

STATE OF MINNESOTA

DISTRICT COURT

COUNTY OF RAMSEY

SECOND JUDICIAL DISTRICT

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Howard Swanson and Lambert Niesen, Steven  
Bornus, Richard Maus, James R. Otto, and William  
H. Kuretsky,

CASE TYPE: Other Civil

Court File No. 62-CV-10-05285  
Hon. Gregg E. Johnson

Plaintiffs,

vs.

**ORDER AND MEMORANDUM**

State of Minnesota, Public Employees' Retirement  
Association of Minnesota, Minnesota State  
Retirement System, Teachers Retirement Association  
of Minnesota, Thomas L. Marshall (in his official  
capacity), Mary Most Vanek (in her official  
capacity), Mary Benner (in her official capacity),  
David Bergstrom (in his official capacity), Martha  
Lee Zins (in her official capacity), and Laurie Fiori  
Hacking (in her official capacity),

Defendants.

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The above-entitled matter came before the undersigned on March 22, 2011, upon completion of discovery and pursuant to the Plaintiffs' and Defendants' cross-motions for summary judgment.

Attorneys Stephen Pincus and Susan Coler represented the Plaintiffs. Assistant Attorneys General Rita Coyle DeMeules and Carla Heyl represented the Defendants.

Based on the files, records, and proceedings herein, the Court makes the following Order:

1. Plaintiffs' Motion for Summary Judgment pursuant to Minn. R. Civ. P. 56 is denied in its entirety.

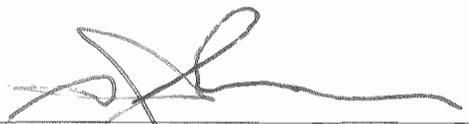
2. Defendants' Motion for Summary Judgment pursuant to Minn. R. Civ. P. 56 is granted in its entirety.

3. Claims I through VI of Plaintiffs' Amended Complaint are hereby dismissed with prejudice.

4. The attached Memorandum is incorporated into and made a part of this Order.

**LET JUDGMENT BE ENTERED ACCORDINGLY.**

Dated: June 29, 2011



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**GREGG E. JOHNSON**  
District Court Judge

**MEMORANDUM**

Plaintiffs, on behalf of themselves and a putative class of persons, challenge the constitutionality of legislative amendments made in 2009 and 2010 to the pension laws governing Minnesota's previously retired public employees' retirement benefits. Plaintiffs contend that the legislation which reduced the formula for post-retirement adjustments without due compensation violates the contracts and taking clauses of the United States and Minnesota Constitutions. Plaintiffs also assert a 42 U.S.C. § 1983 action. Statutes are presumed constitutional and should be declared otherwise only if it is shown beyond a reasonable doubt that a constitutional provision is violated. *Scott v. Minneapolis Police Relief Ass'n, Inc.*, 615 N.W.2d 66, 73 (Minn. 2000).

The sole issue before the Court is whether the Legislature has the authority to amend a statutory formula that is used to calculate the availability and amount of future adjustments to public retirees' pension annuities.

The issues before the court are:

- (1) whether any contract or promise to a particular statutory formula exists that has been unconstitutionally impaired by amendments modifying that formula; or,
- (2) whether a legislative amendment to a statutory formula is an unconstitutional taking of property without just compensation; or,
- (3) whether the individual defendants' acts violate 42 U.S.C. § 1983.

In review of all submissions of counsel, including memorandum of law, exhibits and affidavits, the court agrees with counsel that there are no material facts in dispute and that this matter is ripe for summary judgment.

The Court concludes that Plaintiffs have not met their burden to show unconstitutionality beyond a reasonable doubt.

First, statutes are not contracts absent plain and unambiguous terms that show an intent to contract. To decide otherwise risks a serious intrusion into the Legislature's policymaking authority. The relevant statutory language does not encompass a legislative contract or promise to refrain from amending the statutory formula, for those public employees who have retired. In the Minnesota Supreme Court's 1983 decision, *Christensen v. Minneapolis Municipal Retirement Bd.*, 331 N.W.2d 740 (Minn. 1983), the promissory estoppel analysis used there dictates a balancing of retirees' interests with the state's paramount public interests. When this is done in light of the undisputed facts here, the Legislature plainly sought to balance the interests of all plan members with the risk posed by an unprecedented financial deterioration in plan assets. In the end, the balance achieved fully preserved retirees' pension annuities, provided for annual adjustments to those annuities, and stabilized the financial deterioration that

threatened Minnesota's public pension Plans. There is no legal or equitable reason for the judiciary to interfere with this legislative policy decision.

Second, the challenged legislative amendments are neither an impairment or nor a taking of constitutional proportions. These amendments are, instead, a minimal alteration in the calculation of future adjustments to retirees' annuities and a reasonable response to a fiscal threat that jeopardized the long-term interests of Plan members, the State, and the State's taxpayers. The Legislature prudently enacted Plan-wide changes that spread the burden of the financial crisis through contribution increases, changes in eligibility requirements, and changes in formulas for annuities and future adjustments. Given the considerable legislative discretion over retirement policy, including the amount and duration of benefits, Plaintiffs have not met their burden to show unconstitutionality beyond a reasonable doubt.

Finally, Plaintiffs' claims fail because they rest on a fundamental disagreement with the Legislature's policy choices and urge the Court to re-write the legislation so it applies only to future retirees. All of these arguments and choices were debated in the public legislative process. This is not a debate for the Court to join. The Legislature is charged with setting state retirement policy, the changes made to the statutory formula for future adjustments to retirement annuities is well within the scope of that body's policy and law-making authority. Given the preservation of retirees' pension annuities, the opportunity for future increases, and the stabilization of the Plans, the Court would threaten the balance of powers between the legislative and judicial branches by second-guessing this legislative wisdom.

A comprehensive statutory structure governs each individual plan, as well as the collective interests of the Plans. Each retirement plan before the Court is governed by a separate chapter, *e.g.*, Minn. Stat. ch. 352 (MSRS); Minn. Stat. ch. 353 (PERA); Minn. Stat. ch.

354 (TRA). Each Defendant Plan is also governed by laws applicable generally to all public plans, *e.g.*, Minn. Stat. chs. 356, 356A. Together, these statutes express State retirement policies, which include preserving adequate retirement benefits for all members and protecting the fiduciary interests of all members, the State, and its citizens. Minn. Stat. § 356.001, subd. 1; Minn. Stat. § 356A.04, subd. 1.

Each plan serves a distinct group of public service employees. The Teachers Retirement Association (“TRA”) provides retirement, disability, and survivor benefits for Minnesota’s public elementary and high school teachers and administrators, and certain Minnesota State Colleges faculty. Minn. Stat. § 354.41. The Minnesota State Retirement System (“MSRS”) provides similar benefits through plans that generally cover state employees, University of Minnesota civil service employees, elected officials including legislators, public safety personnel, and unclassified state employees. Minn. Stat. §§ 352.021, 352.81-.91; Minn. Stat. § 352C.091; Minn. Stat. § 490.123. The Public Employees Retirement Association (“PERA”) provides similar benefits to public employees from school districts, counties, and local units of government, including local police, firefighters, and correctional officers. Minn. Stat. § 353.01, subd. 2.

Minnesota’s tax revenues contribute to the funding requirements for these programs. In order to monitor the fiscally responsible use of taxpayer funds, the Minnesota Legislature requires an annual actuarial review of the financial status of each Plan. Minn. Stat. §§ 356.20; 356.214; 356.215, subd. 2.

The Plans’ actuary must annually conduct a valuation that measures all aspects of the benefit plan, using assumptions for demographic or economic factors. Minn. Stat. § 356.215. The report is filed annually with the Legislative Commission on Pensions and Retirement.

The State Board of Investment (“SBI”) invests the assets of the State’s pension funds to generate additional funds for member benefits. Minn. Stat. §§ 11A.01, 11A.23. SBI is required to invest the State’s pension assets “responsibly” and to “maximize the total rate of return without incurring undue risk.” Minn. Stat. § 11A.01. SBI, through its report to the State Auditor, provides the Legislature with input on the investment performance of the Plans’ invested assets. Minn. Stat. § 356.219.

Each Plan’s Board of Directors and officers, and SBI owe a fiduciary duty to active, deferred, and retiree members; to the State; and to the State’s taxpayers. Minn. Stat. § 356A.04, subd. 1. These fiduciaries are required to act “in a manner consistent with the law,” Minn. Stat. § 356A.05(b), and to manage the Plans by exercising the judgment and care dictated by prevailing circumstances “that persons of prudence, discretion, and intelligence would exercise in the management of their own affairs, not for speculation, considering the probable safety of the plan capital as well as the probable investment return to be derived from the assets.” Minn. Stat. § 356A.04, subd. 2. This fiduciary obligation extends to the investment and expenditure of plan assets, the determination of the amount and duration of benefits, and the determination of plan funding requirements. Minn. Stat. § 356A.02, subd. 2.

Once eligible and retired, a Plan member qualifies for retirement benefits. Minn. Stat. § 352.115, subd. 1 (MSRS qualifications); Minn. Stat. § 353.29, subd. 1 (PERA qualifications); Minn. Stat. § 354.44, subd. 1 (TRA, same). A member’s retirement annuity is calculated based on a statutory formula established by the Legislature and generates an annuity that varies for each retiree depending on factors such as salary and credited years of work.

Historically, Minnesota’s Plans’ benefits were paid from a two-fund structure. These two funds were known as the Active Fund and the Post Fund.

Each individual Plan (TRA, PERA, or MSRS) maintained a fund into which the contributions made by or on behalf of active members, and earnings on those contributions were held (the “Active Fund”). Minn. Stat. § 352.04, subd. 1 (a) (2006) (MSRS-General Fund); Minn. Stat. § 353.27, subd. 1 (2006) (PERA General Fund); Minn. Stat. § 354.42, subd. 1a(b) (2006) (TRA Fund).

A separate single fund held the combined retiree assets for all three statewide funds, i.e., the present value of reserves sufficient to fund retirees’ monthly annuity payments, assuming a certain level of post-retirement investment earnings (the “Post Fund”). Minn. Stat. § 11A.18, subd. 2 (2008). At retirement, the actuarially determined reserves for the retiree’s annuity, discounted by the legislatively-set interest rate, were transferred from the retiree-member’s Active Fund to the Post Fund. Minn. Stat. § 352.119, subd. 2(a) (2006) (MSRS transfer requirement); Minn. Stat. § 353.271, subd. 2(a) (2006) (PERA, same requirement); Minn. Stat. § 354.63, subd. 2(1) (2006) (TRA, same requirement); Minn. Stat. § 11A.18, subd. 6 (2006) (directing SBI to hold transferred retiree assets); Minn. Stat. § 356.215, subd. 8 (2006) (setting post-retirement interest rate for all funds). Until 2009, retirees’ benefits were paid from the assets maintained in the Post Fund.

In addition to a monthly retirement annuity, retired Plan members have received an annual adjustment to that annuity. The purpose of this annual adjustment is to address the impact of economic inflation over the retirement years. Since 1970, a statutory formula has been used to determine the availability and amount of any annual adjustment.

Once granted, neither the formula-based retirement annuity, nor the annuity paid after an adjustment is granted, can be reduced. Minn. Stat. § 354.05, subd. 26 (2008).

In 1992, based upon a recommendation of the Legislative Auditor, the Legislature enacted a statutory formula that used both inflation and investment performance to calculate funds available for post-retirement adjustments. 1992 Minn. Laws 1354, Chapter 530. The 1992 formula also used a percentage for adjustments, based on inflation (up to 3.5%) plus net investment returns (after required 5%). Minn. Stat. § 11A.18, subd. 9(b), (c) (1992). The inflation component was reduced to 2.5% in 1997. 1997 Minn. Laws 2648, ch. 233, Art. I, § 5.

The 1992 formula required the Post Fund's investment performance, including gains and losses, to be spread over five (5) years. Minn. Stat. § 11A.18, subd. 9 (c)(8) (1992). The purpose of the five-year spread, referred to as "smoothing," was to diminish the impact of year-to-year market swings and volatility.

The 1992 formula generated adjustments that exceeded inflation in several years, sometimes by double digits. It also had no mechanism to protect against de-stabilizing decreases in asset values. In 2001, the Post Fund had investment losses of 6.9%, but because gains from earlier years were still used in the formula (for "smoothing"), retirees' annuities were adjusted by 9.5%. In 2002, the Post Fund's investment losses increased to 7.8%, but an adjustment of 4.5% was granted by operation of the formula. Between 2000 and 2003, the Post Fund shifted from a surplus of \$3.0 billion to a deficit of \$5.1 billion. By 2003, the Post Fund's deficiency reached the point where no investment-based adjustment could be granted. The increase paid in 2003 and 2004 simply matched inflation (0.7% and 2.1%, respectively).

The Post Fund deficiency between 2004-2005 was approximately \$4 billion.

The Plans jointly evaluated possible proposed legislative amendments to the 1992 statutory adjustment formula, and from time to time, made proposals to the Legislature supporting such amendments.

In 2006, the Legislature amended the statutory formula to impose an overall 5% cap on any future adjustments, effective 2010. 2006 Minn. Laws 1051, ch. 277, Art. 1, § 3.

The 5% cap did not resolve the Post Fund's deficiency and by July 1, 2006, the Post Fund had a \$4 billion deficiency and was approximately 84% funded.

After the 2006 legislative session, the Plans explored options for resolving the Post Fund's persistent deficit, particularly in light of concerns expressed by SBI and the Plans' actuaries.

In 2007, a Post Fund Committee comprising Board members from all 3 Plans, met and evaluated input from the Plans' Directors, SBI, actuaries, and retiree and active members, and developed recommended proposals for legislative changes to the Post Fund including changes to the statutory adjustment formula.

The 2008 Legislature adopted the Plans' recommended solution for the Post Fund deficiency, which was based on two possible scenarios. In the first scenario, if the Post Fund recovered (defined as a funding ratio no lower than 80%), the existing inflation component (100% of inflation, up to 2.5%) would be used as the adjustment formula. 2008 Minn. Laws 1483-91. If investment returns were sufficient (i.e., in excess of 8.5% and Post Fund more than 100% funded), an additional increase could be authorized with an overall cap of 5% annually.

In the second scenario, if the deficiency worsened, the Post Fund would be dissolved and its assets returned to the MSRS, TRA, or PERA Active Funds. The legislation set two benchmarks or "triggers" for a potential Post Fund dissolution: (a) a funding ratio of less than 85% for 2 consecutive years; or, (b) a funding ratio of less than 80% for 1 year. 2008 Minn. Laws 1491-92. If one of the triggers occurred and the Post Fund was dissolved, a flat 2.5% annual adjustment would be authorized.

For the fiscal year ending June 30, 2008, the Post Fund's investment return was a negative 5.2%. On November 21, 2008, SBI announced that the Post Fund's funded ratio at the end of fiscal year 2008 was 79.7%, thus falling below the statutory floor and triggering the Fund's dissolution. On January 1, 2009, retirees were granted the last post-retirement adjustment from the Post Fund authorized by Minnesota Statute Section 11A.18. *Id.* No adjustment was made based on investment returns because the Post Fund continued to report a deficiency of \$5.9 billion.

The 2008 Legislation required the Plan Directors to recommend the necessary legislative proposals to conform various pension laws with a dissolved Post Fund should that event come to pass. Legislation was proposed for the 2009 session to implement the Post Fund's dissolution and merger with the Active Funds. The actual merger, or transfer, of Post Fund assets into the designated Active Funds occurred as of June 30, 2009. Thereafter, each Plan separately held and maintained the combined active and retired members' assets in a single fund.

Between the triggered dissolution of the Post Fund in 2008 and the passage of the 2009 technical amendments to implement that dissolution, the nation's economy entered a significant financial crisis and Minnesota's public pension funds were severely impacted.

In the first six (6) months of fiscal year 2009, TRA's investment performance fell 21%; for the entire fiscal year, returns fell 18.8%. TRA's funding ratio on a market valuation basis was 60%, leaving TRA with an unfunded liability of over \$9 billion. The TRA actuary, Mercer, warned that fund exhaustion, or insolvency, could be reached by 2032, and that without changes in contribution rates, benefit provisions, or other plan elements, TRA's funded status would continue to deteriorate.

The funding ratio for PERA's General Fund fell from approximately 72% in fiscal year 2008 to slightly less than 54% in fiscal year 2009. PERA's Police & Fire and Correctional Plans had similarly precipitous funding declines, with both funds well under 75% funding ratios. PERA's actuary projected a continuing downward trend in funding ratios.

MSRS, which in 2006 had a funding status of 96.23%, saw losses reach over 30% in the 2009 fiscal year, ultimately lost over 19% in its funds, and by June 30, 2009, faced a funding ratio of just 65.61%. MSRS's funds lost over \$2.2 billion in net assets. Actuarial projections showed funding levels below 20% in less than 20 years if no corrective measures were taken.

Each Plan concluded that attempting to ride out the market downturn was inconsistent with the statutory fiduciary duty owed to members, the State, and the State's taxpayers. Each Plan therefore recommended a package of changes to their respective funding and benefit laws that were designed to stabilize the fund and allow a recovery from the projected downward trends.

The Legislature's actuary concluded that the Plans had suffered "significant declines" in their funding ratios and that the Plans' future investment returns were not likely to be sufficient to overcome the deficit. Further, given the 5-year smoothing process, the actuary concluded that there were significant losses yet to be recognized and that the Plans' funding ratios would likely decrease further. The Plans concluded that relying on investment returns alone risked the possibility of further deterioration in funded status, which in turn raised the cost of possible future solutions.

The Plans also considered Minnesota's historical pattern of balancing the contribution requirements evenly between employer and employee and considered the financial impact of recent contribution increases. Actuarial projections showed that substantially higher

contribution rates, at levels deemed financially burdensome, would be required to solve the funding crisis. Despite these concerns, the Legislature increased employer contribution rates for TRA, PERA, and MSRS State Patrol member-employers. Employee contribution rates were increased for TRA, MSRS State Patrol, and PERA Police & Fire members.

Each Plan also considered the possibility of limiting proposed changes to new hires or future retirees. Based on actuarial input, each Plan concluded that the savings needed would only be recognized too far in the future to be effective in immediately addressing the current funding deficiencies.

Vesting requirements for new members were ultimately increased for MSRS-General, Correction, and State Patrol members, and for all PERA Plan members. Changes were also made to the early retirement reduction factor for some MSRS Plan members.

During the 2010 legislative session, the Minnesota Legislature considered the Funds' Financial Sustainability proposals, with testimony and debate held in both House and Senate Committees, the LCPR, and on the House and Senate Floors. The Legislature ultimately passed the 2010 Financial Sustainability legislation with widespread bipartisan support and was signed into law by then Governor Pawlenty.

The 2010 Legislature amended contribution rates, vesting periods, annuity formulas, interest rates, and the post-retirement adjustment formula, although the changes made for each Plan depended on the Plan's individual economic and demographic circumstances.

For MSRS-General and most other MSRS plans, the post-retirement adjustment was reduced from 2.5% to 2.0%, with the higher level restored when MSRS achieves 90% funding on a market value basis; for the State Patrol Plan, the post-retirement adjustment was reduced from 2.5% to 1.5%. 2010 Minn. Laws 1345-51, ch. 359, art. 1, §§ 76-81.

For PERA-General and most other PERA plans, the post-retirement adjustment was reduced from 2.5% to 1.0%, with the higher level restored when PERA achieves 90% funding on a market value basis. 2010 Minn. Laws 1345-51, ch. 359, art. 1, §§ 76-81.

For TRA, the post-retirement adjustment was maintained at 0% in 2011 and 2012. Adjustments will be 2.0% thereafter. A 2.5% adjustment will be effective when TRA achieves 90% funding on a market value basis. 2010 Minn. Laws 1345-51, ch. 359, art. 1, §§ 76-81.

Summary judgment is proper where there are no genuine issues of material disputed facts and the applicable law will resolve the controversy. Minn. R. Civ. P. 56.03; *DLH, Inc. v. Russ*, 566 N.W.2d 60, 69 (Minn. 1997). “‘Summary judgment [is] a fully appropriate procedural vehicle’ for a court to use when applying statutory language to the undisputed facts of a case.” *Wallin v. Letourneau*, 534 N.W.2d 712, 715 (Minn. 1995) (quoting *A.J. Chromy Constr. Co. v. Commercial Mechanical Servs., Inc.*, 260 N.W.2d 579, 581 (Minn. 1977)). This matter is ripe for summary judgment because the public record of facts are undisputed and the law is clear.

In reviewing the facts on which both sides rely, the Court has to apply certain well-settled evidentiary standards. First, only material facts — those that are outcome-dispositive given the controlling law — are relevant. *Bond v. Comm’r of Revenue*, 691 N.W.2d 831, 836 (Minn.), *cert. denied*, 545 U.S. 1116 (2005). Second, statutes are presumed constitutional and challenges asserting otherwise “are disfavored.” *Minneapolis Teachers Retirement Fund Ass’n v. State*, 490 N.W.2d 124, 127 (Minn. Ct. App. 1992) *rev. denied* (Minn., Oct. 28, 1992). The Court must invoke every presumption in favor of sustaining that constitutionality and “declare statutes unconstitutional only when absolutely necessary and with extreme caution.” *Council of Indep’t Tobacco Mfrs. of America v. State of Minnesota*, 713 N.W.2d 300, 305 (Minn.) *cert.*

*denied*, 549 U.S. 1052 (2006). Third, the party challenging the constitutionality of legislation must establish the alleged unconstitutionality “beyond a reasonable doubt.” *Minneapolis Teachers Retirement Fund Ass’n*, 490 N.W.2d at 127.

The Court will apply the beyond a reasonable doubt standard to its analysis of the following issues that are raised by the parties’ cross-motions:

- (1) whether the challenged legislation operates retroactively or prospectively;
- (2) whether there is a contract or promise to use a particular formula for post-retirement adjustments to retirees’ annuities;
- (3) if there is a contract or promise, whether that contract or promise has been impaired, and, if there is an impairment, whether the impairment is substantial or is permissible legislative action taken in the public interest;
- (4) whether there is a protected property interest that has been taken without just compensation; and,
- (5) whether there is a basis for the Section 1983 claims.

These issues are considered in light of the specific pension right to which Plaintiffs claim they are entitled: “to receive pension increases based on the statutory postretirement adjustment formula that was in effect at the time they retired.”

Plaintiffs argue that the challenged legislation operates retroactively by taking away a statutory post-retirement adjustment formula to which they became entitled on the date of their retirement.

The Defendants, in contrast, argue that the challenged legislation is prospective only. They note that nothing was taken away by the challenged legislation because all benefits

previously paid were unaffected. The Defendants further argue that no court has found an unconstitutional impairment in legislation that has a prospective-only effect.

The Court notes that, by its express terms, the challenged legislation operates prospectively only. 2009 Minn. Laws 2302, Ch. 169, art. 1, § 73; 2010 Minn. Laws 1346-51. That is, the amended statutory formula was effective for adjustments granted *after* the effective date of the legislation. This undisputed fact, by itself, is strong evidence that the legislation is not retroactive. Minn. Stat. § 645.21 (no law “shall be construed to be retroactive unless clearly and manifestly so intended by the legislature”).

What’s more, prior to its repeal in 2009, the statute had no terms that limited its application to any particular group or class of retirees, nor that defined its use by date of retirement. Minn. Stat. § 11A.18, subd. 9 (2008).

Plaintiffs rely on *Butler v. Minneapolis Police Relief Ass’n*, 166 N.W.2d 705 (Minn. 1969); and *Krake v. Minneapolis Fire Dept. Relief Ass’n*, 284 N.W. 884 (Minn. 1939) for the rule that the law in force when the claim to a pension arises governs the right to the pension. This is a correct statement of the rule in these decisions. However, the issue is not whether Plaintiffs are entitled to a pension benefit. It is undisputed that Plaintiffs have received their annuities, and those annuities have been adjusted annually. The *Butler/Krake* rule doesn’t apply here because Plaintiffs have received the pension benefit to which they became entitled at the time of their retirement. The *Butler/Krake* rule addresses the eligibility for a claimed benefit, rather than how the benefit is calculated.

The post-retirement adjustment process is an annual event that each year uses a formula to determine the amount of that year’s adjustment. Minn. Stat. § 11A.18, subd. 9 (2008). It is available to all members receiving an annuity, regardless of retirement date. The adjustment

thus logically rests on a formula used *as of the date of the calculation*, not the date of retirement.

The legislation operates prospectively since no retiree's basic retirement annuity has been reduced. No sums previously paid to any retiree were taken away. No retiree was divested of the adjustment generated by a previous formula and added to a basic retirement annuity. These undisputed facts are strong evidence that the challenged legislation operates prospectively, not retroactively.

The Court concludes that the Legislature neither contracted to use, nor promised to use, the formula in effect on the date of retirement for future post-retirement adjustments to retirement annuities. The Court now turns to the assertion by Plaintiffs that a contract or promise to use a particular statutory formula has been unconstitutionally impaired.

Minnesota has generally evaluated challenges to changes in pension program terms under one of three contract theories: (a) express or unilateral contract, *Sylvestre v. State*, 214 N.W.2d 658 (Minn. 1973); (b) implied contract, *AFSCME Councils 6, 14, 65 & 96 v. Sundquist*, 338 N.W.2d 560 (Minn. 1983); or, (c) quasi-contract or promissory estoppel, *Christensen v. Minneapolis Municipal Retirement Bd.*, 331 N.W.2d 740 (Minn. 1983). The State Defendants correctly point out that the *Christensen* Court declined to apply "strict contract" principles, 331 N.W.2d at 747. Nevertheless, contract principles continue to have some relevance in the pension context, *Sundquist*, 338 N.W.2d at 566 (stating *Christensen* "augmented the contract approach").

The plain statutory language says nothing about a contract. Thus, there is no express contract to use only the statutory adjustment formula that is in effect as of a member's retirement. To conclude otherwise, as Plaintiffs urge, would significantly constrain the

legislature's ability to respond to fiscal integrity concerns, which in turn would be an extraordinary expansion of the Contract Clauses of the United States and Minnesota Constitutions. Those constitutional provisions have long been understood to permit legislative action in the form of statutory changes, either by amending or repealing statutes, because legislation is presumed to simply state the policy that is effective until the Legislature declares otherwise. *National Railroad Passenger Corp. v. Atchison, Topeka & Santa Fe Ry. Co.*, 470 U.S. 451, 465-66, 105 S.Ct. 1441, 1451-52 (1985); *United States Trust Co. v. New Jersey*, 431 U.S. 1, 17, 97 S.Ct. 1505, 1515 (1977). Thus, statutes do not create contract rights absent compelling evidence that the State intended to create such rights. *Peterson v. Humphrey*, 381 N.W.2d 472, 475 (Minn. Ct. App.), *rev. denied* (Minn. Apr. 11, 1986).

Here, no plain and unambiguous language shows the Legislature intended to confer contract rights to a particular adjustment formula. Until 2009, the Plans adjusted retirees' annuities after SBI calculated the percentage amount. Minn. Stat. § 352.119, subd. 2(b) (1992) (MSRS); Minn. Stat. § 353.271, subd. 2(2) (PERA); Minn. Stat. § 354.63, subd. 2(2) (TRA). Similarly, SBI was required only to "use the procedures" to calculate "whether an adjustment is payable." Minn. Stat. § 11A.18, subd. 9(a) (1992) (noting procedures to be used "annually"). This language falls far short of plain and unmistakable terms that confer express contract rights to a formula.

Plaintiffs correctly point out that the Legislature did not reserve the right to amend the statutory formula in the future. But this argument misconstrues legislative authority: the right to change state policy via amended statutory terms is an inherent element of legislative power. *United States Trust Co.*, 431 U.S. at 17. The Legislature need not reserve the right to exercise

its inherent authority. *Christensen*, 331 N.W.2d at 748 (noting State’s interest in modifying pension program in the public interest is “paramount”).

Plaintiffs also point to the 1984 repeal of the Plans’ “no contract” statutes, which all stated in one form or another that the Plans’ statutory terms did not “create or give any contract” rights to Plan members. Minn. Stat. § 352.22 (1980); Minn. Stat. § 353.38 (1980); Minn. Stat. § 354.07, subd. 8 (1980). After the 1983 decisions in *Christensen* and *Sundquist*, the Legislature repealed these provisions. 1984 Minn. Laws 1086, ch. 564, § 51. Repeal of the no-contract provisions did not narrow the Legislature’s inherent powers. If mandatory statutory language does not create contract rights, surely repealing statutes that acknowledge the absence of such rights does not thereby implicitly give rise to such rights.

In addition, rejecting Plaintiffs’ claimed contract right to a particular formula is consistent with the legislative intent to amend, revise, and if necessary repeal, pension statutes when doing so is consistent with maintaining those plans for the benefit of all members. Minn. Stat. § 356.001, subd. 1. In fact, the broad fiduciary duty owed by the Plans and SBI, to Plan members, to the State, and to its taxpayers, necessarily contemplates that the Legislature will act upon recommendations made in the exercise of that duty, through future amendments to statutory terms for benefits, eligibility for benefits, or the amount or duration of benefits given prevailing circumstances. Minn. Stat. § 356A.02, subd. 2; Minn. Stat. § 356A.04.

The absence of contract right to a statutory formula is also logically consistent with the Legislature’s stated policy for the State’s public pension programs: to provide a benefit adequate at retirement and in light of changes in the economy. Retained legislative flexibility to respond to unintended operational consequences of plan terms, or funding deficiencies stemming from economic and marketplace forces beyond the control of the Legislature and the

Plans, is critical to fulfilling the broader public interest in providing a benefit adequate for all members. *Christensen*, 331 N.W.2d at 751 (correcting a fiscal misjudgment can be a legitimate public purpose).

The conclusion that the statutory language does not confer contract rights in plain and unambiguous terms also disposes of Plaintiffs' unilateral contract theory. This theory has been applied just once in a public pension case, in *Sylvestre v. State*, 214 N.W.2d 658 (Minn. 1973). The Court's decision to do so was heavily influenced by the constitutional basis for the retiree-judges' office and compensation. *Id.* at 662 ("The position of judge of the district court is not created by the legislature, but derives from the Constitution of the State of Minnesota."). The *Christensen* Court, just ten years later, recognized *Sylvestre's* unilateral contract theory had no application outside its unique facts. *Christensen*, 331 N.W.2d at 747.

There is no implied contract to a particular post-retirement adjustment formula. An implied contract is "established by circumstantial evidence showing a mutual intention to contract." *Sundquist*, 338 N.W.2d at 567. The mere existence of a comprehensive statutory system regulating Minnesota's pension funds is not such a contract. *Minneapolis Teachers Retirement Fund Ass'n*, 490 N.W.2d at 128-29 (reviewing decades of legislation requiring contributions to pension fund, and concluding legislation did not represent a state contract to keep fund actuarially sound); *Sundquist*, 338 N.W.2d at 567 (holding State did not intend to guarantee "fixed levels of employee retirement contributions" simply by enacting statutory requirements for contributions). If the express statutory terms do not create contract rights, it is inconceivable that the same language would show a "mutual intention" to enter into an implied contract. The history of legislative amendments to the statutory adjustment formula, and the longstanding, reserved legislative flexibility and discretion to amend pension benefits in the

interests of all members, the State and its taxpayers are inconsistent with the notion of a “mutual intention to contract” and an unwarranted restriction of legislative flexibility. *Duluth Firemen’s Relief Ass’n*, 361 N.W.2d at 386; *Christensen*, 331 N.W.2d at 747 (noting “conventional contract approach” deprives the employer-employee relationship “of a needed flexibility”).

Plaintiffs argue that the Plans’ communications with members about post-retirement adjustments are consistent with the understanding that retirees’ benefits are subject to contract protections; that the statutory formula together with those communications reflect a mutual intention to contract. The Court has already concluded that the relevant statutes confer no contractual right to a particular formula for post-retirement adjustments. The Plans’ communications cannot elevate non-contractual language to a binding contract. *Axelson v. Minneapolis Teachers’ Retirement Fund Ass’n*, 544 N.W.2d 297 (Minn. 1996). Thus, the Plans’ communications cannot create contract rights nor are they consistent with any such rights. This is particularly true given that the Plans routinely reminded members that the law, not their communications, controlled.

With respect to Plaintiffs’ claims under the theory of promissory estoppel, the statutory language is a barrier to this claim. Since the statutory language does not demonstrate the existence of a binding contract, it fails to reflect the existence of a promise to refrain from amending the statutory formula. This is particularly true given that a promissory estoppel claim necessarily invokes equitable principles. *Christensen*, 331 N.W.2d at 749 (“Promissory estoppel . . . may be applied against the state to the extent that justice requires.”). There are two relevant factors in the promissory estoppel inquiry:

- (1) What has been promised by the state? and
- (2) to what degree and to what aspects of the promise has there been reasonable reliance on the part of the

employee? Not every promise in all its implications is necessarily enforceable under promissory estoppel. Estoppel applies only to avoid injustice.

*Id.* at 749. The promise enforced in *Christensen* was the continuing existence of a pension program, which the challenged legislation, in contrast, had fully suspended for a period of almost 12 years. *Id.* at 748. Here, Plaintiffs continue to receive their monthly annuities, those annuities have been adjusted, and no sums have been withheld from retirees.

Justice does not, however, require enforcement of an alleged promise to a particular adjustment formula. Retirees have received adjustments in the last 2 years greater than would have been granted under the 1992 formula. In addition, justice does not require enforcing Plaintiffs' claimed promise over all others. This assumption is inconsistent with the statutory fiduciary duty, Minn. Stat. § 356A.02, and elevates Plaintiffs' expectation of greater future adjustments over the State's paramount interest in the fiscal stability of these plans. The equitable principles that underlie promissory estoppel do not support Plaintiffs' claim. *Christensen*, 331 N.W.2d at 749 (claim applies only to avoid an injustice and pension program terms are "subject to reasonable legislative modification").

Finally, the promissory estoppel claim fails because Plaintiffs' claimed reliance is unreasonable as a matter of law. *Christensen*, 331 N.W.2d at 749. The statutory language is inconsistent with the promise on which Plaintiffs claim reliance. In addition, the Plans' repeatedly advised members that the law governed their retirement benefits. The Plans also publicly evaluated possible formula changes, or made proposals to the Legislature for changes in 2000, 2003, 2004, 2005, 2006, and 2007. Any claimed reliance on the continuing existence of the 1992 adjustment formula is not reasonable in light of this record.

If there is no enforceable contract or promise, there is no basis for a contract impairment claim. *Sundquist*, 338 N.W.2d at 566. However, assuming there was, Plaintiffs have failed to

demonstrate beyond a reasonable doubt that such contract or promise was substantially impaired.

The Contract Clause of the United States Constitution states: “No State shall . . . pass any . . . Law impairing the Obligation of Contracts.” U.S. Const. art. I, § 10. Despite the broad language of this clause, not every impairment is a constitutional violation. A law is invalid under the Contracts Clause *only if* it substantially impairs a contractual relationship and is not reasonable and necessary to serve an important and legitimate public purpose. *United States Trust Co.*, 431 U.S. at 17; *Christensen*, 331 N.W.2d at 750-51. Three (3) factors must be shown to support an impairment claim.

The initial question is whether the state law has, in fact, operated as a substantial impairment of a contractual obligation. The severity of the impairment increases the level of scrutiny to which the legislation is subjected. If there is a substantial impairment, the state, at the second step, must demonstrate a significant and legitimate public purpose behind the legislation. Third, the state’s action is examined in the light of this public purpose to see ‘whether the adjustment of the rights and responsibilities of the contracting parties [is based] upon reasonable conditions and [is] of a character appropriate to the public purpose justifying [the legislation’s] adoption.’

*Christensen*, 331 N.W.2d at 750-51.

Plaintiffs’ contract impairment claims fail because there has been no substantial impairment of their interest in an annual adjustment to their retirement annuities. A contract impairment occurs when a state law substantially disrupts a party’s reasonable contractual expectations. *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 244-46, 98 S.Ct. 2716, 2722-23 (1978) (noting legislation cannot alter contract terms “by effectively imposing on one of the parties an obligation which it had not reasonably anticipated or relieving a party of a contractual obligation.”). A “technical” or minimal contract alteration is not a constitutional violation. *Id.* at 245, 98 S.Ct. at 2723 (“Minimal alteration of contractual obligations may end

the inquiry at its first stage.”); *Acton Const’n v. Comm’r of Revenue*, 391 N.W.2d 828, 833 (Minn. 1986) (legislation restricting party to gains reasonably expected from a contract is not an impairment).

Plaintiffs’ annuities and paid adjustments are undiminished and their pensions remain “eligible” for future increases. The fundamental retirement benefit structure for Plaintiffs is the same both before and after enactment of the challenged legislation. Plaintiffs continue to be paid a monthly annuity that has not been reduced. Plaintiffs also remain eligible for an annual adjustment based on a statutory formula. The change in the statutory adjustment formula did not impair any protected right.

The undisputed facts show the Plans and the Legislature repeatedly evaluated changes to, or modified, the statutory adjustment formula to attain greater consistency with stated legislative retirement policy, to eliminate inequities between retiree groups, and to address the de-stabilizing effects of market volatility. Further, the challenged legislation followed years of historical funding depletions that were left unresolved by previous legislative measures and were exacerbated by the unprecedented market conditions in 2008-09. The Legislature properly responded to these events. The challenged legislation addressed legitimate and significant public purposes, particularly given that these Plans are intended to be viable beyond the lifetime of the current Plaintiffs. *Christensen*, 331 N.W.2d at 751 (responding to a fiscal misjudgment is a legitimate public purpose).

Finally, Plaintiffs’ impairment claims fail because the challenged legislation was a reasonable and appropriate exercise of legislative authority and responsibility to maintain the Plans’ fiscal stability for the benefit of all members. *Christensen*, 331 N.W.2d at 751 (noting balance required between security in retirement program and public’s concern for fiscal

integrity of state and pension fund). In exercising its authority here, the legislative change to the statutory adjustment formula was a comprehensive package of amendments that spread the burden and sacrifice of stabilizing the Plans across all members, the State, and the taxpayers. The Court will not intrude on this legislative judgment. *Mpls. Teachers Retirement Fund Ass'n*, 490 N.W.2d at 131 (“It is not within the power of the court to second guess the policy determinations of the legislature”).

Plaintiffs argue that the legislation was unnecessary because the risk of default was not imminent. However, this argument is inconsistent with the undisputed facts. The testimony by the Plans’ witnesses is uncontradicted: actuarial projections showed a continual decline in funding status, and MSRS and TRA faced projected default dates within the lifetime of most of their retiree members, including Plaintiffs. All of the Plans had seen unprecedented losses in values (actuarial or market) in a matter of months. While the Plans may not have been on the brink of default, the speed and depth of the financial decline posed a credible risk of default that required a response.

Plaintiffs also argue that other alternatives were available to the Legislature. Plaintiffs argue that a tax increase would have been a viable option but for the political climate at the time; or, increased contribution rates across all plans or in a greater amount would have resolved much of the deficiency. These choices, however, are firmly within the Legislature’s policy arena. *Mpls Teachers Retirement Fund Ass’n*, 490 N.W.2d at 131. In addition, the testimony by the Plans’ representatives on the viability of these alternatives was uncontradicted. They did not go far enough to provide the immediate financial stability needed, and these measures unduly burdened active members who already bore the brunt of the financial solution

with increased contribution rates and will be subject to the same adjustment formula at retirement.

Finally, Plaintiffs argue that the Court cannot simply defer to the Legislature's choices because the State's self-interest was at stake. However, the Plans and the Legislature are charged with monitoring the pension system and ensuring its fiscal integrity for all members, active, retired, and deferred. No facts support Plaintiffs' theory that the State's self-interest led to a change in the statutory adjustment formula. To the contrary, the public record before the Legislature included actuarial opinions and projections, as well as dozens of modeled scenarios using multiple possible combinations of plan changes. The uncontested opinions from the actuary for the Plans' and the Legislature's actuary supported the multi-pronged response enacted. The Legislature appropriately and responsibly took a multitude of steps, not in the State's self-interest, but in the collective interests of all members.

Plaintiffs have not met their evidentiary burden to show an unconstitutional impairment beyond a reasonable doubt.

Plaintiffs alleged that the change in the adjustment formula violates the Takings Clause of the Minnesota and Federal Constitutions because it deprives them of future adjustments to which they were entitled based on the formula in effect as of the date of their retirement.

The Taking Clauses restrict the ability of government to take private property without just compensation. U.S. CONST. AMEND. V ("nor shall private property be taken for public use, without just compensation"); MINN. CONST. art. 1, § 13 ("private property shall not be taken, destroyed or damaged for public use, without just compensation therefore first paid or secured"); *Wensmann Realty, Inc. v. City of Eagan*, 734 N.W.2d 623, 631-32 (Minn. 2007)

(noting the Takings Clause ensures that government does not require some citizens to bear a burden that should be borne by the public as a whole).

Plaintiffs' Takings claims fail because they rest ultimately on the expectation that future adjustments would be made pursuant to a particular formula. As shown above, that expectation has neither a contractual basis, nor a reasonable basis enforceable by estoppel principles.

In addition, Plaintiffs provided no law to support their theory that a statutory formula is "property" that can be protected by the Takings Clauses. Plaintiffs' claimed expectation to a future adjustments to their annuities that may have been greater under the former formula is not a property right protected by the Takings Clauses.

Given the fundamental and undisputed fact that Plaintiffs' expectations have been met and they have received increases greater than would have been available under the previous formula, Plaintiffs cannot meet their demanding burden to show that any property was taken and that the challenged legislation is unconstitutional beyond a reasonable doubt.

Plaintiffs sued the individual Defendants in their official capacities, asserting in addition to alleged constitutional violations that these Defendants violated 42 U.S.C. § 1983 by enforcing allegedly unconstitutional laws. Having concluded that the underlying substantive constitutional claims should be dismissed as a matter of law, the Section 1983 claims (Counts V, VI) are dismissed as well.

In addition, because the substantive claims are dismissed in their entirety and with prejudice, the Court does not address the allegations in the Complaint regarding the proposed class treatment for Plaintiffs' claims.

**GEJ**