *Bartlett*, as here and in *Justus*, is whether there is a right to a particular formula for determining postretirement benefit adjustments, not whether the formula allows for variables or whether the formula is fixed (though the adjustment formula was fixed in *Justus*). *See Bartlett*, 316 P.3d at 893 (“The question before this Court, then, is whether the COLA is part of the retirement benefit.”) Based on the plain language of the New Mexico statutes and the history of statutory revisions to the postretirement benefit adjustments, the New Mexico Supreme Court unanimously determined that the adjustment was not part of the retirement benefit. *Bartlett*, 316 P.3d at 894-96. The New Mexico Supreme Court faced the same issues this Court faces, and the *Bartlett* case provides a useful roadmap. For the reasons provided in *Wage Appeal*, *Justus*, and *Bartlett*, there is no contract right to an unalterable, fixed GABA in perpetuity, and Defendants are entitled to summary judgment as a matter of law.

**IV. REGARDLESS, THERE IS NO SUBSTANTIAL IMPAIRMENT BECAUSE PLAINTIFFS COULD NOT HAVE REASONABLY EXPECTED THE SPECIFIC GABA RATE TO BE PERMANENT.**

The Colorado Supreme Court determined that because the COLA formula had been amended numerous times, the retiree plaintiffs “could not have reasonably expected” the COLA in effect when they retired would be “protected from change.” *Justus*, 2014 CO 75, ¶ 36. This comports with Montana as well as U.S. Supreme Court precedent. *Neel v. First Federal Savings and Loan Ass’n of Great Falls*, 207 Mont. 376, 392, 675 P.2d 96, 105 (1984) (a “law which restricts a party to gains reasonably expected from a contract is not a substantial impairment.”); accord *Energy Reserves Group v. Kansas Power & Light*, 459 U.S. 400, 411 (1983).

Likewise here, the GABA statute has been amended five times over the past ten years. See Mont. Code Ann. § 19-3-1605; Defs.’ Opening Br. at 14. Additionally, the contract statute states that revisions may be included after retirement if the Legislature specifically provides for inclusion. Mont. Code Ann. § 19-2-502(2) (“Unless specifically provided for by statute, the contract does not contain revisions to statutes after the time of retirement or termination of membership.”) (emphasis added). Finally, the Montana Constitution, unlike the Colorado Constitution apparently (see *Justus* (not referencing constitutional provision)), requires that the retirement system “be funded on an actuarially sound basis.” Mont. Const. art. VIII, § 15(1).

Plaintiffs nevertheless claim that the numerous changes to the GABA “should not diminish expectations that the GABA would be paid for life.” Pls.’ Resp. at 10. Plaintiffs specifically point out that, though changed multiple times, the changes affected “future

employees only.” *Id.* But this ignores the constitutional requirement that the system be funded in a way to ensure actuarial soundness, and the legislative declaration that “any statute may be repealed at any time except when it is otherwise provided therein.” Mont. Code. Ann. § 1-2-110. It was clear that the Legislature had and would change the GABA, and when the presumption that a statute does not create a contract is taken into account, the potential that a future legislature would decrease the GABA rate for all members, including retirees, should have been reasonably expected.

**V. HB 454 IS DIRECTLY RELATED TO THE CONSTITUTIONALLY REQUIRED PURPOSE OF ENSURING ACTUARIAL SOUNDNESS.**

When the Legislature convened for the 2013 session it had a problem--the PERS pension trust fund did not amortize within 30 years and therefore was in violation of the Constitution’s actuarial soundness requirement. Doc. 39, ¶ 36. In order to fully fund the retirement system “on an actuarially sound basis,” the Legislature made several changes, including changing the annual benefit adjustment formula. While Plaintiffs question the manner in which the Legislature addressed this funding shortfall, Pls.’ Resp. at 12, they do not challenge the fact that complying with the Constitution is not only a “significant and legitimate” interest, but a compelling one.

HB 454, including the GABA amendment, was reasonably, indeed directly, related to protecting the retirement fund and ensuring actuarial soundness. *See* Preamble to HB 454 (prior contribution and benefit rates had “no prospect” of funding the system “on an actuarially sound basis,” and “failure” to make changes would place the fund “in jeopardy”). The Legislature is entitled to “meaningful deference” in deciding how to address its

constitutional obligation. *United Auto., Aerospace, Agric. Implement Workers of America Int'l Union v. Fortuno*, 633 F.3d 37, 44 (1st Cir. 2011) (a state's justifications for impairment of its own contracts is still "afforded meaningful deference.").

Plaintiffs nevertheless point to the June 2014 Actuarial Valuation,<sup>1</sup> which projects that the fund will amortize in 29.3 years if HB 454's GABA change is not implemented, and assert that this proves "the GABA reduction in HB 454 was unnecessary and unreasonable." Pls.' Resp. at 12; Actuarial Valuation at 2. But the health of the fund more than a year after the 2013 Legislature passed HB 454 is irrelevant to whether the GABA change was reasonably related to achieving the important purpose of ensuring actuarial soundness when the Legislature passed the law. Even if considered, the 2014 Valuation is barely under the 30-year amortization requirement, and in any case merely shows that market conditions are constantly changing (from a 36.7 year projected amortization period in the HB 454 fiscal note, to 43.7 years in 2013, to 29.1 years just a year later). Defs.' Opening Br. at 15 n.4. 2014 was a banner year for the fund ("returning 17.12% from the value at the prior valuation," Valuation at 3), but 2008-2009 was anything but and the future is anybody's guess. This volatile financial landscape underscores the need for the Legislature to have some flexibility to make statutory changes to the retirement system to address the financial health of the retirement fund.

Plaintiffs also claim that the "GABA reduction deprives Retirees of over" \$696 million worth of benefits. This too though, like the 2014 Valuation, actually cuts in favor of Defendants' position. The flip side of this number is that this represents the cost to the

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<sup>1</sup> Available at <http://mpera.mt.gov/docs/vpers.pdf>.

retirement plan if the GABA is continued at the old rates, and in fact the cost may well be over \$700 million depending on how it is calculated.<sup>2</sup> The Legislature’s decision to reduce the pension trust fund’s liability by over \$700 million is certainly reasonably related to maintaining actuarial soundness.

**VI. THE TAKINGS CLAIM NECESSARILY FAILS BECAUSE PLAINTIFFS HAVE NO PROPERTY RIGHT IN A PERMANENT, FIXED BENEFIT INCREASE.**

Plaintiffs, in their opening brief, made a bare-bones, paragraph-long argument that HB 454 effectuated a taking, citing to no legal authority other than the Constitution. Doc. 38 at 20. After the insufficiency of this argument was pointed out by Defendants, Doc. 47 at 19, Plaintiffs now attempt to make a more robust argument in their reply. Doc. 50 at 15-19. Plaintiffs’ attempt is too little too late. Their takings claim is essentially a rehash of their Contract Clause claim to an unalterable GABA formula. Pls.’ Resp. Br. at 16 (linking their property claim to a contract with the State). As succinctly stated by the Colorado Supreme Court, because Plaintiffs have no contract right to a particular benefit adjustment, they likewise “have no property right in a particular [GABA] . . . [and] their Takings claims . . . necessarily also fail.” *Justus*, 2014 CO 75, ¶ 37.

Plaintiffs also point this Court to *Lynch v. United States*, an odd choice given that the United States Supreme Court there described pensions as “gratuities” that create no vested rights. 292 U.S. 571, 577 (1934) (“Pensions, compensation allowances and privileges are

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<sup>2</sup> The difference between the actuarial liability between the 2013 valuation with the GABA change, and the 2014 valuation without the change, is slightly over \$1 billion. 2014 Actuarial Valuation at 2.

gratuities. They involve no agreement of parties; and the grant of them creates no vested right.”). Moreover, the *Lynch* case dealt with a “consent to sue” provision. Plaintiffs fail to explain how the case has any relevance to whether an obligation to pay money gives rise to a takings claim. In any case, other courts have observed that *Lynch* was effectively overruled by *Connolly v. Pension Benefit Guaranty*, 475 U.S. 211 (1986). *Pro-Eco, Inc. v. Board of Comm’rs*, 57 F.3d 505, 510 n.2 (7th Cir. 1995) (reading *Connolly* as overruling *Lynch* “to the extent it flatly holds that contracts are property that the government may not take without compensation.”). The *Lynch* case does not support Plaintiffs and Plaintiffs’ takings claim fails.

### CONCLUSION

For the reasons stated above, this Court should grant summary judgment in favor of Defendants.

Respectfully submitted this 24th day of November, 2014.

TIMOTHY C. FOX  
Montana Attorney General  
215 North Sanders  
P.O. Box 201401  
Helena, MT 59620-1401

By: 

\_\_\_\_\_  
MICHAEL G. BLACK  
Assistant Attorney General

By: 

\_\_\_\_\_  
J. STUART SEGREST  
Assistant Attorney General

**CERTIFICATE OF SERVICE**

I hereby certify that I caused a true and accurate copy of the foregoing document to be mailed to:

Mr. Leo Berry  
Mr. Chad E. Adams  
Ms. Jessie L. Luther  
Browning, Kaleczyc, Berry & Hoven, P.C.  
800 N. Last Chance Gulch, Suite 101  
P.O. Box 1697  
Helena, MT 59624-1697

DATED: 11/24/14 J. H. H. H.