SUPREME COURT, STATE OF COLORADO 2 East 14th Avenue Denver, CO 80203 COLORADO COURT OF APPEALS Court of Appeals Case No. 11CA1507 City and County of Denver District Court No. 10CV1589 Honorable Robert S. Hyatt, Judge	▲ **COURT USE ONLY** ▲
Petitioners/Plaintiffs: GARY R. JUSTUS; KATHLEEN HOPKINS; EUGENE HALAAS; and ROBERT P. LAIRD, JR., on behalf of themselves and those similarly situated, **Respondents/Defendants:** THE STATE OF COLORADO; GOVERNOR JOHN HICKENLOOPER, in his official capacity; COLORADO PUBLIC EMPLOYEES' RETIREMENT ASSOCIATION; CAROLE WRIGHT, in her official capacity; and MARYANN MOTZA, in her official capacity	Supreme Court Case No.: 2012SC906
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PLAINTIFF-PETITIONERS' AMENDED OPENING BRIEF

SUPREME COURT, STATE OF COLORADO 101 West Colfax Avenue, Suite 800 Denver, CO 80203 Telephone: 303-861-1111	
Appeal from COLORADO COURT OF APPEALS Case No. 11CA1507 City and County of Denver District Court No. 10CV1589 Honorable Robert S. Hyatt, Judge	▲ **COURT USE ONLY** ▲
Petitioners/Plaintiffs: GARY R. JUSTUS, KATHLEEN HOPKINS, EUGENE HALAAS, and ROBERT P. LAIRD, JR., on behalf of themselves and those similarly situated. Respondents/Defendants: THE STATE OF COLORADO; PUBLIC EMPLOYEES' RETIREMENT ASSOCIATION OF COLORADO; GOVERNOR JOHN HICKENLOOPER, CAROLE WRIGHT, and MARYANN MOTZA, in their official capacities only.	Supreme Court Case No.: 2012SC906
CERTIFICATE OF COMPLIANCE	

I hereby certify that this brief complies with all requirements of C.A.R. 28 and C.A.R. 32, including all formatting requirements set forth in these rules. Specifically, the undersigned certifies that:

The brief complies with C.A.R. 28(g).

It contains 8,355 words.

The brief complies with C.A.R. 28(k).

It contains under a separate heading (1) a concise statement of the applicable standard of appellate review with citation to authority; and (2) a citation to the precise location in the record (R.__, p.___), not to an entire document, where the issue was raised and ruled on.

S/Richard Rosenblatt
Richard Rosenblatt, Esq.

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STATEMENT OF THE ISSUES

1. Whether the contracts clause framework articulated in In re Estate of DeWitt, 54 P.3d 849 (Colo. 2002), applies to all contract clause claims under the Colorado Constitution.

Suggested Answer: No, it does not apply in cases where employers cut the pension benefits that public employees already earned, and even if it does, such cuts are *per se* not "reasonable and necessary to serve a significant and legitimate public purpose."

2. Whether Colorado Public Employees' Retirement Association members have contractual rights to the cost-of-living adjustment formulas in place at their respective retirements for life without change.

Suggested Answer: Yes.

3. Whether Senate Bill 10-001, which adjusted cost-of-living adjustments to their current level of two percent compounded annually, was constitutional because it (a) did not substantially impair contractual expectations and was reasonable and necessary to ensure the pension funds' long term viability, and (b) was not a regulatory taking.

Suggested Answer: No. [Amended from original Opening Brief]

STATEMENT OF THE CASE

A. Nature of the Case

Plaintiffs Gary R. Justus, Kathleen Hopkins, Eugene Halaas, Jr., and Robert Laird, Jr., on behalf of themselves and those similarly situated (collectively, "Retirees"), commenced this action in the District Court for Denver County on February 26, 2010. Compl., Bookmark ID #27944505, CD page 2. The proposed class includes approximately 50,000 Colorado public sector employees who have retired. All Retirees are members of the Public Employees Retirement Association of Colorado ("PERA"), which includes former public school teachers; retired state judges; retired police officers; and other retired state, county and local government workers who were employed in the various sectors of Colorado government.

Retirees alleged that in exchange for their service, they were promised certain specified pension benefits, including an annual cost-of-living adjustment ("COLA"). Retirees further alleged that they held up their end of the bargain by rendering years of service, often at a lower wage than they could have earned in the private sector. Further, throughout their working lives, Retirees made contributions to Colorado's Retirement Systems, as required by state law. Having done so, they reasonably expected that they would receive the promised pension benefits that would sustain them throughout retirement.

In 2010, the Colorado Legislature enacted Senate Bill 10-001 ("2010 Pension Legislation"), which reduced the pension benefits promised to Retirees by eliminating the COLA entirely for 2010 and by scaling back the annual COLA thereafter. Retirees allege that under well-established Colorado case law, they acquired rights to fully vested pension benefits, including the annual COLA in effect under the law when they became eligible to retire, and that the 2010 Pension Legislation violated those rights.

B. Course of Proceedings

Retirees commenced their District Court action with a Complaint filed February 26, 2010, naming as Defendants the State Of Colorado, the Public Employees' Retirement Association of Colorado ("PERA"), and the then Governor and two former PERA officials, in their official capacities only; the individual defendants have since been replaced with the appropriate current officials. Retirees filed a First Amended Complaint on March 18, 2010. First Am. Compl., Bookmark ID #28459106, CD page 13. Retirees sought a judicial declaration finding Sections 19 and 20 of Senate Bill 10-001 in violation of the Contract clause of the Colorado Constitution (Count I);[1] and the Contract (Count III), Takings (Count IV), and Substantive Due Process (Count V) Clauses of the United States

[1] Count II had alleged a violation of Article V, § 48 of the Colorado Constitution, but Plaintiffs agreed this claim could be dismissed on September 14, 2010.

Constitution. Retirees also sought relief pursuant to 42 U.S.C. § 1983 against the individual defendants in their official capacities for violations of the Contract (Count VI), Takings (Count VII) and Substantive Due Process (Count VIII) Clauses of the United States Constitution.

The parties filed cross motions for summary judgment. Pls.' Summ. J. Mot., Bookmark ID #34753454, CD page 521; PERA Defs.' Summ. J. Mot., Bookmark ID #37730166, CD page 924. Retirees relied extensively on Police Pension and Relief Board of the City and County of Denver v. McPhail, 338 P.2d 694 (Colo. 1959), and Police Pension and Relief Bd. of City and County of Denver v. Bills, 366 P.2d 581 (Colo. 1961). Pls.' Summ. J. Mot., Bookmark ID #34753454, CD page 522-23, 532-537; see also Pls.' Reply Br. in Supp. of Summ. J. Mot., Bookmark ID #38028147, CD pages 1053-56, 1058-63, 1066-68, 1070, 1072 (extensively discussing McPhail and Bills); see also Second Am. Class Action Compl., Bookmark ID #37056989, CD page 664 (addressing McPhail and Bills in four paragraphs). Defendants also extensively briefed the significance of McPhail and Bills. PERA Defs.' Opp'n to Pls.' Mot. for Partial Summ. J., Bookmark ID #37720186. CD pages 822-824, 849-857, 870.

By Order dated June 20, 2011, Denver District Court Judge Robert S. Hyatt denied Retirees' Motion for Partial Summary Judgment. Order, Bookmark ID

#40216707, CD page 1586. Without explaining the basis for this conclusion, the District Court simply stated that Retirees had not met their summary judgment burden. Id. at CD page 1591. By Order dated June 29, 2011, the District Court granted the Colorado Defendants' Motion for Summary Judgment, dismissing all of Retirees' claims. Order, Bookmark ID #40496384, CD page 1600. The court concluded that "based on numerous and steady changes in the PERA COLA formula for retirees, Plaintiffs could not have had a reasonable expectation that the COLA formula that happened to be in place at the date of their retirement would be unchangeable for the rest of their lives." Id. at CD page 1607. Neither of the District Court's summary judgment orders even cited, let alone discussed, McPhail or Bills. See id.

C. Disposition of Court Below

Plaintiffs appealed to the Court of Appeals, which by Judgment entered October 11, 2012, Justus v. State, ___P.3d ___, 2012 WL 4829545 (Colo. App. Oct. 11, 2012), reversed the District Court. The court held that under McPhail and Bills, "plaintiffs have a contractual right to the COLA in effect when their rights vested." Id. at *7. However, the court also concluded that McPhail and Bills were modified by the Colorado Supreme Court's subsequent decision In re Estate of DeWitt, 54 P.3d 849 (Colo. 2002), which did not involve a government contract,

but articulated a general test for Contract Clause claims. Interpreting McPhail, Bills, and DeWitt, the Court of Appeals ruled that Retirees may prevail on their Contract Clause claim only if their contractual impairment was not "reasonable and necessary to serve a significant and legitimate public purpose." Id. at *11. The Court of Appeals also remanded the case to the District Court for further proceedings.

Pursuant to Colo. Rev. Stat. § 13-4-102(1) (2006), and C.A.R. 49(a)(2), this appeal followed.

STATEMENT OF THE FACTS

A. The Plaintiffs and PERA

The Plaintiffs are retired members of PERA and currently receive pension benefits from PERA. Plaintiff Gary Justus worked for more than 29 years for the Denver Public Schools ("DPS") before retiring in 2003, when he began receiving DPS pension benefits and later PERA benefits after the DPS retirement plan merged into PERA. Aff. of Gary Justus, Bookmark ID #38369859, CD page 1219-20. Plaintiff Eugene Halaas, Jr. worked for more than 27 years as a judge for the State of Colorado before retiring in 1999. Aff. of Eugene Halass, Jr., Bookmark ID #38369859, CD page 1222-23. Plaintiff Robert Laird, Jr. retired in July 2010 after working 32 years for the Pikes Peak Community College. Aff. of Robert

Laird, Bookmark ID #38369859, CD page 1225. Plaintiff Kathleen Hopkins worked approximately 15 years for the State of Colorado before retiring in July 2001. First Am. Compl., Bookmark ID #28459106, CD page 14.

Defendant PERA **"**provides retirement and other benefits to the employees of more than 400 government agencies and public entities in the state of Colorado. PERA is the twenty-first largest public pension plan in the United States." About Colorado PERA Overview, Colo. PERA (last visited 10/22/10), http://www.copera.org/pera/about/overview.htm (cited in Pls.' Mot. for Partial Summ. J., Bookmark ID #34753454, CD page 525). "Its membership includes employees of the Colorado state government, public school teachers in the state, many university and college employees, judges, many employees of cities and towns, state troopers, and the employees of a number of other public entities." Id. Further, "PERA is a substitute for Social Security for most of these public employees. Benefits are pre-funded, which means while a member is working, he or she is required to contribute a fixed percentage of their [*sic*] salary to the retirement trust funds." Id.

In addition to the members' contributions, PERA employers are required to make contributions to PERA. However, the Legislature has continually kept contribution rates below the annual required contribution as determined by

PERA's actuaries. In a March 2010 Report, the Pew Center on the States reported that Colorado contributed only 68.3% of its full actuarial required contribution over the past 10 years, and flagged it as one of ten "lagging" states. PEW Report, Bookmark ID #3839946, CD page 1264.

B. The Governing Pension Law Provided Retirees with a Fixed Cost of Living Adjustment

For many years, the State of Colorado and the Denver Public Schools promised Retirees that they would receive a fixed, post-retirement annual cost of living adjustments to their pensions.

1. Non-DPS PERA Retirees

Prior to March 1, 1994, the state law that governed PERA provided that "[c]ost of living increases in retirement benefits and survivor benefits shall be made only upon approval by the general assembly." Colo. Rev. Stat. § 24-51-1001 (1992). In 1993, the Legislature amended this provision to make annual COLA increases granted on or after March 1, 1994 **automatic** and no longer dependent each year on approval by the legislature. HB 93-1324, § 7 (1993). Under the new law:

> (1) Annual increases in retirement benefits and survivor benefits shall occur on March 1 if said benefits have been paid for at least three months preceding March 1. Such increases in benefits shall be calculated in accordance with the provisions of sections 24-52-1002 and 24-51-1003 and shall be paid from the division trust funds.

Colo. Rev. Stat. § 24-51-1001 (1994) (emphasis added).

In Colo. Rev. Stat. § 24-51-1002—the part of the statute that made annual COLA increases automatic—the Legislature utilized language ("shall") that plainly showed that these yearly adjustments were mandatory:

> (1) The cumulative increase applied to benefits paid **shall** be recalculated annually as of March 1 and **shall** be the lesser of:
>
> (a) The total percent derived by multiplying three and one-half percent, compounded annually, times the number of years such benefit has been effective after March 1, 1993; and
>
> (b) The percent increase in the consumer price index from 1992, or the year prior to the year in which the benefit becomes effective, whichever is later, to the year preceding March 1.

Colo. Rev. Stat. § 24-51-1002 (1994) (emphasis added). As a consequence of this amendment, from 1994 through 2000, pension benefits of PERA retirees were automatically and mandatorily increased under specific formulae.

In 2000, the Legislature amended Colo. Rev. Stat. § 24-51-1002 again, this time replacing the annual variable COLA adjustment with **a guaranteed 3.5%** annual increase effective March 1, 2001. Laws 2000, Ch. 186, § 7. As amended, the statute provided:

> The cumulative increase applied to benefits paid **shall** be recalculated annually as of March 1 and shall be the total percent derived by multiplying three and one-half percent, compounded annually, times the number of years such benefit has been effective after March 1, 2000.

Colo. Rev. Stat. § 24-51-1002 (2002) (emphasis added).

In 2004, the Legislature amended Colo. Rev. Stat. § 24-51-1002 *for future PERA members only*, effectively grandfathering past members at the 3.5 percent level. Thus, the 2005 legislation provided that the annual increase for persons who became members on or after July 1, 2005 shall be the lesser of 3% or the actual increase of the consumer price index ("CPI"). Laws 2004, Ch. 214, § 9 (codified at Colo. Rev. Stat. § 24-51-1002(a.5)(I) (2005)). Two years later, the Legislature included individuals who were PERA members as of June 30, 2005, but who were not members as of December 30, 2006, among those PERA members who would receive a COLA of CPI up to 3%. Laws 2006, Ch. 308, § 40 (codified at Colo. Rev. Stat. § 24-51-1002(3)(a) (2007)). After the 2006 amendment and until the effective date of the 2010 Pension Legislation, the following language governed annual increases for Class members:

> (1) For benefit recipients whose benefits are based on the account of a member who was a member, inactive member, or retiree on December 31, 2006, the cumulative increase applied to benefits paid shall be recalculated annually as of March 1 and shall be the total percent derived by multiplying three and one-half percent, compounded annually, times the number of years such benefit has been effective after March 1, 2000. . . .

Colo. Rev. Stat. § 24-51-1002(1) (2007).

2. DPS Retirees

Until it merged with PERA, the Denver Public Schools Retirement System ("DPSRS") had been providing some form of guaranteed annual adjustment to member pensions since at least 1981, when DPSRS began increasing pensions annually by 3.0% (non-compounding). See DPSRS, Significant Facts (July 1, 2009), Bookmark ID #38370051, CD Page 1346. In 1986, DPSRS raised the yearly adjustment to 3.25% (non-compounding); and in 2000, DPSRS began to compound interest. Id. at CD Page 1346-47.

When DPSRS became a part of PERA on January 1, 2010, PERA assumed DPSRS' obligation for the guaranteed 3.25% (compounded) annual increase for DPS Subclass Members. Colo. Rev. Stat. § 24-51-1732 (effective January 1, 2010).

C. PERA Repeatedly Informed its Members that they would Receive Annual COLA's Upon Retirement

PERA regularly assured Retirees that they could count on continuing to receive their promised postretirement adjustments throughout retirement. For example, an October 2000 PERA booklet described the COLA change as follows:

> **PERA will increase your benefit each year by 3.5 percent compounded annually from the date of your initial benefit.** This increase is recalculated on the last workday of each March and is based on your total benefit. Your first increase will be prorated for the number of months you have been retired.

Colo. PERA, Your PERA Benefits, Bookmark ID #38370051, CD page 1355 (emphasis added).

In other communications with its members, PERA plainly informed Retirees that they will "[r]eceive an annual automatic increase of 3.5 percent in your monthly retirement benefit to help keep up with the cost of living." Colo. PERA, Benefits at a Glance (Rev. July 2004), Bookmark ID #38370051, CD page 1357. Similarly, in a September 2004 "Member Report," PERA explained how a "PERA account will grow from the 'magic of interest compounding'" and stated that if a member chooses to receive a lifetime monthly benefit, he "will receive a benefit increase that is indexed for inflation at 3.5 percent." Colo. PERA, Member Report (Sept. 2004), Bookmark ID #38370051, CD page 1359; see also Annual Benefit Increases, Colo PERA (accessed on Nov. 11, 2009), https://www.copera.org/pera/retiree/benefitincrease.htm , Bookmark ID #38370051, CD page 1362 ("If you begin PERA membership on or before June 30, 2005, you will receive an annual increase of 3.5 percent.").

D. Colorado's Attorney General Issues an Opinion Finding that PERA Pensions may not Be Reduced for those Fully Vested

In 2005, three years after In re Dewitt was published, Colorado Attorney General Ken Salazar issued a formal opinion in response to the following question from Colorado's Treasurer: "What, if any, limitations exist upon the Legislature's

ability to reduce the capacity of current employees to earn additional retirement benefits to assure the long term actuarial soundness of the plan?"

First addressing the rights of those who had *yet to qualify* for retirement and whose benefits were therefore "*partially vested*" (none of whom are members of the proposed class in this lawsuit), then Attorney General Ken Salazar responded:

> The rate and amount of retirement benefits may qualify as a partially vested pension right protected by the contract clause of the constitution. An adverse change to a partially vested pension right is lawful only if it is balanced by a corresponding change of a beneficial nature, a change that is actuarially necessary, or a change that strengthens or improves the pension plan.

Attorney General Formal Opinion No. 05-04, Bookmark ID #34753564, CD page 579. As for PERA members who had *fulfilled all of the requirements for the pension* (as have members of the proposed class in this lawsuit), the Attorney General concluded:

> Once a PERA member fulfills all the statutory requirements for a pension benefit, retires and begins receiving a pension, **the member's fully vested pension right cannot be reduced by the General Assembly.**

Id. at CD page 583 (emphasis added). In the "Discussion" section, the Attorney General explained his answer as to those already vested in their benefits:

> Some vested pension rights cannot be eliminated. When a PERA member retires from active service and begins receiving a pension, the member's pension becomes a vested contractual obligation of the pension program that is not subject to unilateral change **of any type**

> by the General Assembly. Police Pension & Relief Board of City and County of Denver v. Bills,148 Colo. 383, 366 P.2d 581, 584 (1961) (citing Police Pension & Relief Board of the City and County of Denver v. McPhail, 139 Colo. 330, 338 P.2d 694, 700 (1959)). **When an employee retires and begins receiving a pension, trustees may not adopt an amendment that reduces an employee's vested pension under the plan.** Walker v. Board of Trustees of Regional Transportation District Pension Plan, 69 Fed. Appx. 953, 2003 WL 21690534 (10th Cir. Colo.) (impairment of vested pension rights is arbitrary and capricious, a breach of contract, and a breach of its fiduciary duties) (citing Police Pension & Relief Board of City and County of Denver v. Bills)…

Id. (emphasis added). Thus, Colorado's Attorney General relied on Bills and McPhail to conclude that once a PERA member is eligible for a pension, or once he or she retires and begins receiving a pension, the member's fully vested pension right cannot be reduced.

PERA Executive Director Meredith Williams endorsed this analysis as recently as December 2008 in an issue of the PERA publication "Retiree Update":

> PERA continues efforts to work with other large pension plans and others to ensure that our members' and retirees' retirements are protected and to find a resolution to the current market turmoil. A Colorado Attorney General's (AG) Formal Opinion concerns constitutional limits to the ability of the state General Assembly to alter retirement benefits for public employees under the pension program administered by PERA. The AG's opinion states that when a PERA member retires and begins receiving pension benefits, **such member's pension rights have fully vested and such pension benefits may not be reduced**. Current members [i.e., those not yet retired] may also have certain pension benefit rights protected under the Constitution, although the General Assembly may make changes

> to such benefits if the changes are balanced by corresponding changes of a beneficial nature or are actuarially necessary.

Colo. PERA, Retiree Update (Dec. 2008), Bookmark ID #38376075, CD page 1420 (emphasis added).

The named plaintiffs each took government positions and stayed in them, not only to engage in public service, but also because the pensions available to them were sufficiently attractive to warrant the lesser salaries and other encumbrances that came with a government position. Justus Aff., Bookmark ID #38369859, CD page 1219-20; Halaas Aff., Bookmark ID #38369859, CD page 1222; Laird Aff., Bookmark ID #38369859, CD page 1225. Each of them believed that they would be permanently entitled to the pension formula in effect at the time that they left their paying jobs; they each retired and applied for their pension benefits; and each of them experienced a reduction in their postretirement adjustments as a result of the retroactive application of the Pension Legislation. Justus Aff., CD page 1219-20; Halaas Aff., CD page 1222-23; Laird Aff., CD page 1225-26. They all believed that upon becoming eligible to retire or upon retirement they were entitled to the same formula for the postretirement adjustments (or an equivalent formula) throughout their lifetimes and those of any designated survivors. Id. These beliefs were based on the law and various types of communications from the plans themselves. Id.

E. Senate Bill 10-001

After the Legislature passed SB 10-001, Governor Ritter signed it into law on February 23, 2010. SB 10-001, hereinafter referred to as the 2010 Pension Legislation, modified PERA in several respects. Among other things, it increased employer and employee contributions; it raised service eligibility requirements for PERA members hired after January 1, 2011; and it changed the formula for calculating the Highest Average Salary for PERA members not eligible to retire as of January 1, 2011.

Most important for purposes of this lawsuit, the 2010 Pension Legislation eliminated the guaranteed automatic 3.5% annual COLA increase for PERA public employee retirees and the 3.25% annual COLA increase for DPS retirees. This aspect of 2010 Pension Legislation applies to PERA members who have just begun their employment, as well as those who are already retired. The 2010 Pension Legislation provides a COLA based on the Consumer Price Index ("CPI"), capped at 2%, that could—and in 2010 did—yield a **0% increase**. In its current form, Colo. Rev. Stat. § 24-51-1002 in pertinent part reads:

> (1) For benefit recipients whose benefits are based on the account of a member who was a member, inactive member, or retiree on December 31, 2006, or for benefit recipients whose benefits are based on the account of a DPS member or DPS retiree, **the increase applied to benefits for the year 2010 shall be the lesser of two percent or the average of the annual increases determined for each month, to the**

nearest one-tenth of a percent, as calculated by the United States department of labor, in the national consumer price index for urban wage earners and clerical workers for each of the months in the 2009 calendar year.

(2) **Beginning in the year 2011**, subject to the provisions of section 24-51-1009.5, for benefit recipients whose benefits are based on the account of a member who was a member, inactive member, or retiree on December 31, 2006, or for benefit recipients whose benefits are based on the account of a DPS member or DPS retiree, **the increase applied to benefits paid shall be the lesser of two percent or the average of the annual increases determined for each month, to the nearest one-tenth of a percent, as calculated by the United States department of labor, in the national consumer price index for urban wage earners and clerical workers during the calendar year preceding the increase in the benefit.** Notwithstanding the provisions of this subsection (2), the increase shall be the maximum permitted under this subsection (2) and section 24-51-1009.5 unless the association's annual audited return on investments is negative for the preceding calendar year, at which point the annual increase for the subsequent three years shall be the lesser of two percent or the average of the annual increases determined for each month, to the nearest one-tenth of a percent, as calculated by the United States department of labor, in the national consumer price index for urban wage earners and clerical workers during the calendar year preceding the increase in the benefit. The increase applied to such benefits shall be recalculated annually as of July 1, and shall be the compounded annual percentage of the annual increases applied to such benefits. In the first year that the benefit recipient is eligible to receive an annual increase pursuant to section 24-51-10001, the annual increase shall be prorated.

Laws 2010, Ch. 2, § 29; Colo. Rev. Stat. § 24-51-1002 (2010) (emphasis added).

The 2010 Pension Legislation also provides a 0.25% increase to the 2.0% cap if the actuarial value of PERA's assets exceeds an actuarial funding ratio of

103% and a 0.25% decrease if the asset value subsequently falls below 99%. Laws 2010, Ch. 2, § 23; Colo. Rev. Stat. § 24-51-1009.5 (2010). In addition, the legislation changes the traditional date for implementing annual COLA increases, moving it forward by three months, from March to July. Colo. Rev. Stat. § 24-51-1001 (2010).

The 2010 Pension Legislation substantially reduced the pension benefits of class members. For example, a retiree with the average annual benefit in 2008 of $33,264 will lose more than $165,000 over the first twenty years after enactment. Second Am. Compl., Bookmark ID #34657720, CD page 510-11.

SUMMARY OF THE ARGUMENT

The District Court erred as a matter of law in entering summary judgment for the Colorado Defendants and against Retirees. While the Court of Appeals correctly reversed the District Court for failing to apply McPhail and Bills, the Court of Appeals wrongly concluded that In re DeWitt modified the fundamental public pension rule applied in these cases. Even if Dewitt is applicable, McPhail and Bills establish that it is never "reasonable and necessary" for the Legislature to reduce the PERA pensions of those fully vested in their pensions. Finally, SB 10-001 is unconstitutional because it (a) substantially impaired impair contractual expectations and was not reasonable and necessary to ensure the

pension funds' long-term viability, and (b) was a regulatory taking. At the very least, these questions should be answered only after the Plaintiffs have had an opportunity to conduct discovery on these questions.

ARGUMENT

I. The Dewitt Test does not Apply to Legislation Affecting Public Retirement Benefits for those Fully Vested in their Pensions.

A. The Contract Clause is subordinate to the State's inherent "police powers."

The Contract Clauses of the United States and Colorado Constitutions both prohibit the impairment of contracts by the government. See Colo. Const. art. II, § 11 ("No . . . law impairing the obligation of contracts . . . shall be passed by the general assembly."); U.S. Const. art. I, § 10. ("The United States Constitution states, in pertinent part, that "No state shall ... pass any ... law impairing the obligation of contracts."). Until the twentieth century, the strictures of the Contract Clause were absolute, and a state could not subsequently modify its own contracts even by an amendment to its own constitution. See, e.g., Fisk v. Police Jury of Jefferson, 116 U.S. 131 (1885) (where a police officer provided his services under a law setting forth his compensation, a constitutional amendment restricting the limit of taxation violated federal Contract Clause).

In the early twentieth century, the Contract Clause's protections began to be weighed against the sovereign's inherent powers, such as its "police power" to protect the welfare of its citizens. See Atlantic Coast Line Railroad Co. v. City of Goldsboro, 232 U.S. 548, 558 (1914). As this Court recognized in 1920:

> We think without further discussion that it is the overwhelming weight of judicial opinion in this country that the constitutional interdiction of statutes impairing the obligations of contracts does not prevent the state from properly exercising such powers as are vested in it for the promotion of the common weal, or as are necessary for the general good of the public. . .

Ohio & Colo. Smelting & Refining Co. v. Pub. Util. Comm'n, 68 Colo. 137, 142-43, 187 P. 1082, 1084-85 (Colo. 1920). Further, during the height of Great Depression, the United States Supreme Court expanded the scope of the states' inherent police power to modify contracts when it found that **"**economic interests of the state may justify the exercise of its continuing and dominant protective power notwithstanding interference with contracts." Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 437 (1934).

Historically, pensions were seen as mere gratuities granted by the sovereign to the government employee, in that they could be reduced or eliminated at any time. See, e.g., Bedford, State Auditor v. White, 106 Colo. 439, 444 (1940). By the mid-twentieth century, courts began to increasingly find that pensions were not mere gratuities but rather were contractual in nature. See, e.g., Police Pension and

Relief Bd. of the City and County of Denver v. McPhail, 139 Colo. 330, 341, 338 P.2d 694, 700 (Colo. 1959). Even though by this time courts had determined that the Contract Clause's power was no longer absolute, some state courts determined that an employee became vested with contractual pension rights upon employment and that no change could be made without the employee's agreement. See, e.g., Baker v. Retirement Bd. of Allegheny County, 97 A.2d 231, 233 (Pa. 1953); Yeazell v. Copins, 402 P.2d 541, 546 (Ariz. 1965). Other courts took an approach which considered the state's police power by recognizing that states could, under certain circumstances, make reasonable changes to their pension system but any change could only affect those who were **not fully vested** in their pensions. For example, the Supreme Court of Washington found:

> [T]he employee who accepts a job to which a pension plan is applicable contracts for a substantial pension and is entitled to receive the same when he has fulfilled the prescribed conditions. His pension rights may be modified **prior to retirement**, but only for the purpose of keeping the pension system flexible and maintaining its integrity.

Bakenhaus v. City of Seattle, 296 P.2d 536, 540 (Wash. 1956) (citation omitted) (en banc).

Colorado adopted a similar view of pensions, distinguishing between those who had a "limited vested" right in their pensions and those who were fully vested. In McPhail, which considered the constitutionality of an amendment to the pension

plan which lowered the escalator clause of those **already retired**, this Court found that no reductions whatsoever could be implemented:

> Until an employee has earned his retirement pay, or until the time arrives when he may retire, his retirement pay is but an inchoate right; **but when the conditions are satisfied, at that time retirement pay becomes a vested right of which the person entitled thereto cannot be deprived; it has ripened into a full contractual obligation."**

McPhail, 139 Colo. at 341.

Just two years later, the same escalator clause legislation was at issue in Bills with regard to those officers not yet eligible to retire. Police Pension and Relief Bd. of City and County of Denver v. Bills, 148 Colo. 383, 366 P.2d 581 (Colo. 1961). This Court found that active employees enjoyed "a limited vesting," and that "although prior to their eligibility to retire the pension plan could be changed, it could not be abolished nor could there be a substantial change of an adverse nature, without a corresponding change of a beneficial nature."[2] Id. at 584. Addressing this second category of officers, the court explained:

> These particular plaintiffs had every right to expect that upon retirement their pension would reflect subsequent increases in pay

[2] A number of other state courts have adopted a similar rule, holding that "**prior to absolute vesting**, pension rights are subject to reasonable modification in order to keep the system flexible to meet changing conditions, and to maintain the actuarial soundness of the system."Public. Emp.. Retirement Bd. v. Washoe County, 615 P.2d 972, 974-75 (Nev. 1980) (emphasis added); see Hammon v. Hoffbeck, 627 P.2d 1042, 1056 (Alaska 1981); Nash v. Boise City Fire Dep't, 663 P.2d 1105, 1108-09 (Idaho 1983); Singer v. City of Topeka, 607 P.2d 467, 475 (Kan. 1980).

> granted to those in active service. The charter amendment with which we are here concerned constituted an adverse change in the overall pension plan which deprived plaintiffs of a very substantial right, was unaccompanied by a corresponding change of a beneficial nature, was not shown to be actuarially necessary, nor that it in anywise strengthened or bettered the pension plan.

Id. at 584-85.

The distinction between fully vested and nonvested members of PERA was recognized in the Colorado Attorney General's Formal Opinion issued in 2005 (addressed at pp. 12 to 15, infra), after Dewitt was decided. The Formal Opinion is unequivocal: "the member's fully vested pension right cannot be reduced by the General Assembly."

Formal opinions issued by the Attorney General have "some significance in cases involving consideration of constitutional provisions where there is room for interpretation." Colo. Ass'n of Pub. Emps. v. Lamm, 677 P.2d 1350, 1360 (Colo.1984) (quoting White v. Anderson, 155 Colo. 291, 299, 394 P.2d 333, 336 (1964)); see also Colo. Common Cause v. Meyer, 758 P.2d 153, 159 (Colo.1988) (because the Attorney General issues written opinions pursuant to a statutory duty, "the opinion is obviously entitled to respectful consideration as a contemporaneous interpretation of the law by a governmental official charged with the responsibility of such interpretation").

B. In re Dewitt and its Relationship to McPhail and Bills.

In In re Dewitt, which did not involve impairment of any contract entered into by a government entity, the Court followed a three-part Contract Clause analysis, which the Court of Appeals summarized below:

> To decide whether a change in state law violates these Clauses, a court must first consider whether the change "'operate[s] as a substantial impairment of a contractual relationship' " . . . . If it does, that does not end the inquiry: the impairment may not necessarily run afoul of the Contract Clauses. The court must next determine whether the state has a significant and legitimate public purpose for the change, "such as the remedying of a broad and general social or economic problem" . . . . Finally, if the state does have such a purpose, the court must determine whether the change "is reasonable and necessary to serve [the] important public purpose" . . . . If so, the impairment does not violate the Contract Clauses.

Justus v. State, __ P.3d ___, 2012 WL 4829545, *5 (Colo. App. Oct. 11, 2012) (citations in text omitted).

While many state courts utilize a similar test to review the constitutionality under the Contract Clause of all state legislation, other states have carved out an exception when it comes to pension legislation (and Plaintiffs believe that Bills and McPhail did the same). For example, the Washington Supreme Court has utilized the traditional three-part Contract Clause test to review the constitutionality of most legislation. See, e.g., Pierce County v. State, 148 P.3d 1002 (Wash. 2006) (determine whether legislation impaired public bonds). However, as recently as

three years ago, the court continued to use a unique test to review pension legislation. McAllister v. City of Bellevue Firemen's Pension Board, 210 P.3d 1002, 1110 (Wash. 2009) (quoting Allen v. City of Long Beach, 287 P.2d 765, 767 (Cal. 1955)) (emphasis added)) ("the pension system may be modified **prior to an employee's retirement** in order to keep the system flexible enough to **'**permit adjustments in accord with changing conditions and at the same time maintain the integrity of the system.'").

Even if this Court decides that the Dewitt test should apply to public pension legislation, it should respect the holdings of Bills and McPhail and the distinction between those retired or eligible to retire and those who are not. In short, the McPhail and Bills courts believed simply that, **for people who have already retired or are eligible for retirement,** there is no way cuts can be "reasonable" or justified by actuarial necessity because these people are more vulnerable: They are elderly and retired (or at very end of their careers), with limited ability to go out and do something different that will get them back to the place they always thought they would have been at this stage in life. Bills and McPhail contrasted those who were not yet eligible for retirement: Employees in this second category still have "contracts," but their contracts are subject to modification through the "reasonableness" or "actuarial necessity" exception cases such as Blaisdell, 290

U.S. at 426; Walker v. Bedford, 93 Colo. 400, 412, 26 P.2d 1051, 1056 (Colo. 1933); and Ohio & Colorado Smelting & Refining, 187 P. at 140 -- all of which foreshadow DeWitt but precede Bills and McPhail.

II. Colorado Public Employees' Retirement Association Members have a Vested Right to the Cost of Living Adjustment Formula in Effect when they became Eligible to Retire or Actually Retired.

The Colorado Supreme Court has consistently found that "rights which accrue under a pension plan are contractual obligations which are protected under article II, section 11, of the Colorado Constitution. . . ." Colorado Springs Fire Fighters Ass'n, Local 5 v. City of Colorado Springs, 784 P.2d 766, 770 (Colo. 1989) (en banc) (citing McPhail); see also Bills, supra.

In McPhail, an *en banc* court considered whether Denver's repeal of a particular type of COLA – granted through an "escalator clause" in a city charter and ordinance which promised **post-retirement increases** equal to one-half of any future wage increases -- violated the state Contract Clause. The language of this particular COLA clause in McPhail was the following:

> In the event that salaries in the Denver police department shall be raised after the effective date of this amendment those [retired] members who are receiving a pension **shall be entitled** to an increase in the amount of their pension equal to one-half of the raise in pay granted in the rank said member held at the time he was retired.

McPhail, 139 Colo. at 334 (emphasis added).

Defendants have acknowledged the applicable COLA statutes governing PERA and the DPS Plan also used **mandatory** language ("shall") that requires the payment of COLAs. PERA Def SJ Opp, Bookmark ID #37720186, at CD page 863, 866. Again, this "shall" language is the same exact language used by the court in McPhail to find the escalator clause to constitute a vested contractual right. See McPhail, 139 Colo. at 334.

State appellate courts that have reviewed the question have found that the cost-of-living adjustment in effect at retirement is part and parcel of a retiree's overall pension benefit and therefore, protected under the Contract Clause. See, e.g., Booth v. Sims, 456 S.E.2d 167 (W. Va. 1995) (pension cost of living adjustment is a vested right); United Firefighters of Los Angeles City v. City of Los Angeles, 259 Cal.Rptr. 65 (Cal. Ct. App. 1989); Pasadena Police Officers Association v. City of Pasadena, 195 Cal.Rptr. 339 (Cal. Ct. App. 1984); Arena v. City of Providence, 919 A.2d 379 (R.I. 2007).

Consistent with McPhail and Bills, Plaintiffs have a vested right in the cost-of-living formula in effect when they became eligible to retire or did retire.[3] The Colorado Supreme Court's view that the law in effect at the time of an employee's

[3] To the extent that the COLA formula became more generous after a Plaintiff's retirement, that Plaintiff does not claim a right to the post-retirement improvement.

retirement governs the level of public sector pension benefits due is consistent with other state courts. See, e.g., Arena, 919 A.2d at 395 ("court must look a retirement plan's provisions at the time an employee retires to ascertain whether he or she is entitled to a benefit"); Gulbrandson v. Carey, 901 P.2d 573, 578 (Mont. 1995) ("The terms of [public employee's] retirement benefit contract are determined pursuant to the statutes in effect at the time of his retirement . . . .").

III. SB 10-001 Is Unconstitutional Because It (a) Substantially Impairs Contractual Expectations, And (b) Is a Regulatory Taking.

A. Standard of Review

This Court's standard of review when considering the constitutionality of a statute is de novo. Hinojos-Mendoza v. People, 169 P.3d 662, 668 (Colo. 2007).

"Unless the State itself is a contracting party . . . '[a]s is customary in reviewing economic and social regulation . . . courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure.'" Energy Reserves Grp., Inc. v. Kansas Power & Light Co., 459 U.S. 400, 412-13 (1983) (quoting U.S. Trust Co. of New York v. New Jersey, 431 U.S. 1, 22-23 (1977)). But where the State attempts to abridge its own contract, "complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State's self-interest is at stake." U.S. Trust Co., 431 U.S. at 26; see also Energy Reserves Group, 452 U.S. at 412 n.14 ("When a State itself enters into a contract,

it cannot simply walk away from its financial obligations. In almost every case, the Court has held a governmental unit to its contractual obligations when it enters financial or other markets.").

With respect to its own contractual obligations, a "[s]tate is not free to impose a drastic impairment when an evident and more moderate course would serve its purposes equally well." U.S. Trust Co., 431 U.S. at 25; *see* Ass'n of Surrogates & Supreme Court Reporters Within City of New York v. State of N.Y., 940 F.2d 766, 774 (2d Cir. 1991) ("The contract clause, if it is to mean anything, must prohibit [the State] from dishonoring its existing contractual obligations when other policy alternatives are available."). As the Supreme Court has explained:

> A governmental entity can always find a use for extra money, especially when taxes do not have to be raised. If a State could reduce its financial obligations whenever it wanted to spend the money for what it regarded as an important public purpose, the Contracts Clause would provide no protection at all.

U.S. Trust Co., 431 U.S. at 26 (footnote omitted); see also Carlstrom v. State, 694 P.2d 1, 5 (Wash. 1985) **(**"Financial necessity though superficially compelling, has never been sufficient of itself to permit states to abrogate contracts.").

B. SB 10-001 Substantially Impaired Retirees' Contractual Expectations.

If the Dewitt test is utilized and Retirees satisfy the first part (showing they have vested contractual rights to their COLA Benefits), this Court should find as a matter of law that SB 10-001 has substantially impaired such rights.

"The Supreme Court . . . has provided little specific guidance as to what constitutes a 'substantial' contract impairment." Baltimore Teachers Union, AFT v. Mayor and City Council of Baltimore, 6 F.3d 1012, 1018 (4th Cir. 1993). "Technical impairments, for example do not necessarily rise to the level of constitutional violations." Id. (citation omitted). On the other hand, "[t]otal destruction of contractual expectations is not necessary for a finding of substantial impairment." Energy Reserves, 459 U.S. at 411. "[T]he primary consideration in determining whether the impairment is substantial is the extent to which reasonable expectations under the contract have been disrupted." Sanitation and Recycling Indus. v. City of New York, 107 F.3d 985, 993 (2d Cir. 1997) (citing Energy Reserves, 459 U.S. at 411). As the Supreme Court has stated:

> [T]he severity of an impairment of contractual obligations can be measured by the factors that reflect the high value the Framers placed on the protection of private contracts. Contracts enable individuals to order their personal and business affairs.... Once arranged, those rights and obligations are binding under the law, and the parties are entitled to rely on them.

Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 245 (1978).

The promise to pay a certain sum of money is the "most important element[] of a contract," and "the central provision upon which it can be said [the employees] reasonably rely." Buffalo Teachers Federation v. Tobe, 464 F.3d 362, 368 (2d Cir. 2006) (failure to pay a 2% raise was a substantial impairment). Here, by passing SB 10-001, the Legislature decreased pension benefits earned through years of employment. This cut was substantial by any measure—a retiree with the average annual benefit in 2008 of $33,264 will lose more than $165,000 over the twenty years following enactment.

Courts have consistently found a decrease to a cost-of-living adjustment to constitute a substantial impairment. In United Firefighters of Los Angeles City, the court held that imposition of a 3% cap on pension cost-of-living adjustments for firefighters hired during a period with no caps constituted an impairment of a vested contractual right. 259 Cal.Rptr. 65. In Booth, the State of West Virginia reduced the pension cost-of-living adjustments from 3.75% to 2% for active State Troopers who were eligible for retirement, and argued that the adjustment was necessary to preserve the solvency of the pension fund. 456 S.E.2d at 187. The Supreme Court of West Virginia held that the reduction in the cost-of-living adjustments was an unconstitutional impairment, and that the state retained the burden of ensuring the solvency of the fund. Id. ("Requiring the petitioners to

protect the future solvency of the pension system is an unconstitutional shifting of the state's own burden."). See also Pasadena Police Officers Association, 195 Cal.Rptr. 339(cost-of-living adjustments benefits could not be capped on retired police officers who opted post-retirement for pensions with uncapped cost-of-living adjustments in lieu of a fixed pension).

Impairments worth much less have been found to be "substantial." Indeed, courts have found a substantial impairment when public employees were involuntarily furloughed for a week or less, because the loss of the expected pay "would likely wreak havoc on the finances of many of the affected workers and can only be considered substantial." Opinion of Justices (Furlough), 609 A.2d 1204, 1210 (N.H. 1992); Massachusetts Community College Council v. Commonwealth, 649 N.E.2d 708, 712 (Mass. 1995) (mandatory furloughs substantially impaired rights of state employees). A substantial impairment was similarly found in a decision considering New York's "payroll lag" law that allowed the withholding of two weeks of employees' pay until after they ended employment. Ass'n of Surrogates, 940 F.2d at 772; see also Univ. of Hawaii Professional Assembly v. Cayetano, 183 F.3d 1096 (9th Cir. 1999) (payroll lag law); Donohue v. Paterson, 715 F. Supp. 2d 306, 319 (N.D. N.Y. 2010) (temporary withholding of 4% salary increase that would later be reimbursed was

held to be a substantial contractual impairment); Bailey v. State, 500 S.E.2d 54 (N.C. 1998) (statute that placed cap on tax exemption on employees' retirement benefits was a substantial contractual impairment); State ex rel. Cannon v. Moran, 331 N.W.2d 369 (Wis. 1983) (salary setoff that reduced judges' salaries by the amount of pension benefits they received from prior judicial service); Cf. Sniadach v. Family Fin. Corp., 395 U.S. 337, 342 n. 9 (1969) ("For a poor man to lose part of his salary often means his family will go without the essentials." (quotations omitted)).

Similarly here, the Court should find as a matter of law that Defendants' retroactive application of SB 10-001 to Plaintiffs' COLA benefits resulted in a substantial impairment of their contractual rights to have the formula applied that was in force when they retired.

C. Senate Bill 10-001 is Regulatory Taking

The Fifth Amendment of the United States Constitution states "private property [shall not] be taken for public use, without just compensation." The Amendment is binding on the states through the Fourteenth Amendment. Penn Central Transp. Co. v. New York City, 438 U.S. 104, 122 (1978). Additionally, Article II, section 15 of the Colorado Constitution states that "private property

shall not be taken or damaged, for public or private use, without just compensation."

The Takings Clause is addressed to "every sort of interest the citizen may possess." United States v. General Motors Corp., 323 U.S. 373, 378 (1945); see Florida Rock Industries v. United States, 18 F.3d 1560, 1572 n. 32 (Fed.Cir.1994) (property interests "are about as diverse as the human mind can conceive"). In a seminal law review published almost fifty years ago, former Yale Professor Charles Reich described the role of pensions in a public employee's life:

> No form of government largess is more personal or individual than an old age pension. No form is more clearly earned by the recipient . . . . No form is more obviously a compulsory substitute for private property; the tax on wage earner and employer might readily have gone to higher pay and higher private savings instead. No form is more relied on, and more often thought of as property. No form is more vital to the independence and dignity of the individual.

Charles A. Reich, The New Property, 73 Yale L.J. 733, 769 (1964).[4]

This Court has previously found that for government employees, the promise of postretirement monetary benefits is a term of the employment contract. See Bills, 148 Colo. 38; McPhail, 139 Colo. 330. Although these cases arose under the Contract Clause, the analysis of whether a NHRS member has the requisite

[4] In 2012, this article was found to be the seventh most-cited article among all law review articles ever published. See Fred R. Shapiro and Michelle Pearse, The Most-Cited Law Review Articles of All Time, 110 Mich. L. R. 1483, 1489 (2012).

property right in his or her pension is the same under the Takings Clause. Parella v. Retirement Bd. of Rhode Island Employees' Retirement System, 173 F.3d 46, 58-59 (1st Cir. 1999) ("The facts here require us to consider whether plaintiffs had the requisite property right to support a Takings Clause claim by analyzing their claim under the Contract Clause."); Professional Firefighters Ass'n of Omaha, Local 385 v. City of Omaha, 2010 WL 2426466, *5 (D. Neb. June 10, 2010) ("[C]ut in retiree health benefits violates Contract Clause and also likely constitutes an unlawful taking, contrary to the plaintiffs' rights under the Fifth Amendment.").

In considering whether an injury to private property is an unconstitutional taking, this Court is to "evaluate the 'justice and fairness' of the governmental action." Lake Durango Water Co., Inc. v. Public Utilities Comm'n of State of Colorado, 67 P.3d 12, 19 (Colo. 2003) (quoting Eastern Enterprises v. Apfel, 524 U.S. 498, 522 (1998)). Further,

> [w]hile there is no set formula as to how this evaluation is to be made, the United States Supreme Court has identified certain factors that are particularly significant. . . . Specifically, the character of the governmental action, its economic impact, and its interference with reasonable economic expectations of the property owner.

Id. (citing Eastern Enterprises, 524 U.S. at 522-24).

SB 10-001 imposes retroactive liability on the Retirees that will have a significant economic impact on them. Further, as recounted in their Affidavits, receipt of their pension benefits, including the guaranteed COLA, was an important consideration why Plaintiffs continued to continue to work in the public sector rather than earn more money in a job in the private sector.

CONCLUSION

For the foregoing reasons, Retirees respectfully asks this Court to find that the modification to the Retiree's COLA as provided in Senate Bill 10-001 is unconstitutional as a matter of law.

Respectfully Submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on the 24th day of October, 2013, a true and correct copy of the foregoing **PLAINTIFF-PETITIONERS' AMENDED OPENING BRIEF** was e-filed with the **Clerk of the Court** via ICCES (Integrated Colorado Courts E-filing System) that will electronically notify and serve all registered, interested parties to the case, including the following:

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