NANCY SWEENEY
CLERK DISTRICT COURT
2015 JAN 20 PM 3:40
FILED
BY
Deputy

MONTANA FIRST JUDICIAL DISTRICT COURT
LEWIS AND CLARK COUNTY

JUDY BYRNE, JANET KRANSKY, SUSAN NARDINGER, HAZEL JOHNSON, LORI BREMER, CHARLENE SUCKOW, and MEA-MFT, Plaintiffs, v. STATE OF MONTANAN, TEACHERS' RETIREMENT SYSTEM, of the STATE OF MONTANA, and TEACHERS' RETIREMENT BOARD, Defendants.	Cause No.: ADV-2013-738 **ORDER ON MOTIONS FOR SUMMARY JUDGMENT**

Plaintiffs Judy Byrne, Janet Kransky, Susan Nardinger, Hazel Johnson, Lori Bremer, Charlene Suckow, and MEA-MFT (collectively "MEA-MFT") filed a complaint seeking declaratory and injunctive relief to prevent reductions to the beneficiaries of the Teachers' Retirement System (TRS) of the State of Montana. Specifically, MEA-MFT asks for a declaratory judgment that Section 11 of House Bill 377 (Section 11, Chapter 389, Laws of Montana, 2013), which reduces the guaranteed annual benefit adjustment (GABA) for TRS members, is an

unconstitutional violation of the contracts clause and the takings clause of the Montana Constitution. MEA-MFT also request a permanent injunction barring Defendants State of Montana, Teachers' Retirement System of the State of Montana, and Teachers' Retirement Board (collectively "State") from implementing Section 11 of House Bill 377. Karl Englund and Jonathan McDonald represent MEA-MFT. Matthew Cochenour represents the State.

Before the Court are cross-motions for summary judgment. MEA-MFT filed its motion July 25, 2014. The State filed its motion September 19, 2014. The motions have been fully briefed, and the parties appeared before the Court for oral argument on March 5, 2015. For the following reasons, the Court grants MEA-MFT's motion for summary judgment, grants MEA-MFT's motion for a permanent injunction, and denies the State's motion.

FACTUAL AND PROCEDURAL BACKGROUND

Plaintiffs are retired and/or actively employed Montana public education employees and members of TRS. Judy Byrne taught English, French and drama at Lewistown Junior High School from 1972 until her retirement in 1997. Janet Kransky was a librarian in public schools in Missoula, Malta, and Billings from 1969 until 1988 and from 1993 until her retirement in 2012. Susan Nardinger taught in elementary schools in Great Falls public school district from 1975 until her retirement in 2002. Hazel Johnson retired in 1991 after a 42-year career as a public elementary school teacher in Power, Fairfield, Conrad, Great Falls and Helena. Charlene Suckow taught in elementary schools in the Great Falls public school district from 1971 until her retirement in 2002. Byrne, Kransky, Nardinger, Johnson and Suckow all receive retirement benefits from TRS, including a 1.5 percent guaranteed annual benefit adjustment to their pension

benefits. Lori Bremer is currently employed teaching English and serving as a librarian in Red Lodge public schools. Upon retirement, Bremer intends to rely on the 1.5 percent GABA to pay costs associated with healthcare insurance and long-term care. MEA-MFT is a statewide labor union whose membership comprises approximately 17,500 individuals, including approximately 12,000 members of TRS and approximately 1,065 retired educators receiving TRS benefits.

In 1937, the Montana Legislature created the TRS, now codified in Title 19, section 20 of the Montana Code Annotated. The purpose of TRS is to provide equitable retirement, death, and disability benefits to members of the TRS system based upon each member's service and salary. Section 19-20-102, MCA. Membership in TRS includes educational professionals including teachers, principals, school superintendents, school nurses, speech-language pathologists, paraprofessionals who provide instructional support, administrative support staff and others. Section 19-20-302, MCA. Any person who accepts a position covered by TRS is statutorily required to become a member of TRS and to accept withholdings of contributions from the person's compensation. Section 19-20-103, MCA. TRS members and their employers pay a percentage of each member's gross pay to help fund the system benefits. Upon retirement, a TRS member is entitled to receive a monthly pension benefit payment calculated on the member's total years of service credit and average final compensation. TRS benefits are "payable pursuant to a contract as contained in statute." Section 19-20-501(6), MCA.

The TRS is a "defined benefit plan" wherein members are paid benefits upon qualification, based upon total years of service and final

compensation rates, without regard to the performance of financial markets. Section 19-20-804, MCA. In 1999, the Montana Legislature enacted a GABA which provides a 1.5 percent annual increase in monthly TRS benefits for all members who have received benefits for at least 36 months. Section 19-20-719, MCA (1999). The GABA compounds each year. In 2001, the Montana State Legislature amended the GABA to allow for annual benefit adjustments of up to 3.0 percent per year. Section 19-20-719, MCA (2001). In 2007, the Legislature repealed the 3.0 percent maximum and set the annual GABA back to 1.5 percent per year.

In Montana, public retirement systems, including TRS, must be funded on an "actuarially sound basis." Mont. Const. art. VIII, § 15. For a public retirement system to be actuarially sound, Section 19-2-409, MCA, provides the following definition:

> [A]ctuarially sound basis means that contributions to each retirement plan must be sufficient to pay the full actuarial cost of the plan. For a defined benefit plan, the full actuarial cost includes both the normal cost of providing benefits as they accrue in the future and the cost of amortizing unfunded liabilities over a scheduled period of no more than 30 years.

Although Section 19-2-409, MCA, applies to the Montana's Public Employees' Retirement Act, Sections 19-2-301 through 19-2-1015, MCA, and not to TRS, by policy, TRS has adopted this standard through the Actuarial Standards Board.

Since at least 2008, the TRS has not been actuarially sound. (Pl.'s Br. Supp. Pl.'s Mot. Prelim. Injunction (Oct. 11, 2013), Ex. A (Mont. 2008-2013 TRS Actuarial Valuations).) In 2013, the Montana Legislature passed House Bill 377, which provided for increased contributions to the system and changed the service

requirements for full retirement for new employees. Section 11 also requires a reduction in the GABA from 1.5 percent to 0.5 percent until such time as the actuarial valuation of TRS liabilities reaches 90 percent. Section 19-20-719, MCA (2013). The original version of House Bill 377 did not include a GABA reduction and the budget director for the State of Montana testified at deposition that such a change was unnecessary. (Depo. Dan Villa, 9 (Jul. 8, 2014).) The former director of the TRS system likewise testified that a reduction in the GABA was unnecessary because there were other options that were less egregious, less onerous to our members and that actuarial soundness could be restored without a GABA reduction. (Depo. David Senn, 45 (Jun. 8, 2014).) House Bill 377 Section 25, contains a severability clause that states: "If a part of this act is invalid, all valid parts that are severable from the invalid parts remain in effect. If a part of this act is invalid in one or more of its applications, the part remains in effect in all valid applications that are severable from the invalid applications."

The 2014 actuarial valuation provided to the Court shows that even without reducing the GABA, the TRS remains actuarially sound in that the unfunded liability amortizes in 28 years. (Mont. 2014 TRS Actuarial Valuation (Jul. 1, 2014).)

STANDARD OF REVIEW

Summary judgment is appropriate when "the pleadings, the discovery and disclosure materials on file, and any affidavits show that there is no genuine issue as to any material fact and that the movant is entitled to judgment as a matter of law." Mont. R. Civ. P. 56(c)(3). The party moving for summary judgment must establish the absence of any genuine issue of material fact and the party is entitled to judgment as a matter of law. *Tin Cup County Water &/or Sewer Dist. v. Garden*

City Plumbing, 2008 MT 434, ¶ 22, 347 Mont. 468, 200 P.3d 60. Once the moving party has met its burden, the party opposing summary judgment must present affidavits or other testimony containing material facts which raise a genuine issue as to one or more elements of its case. *Id.*, ¶ 54 (citing *Klock v. Town of Cascade*, 284 Mont. 167, 174, 943 P.2d 1262, 1266 (1997)). Conclusory statements and assertions are not enough to defeat a motion for summary judgment. *Id.* The mere denial of a fact does not satisfy the non-moving party's burden of establishing a genuine issue of material fact and is not a proper basis for denial of a motion for summary judgment. *Vettel-Becker v. Deaconess Med. Ctr. of Billings, Inc.*, 2008 MT 51, ¶ 27, 341 Mont. 435, 177 P.2d 1034.

The constitutionality of a statute is a question of law. *Henry v. State Comp. Ins. Fund*, 1999 MT 126, ¶ 10, 294 Mont. 449, 982 P.2d 456.

> The constitutionality of a legislative enactment is prima facie presumed, and every intendment in its favor will be presumed, unless its unconstitutionality appears beyond a reasonable doubt. The question of constitutionality is not whether it is possible to condemn, but whether it is possible to uphold the legislative action which will not be declared invalid unless it conflicts with the constitution, in the judgment of the court, beyond a reasonable doubt.

Stratemeyer v. Lincoln County, 259 Mont. 147, 150, 855 P.2d 506, 508-509, cert. denied, 510 U.S. 1011 (1993).

ANALYSIS

The Montana Constitution, Article II, section 31 provides: "No ex post facto law nor any law impairing the obligation of contracts, or making any irrevocable grant to special privileges, franchises, or immunities, shall be passed by the legislature." This provision parallels the federal constitution which states,

"[n]o state shall . . . pass any . . . law impairing the obligation of contracts." U.S. Const., Art. I, § 10. "At the time the Constitution was adopted, and for nearly a century thereafter, the Contracts Clause was one of the few express limitations on state power." *U.S. Trust Co. of New York v. New Jersey*, 431 U.S. 1, 14 (1977). Our state has enshrined this limit on state power in the Declaration of Rights, that portion of the Montana Constitution that defines governmental power and affirms the rights of the people.

The Contracts Clause is not a frequent subject of litigation—the general parameters of this limitation are well defined in federal law, which Montana looks to in interpreting our state's corollary provision. *Neel v. First Federal Savings and Loan Ass'n*, 207 Mont. 376, 388, 675 P.2d 96, 103 (1984).

In recent years, however, the Contracts Clause has taken on new life, as "[a] number of states believe that state pension deficits have run amok and that public employees are receiving much too generous benefits and paying too little for these same benefits." (Secunda, Paul M. (2011). Constitutional Contracts Clause Challenges in Public Pension Litigation, *Hofstra Labor & Employment Law Journal*, Vol. 28:263-64.)

The parties both cite numerous out-of-state cases involving recent Contracts Clause litigation in the context of pension reform. Ultimately, those cases have proved unhelpful as they turn on state-specific statutes, interpretation of common-law and constitutional language that differs from this state. In Montana, the 2013 Legislature passed a law that unnecessarily reduced pension benefits for schoolteachers and other public education professionals. The undisputed facts in this case demonstrate that increased contributions borne by workers, employers and the State, which is the guarantor of the TRS, brought

the system back to actuarial soundness without cutting any benefits. Moreover, the Contracts Clause acts to prevent financial self-dealing by the State. It does so by requiring government to choose the most moderate course of action possible when using its legislative power to change its own contractual obligations. Here, a moderate course was sufficient to return the system to actuarial soundness. The undisputed facts demonstrate no reason to cut the GABA. David Senn and Dan Villa both testified that such cuts were unnecessary and the State offered no evidence in rebuttal.

For its part, the State argues for an extreme form of deference to legislative decision-making. It argues that so long as legislators subjectively believed it necessary to cut the GABA in 2013, the courts must respect that decision. Such deference may be permissible when the government's own financial self-interest is not at stake and it acts to disrupt private contracts in the name of the public good. However, as the U.S. Supreme Court determined, "[i]f a state could reduce its financial obligations whenever it wanted to spend the money for what it regarded as an important public purpose, the Contract Clause would provide no protection at all." *U.S. Trust Co.*, 431 U.S. at 26.

This Court is mindful of its obligation to try and find a way to uphold the validity of Section 11 of House Bill 377. However, after due consideration, it cannot find a way to do so. Accordingly, for the reasons set forth below, the Court holds the challenged provision unconstitutional and permanently enjoins its enforcement.

I. Whether this matter is a Breach of Contract Case.

The State incorrectly asserts this is a breach of contract case, not a Contracts Clause case. If the State simply refused to pay the GABA that statutes

require it to pay TRS beneficiaries, then a breach of contract would arise. However, the State here has used its power to amend the statute to alter what it must pay TRS beneficiaries under the statutory contract itself. In *Warkentine v. Salina Public Schools*, 921 F.Supp.2d 1127 (2013), a teacher sued her school district for not permitting her to take advantage of an early retirement incentive program. In Warkentine, the parties disagreed whether the plaintiff was eligible for the program. When the plaintiff brought a claim for breach of contract and another for violation of the Contracts Clause, the Court dismissed the Contracts Clause claim because there was no legislative act involved. *Id.* at 1133.

Here, by contrast, MEA-MFT challenges Section 11 of House Bill 377 which changed the law itself—to the detriment of TRS members. If MEA-MFT sued under the existing post-2013 statutory scheme, they would have no breach of contract remedy because TRS is willing to pay the reduced GABA under the amended statute. The lack of a breach of contract remedy is another sign this is a Contracts Clause case, not a breach of contract case. Id. at 1133-1134 (citing *Horwitz-Matthews, Inc. v. City of Chicago*, 78 F.3d 1248 (7th Cir. 1996).)

II. Whether Plaintiffs have a Contractual Right to the GABA.

Montana law provides that "benefits and refunds" owed to beneficiaries of the TRS system are "payable pursuant to a contract as contained in statute." Section 19-20-501(6), MCA. The State argues that only the base monthly pension benefit—and not the GABA—are the "benefits" subject to protection as a contract. The basis of the State's argument is its reading of Sections 19-20-101(5) and (20), MCA, which define who is a "benefit recipient" and what is a "retirement allowance" or "retirement benefit."

///

(5) "Benefit recipient" means a retired member, not a joint annuitant, or a beneficiary who is receiving a retirement allowance.

. . .

(20) "Retirement allowance" or "retirement benefit" means a monthly payment due to a retired member who has qualified for service or disability retirement or due to a joint annuitant or beneficiary.

The State argues these statutory definitions make "no reference to a postretirement benefit adjustment of any kind," thus the GABA is outside a TRS beneficiary's contractually protected benefits. (Def.s' Combined Resp. Pl.s' Mot. S.J. & Br. Supp. Def.s' Mot. S.J. at 18 (Sept. 19, 2014).) Similarly, the State also relies upon *Wage Appeal of Montana State Highway Patrol Officers v. Board of Personnel Appeals*, 208 Mont. 33, 676 P.2d 194 (1984). There, a pre-1975 law provided that the base salary of highway patrol officers was increased by 1.0 percent for each year of service. After 1975, a new pay plan was adopted which accounted for past annual increases, but provided instead for annual "step" increases plus longevity increases. *Id.*, 208 Mont. at 35. Notwithstanding the legislative change, the Montana Highway Patrol officers subsequently petitioned to receive the annual 1.0 percent increases that were removed during the 1975 Montana Legislature. The Court ruled against them, holding "an employee's right to compensation vests or accrues only after he or she has performed the required services for that pay period." *Id.*, 208 Mont. 42 (citations omitted).

The State's statutory construction argument is unpersuasive. Section 1-2-101, MCA, provides:

In the construction of a statute, the office of the judge is simply to ascertain and declare what is in terms or in substance contained therein, not to insert what has been omitted or to omit what has

been inserted. When there are several provisions or particulars, such a construction is, if possible, to be adopted as will give effect to all.

The substantive definition of "retirement benefit" contained at Section 19-20-101(20), MCA, is "a monthly payment due." This definitional statute does not describe the mechanics of how to calculate (or annually adjust) the amount of the monthly payment due to each recipient. Rather, this is accomplished pursuant to other statutes codified within Chapter 20, Title 19 of the Montana Code Annotated. See, e.g., Section 19-20-804, MCA (service retirement formula); Section 19-20-710, MCA (maximum benefit limitation); Section 19-20-719, MCA (guaranteed annual benefit adjustment). The fact Section 19-20-101(20), MCA, does not discuss the GABA is of no consequence and certainly does not suggest the GABA is not a contractually protected part of the benefits.

Under the State's logic, the failure to mention the GABA in Section 19-20-101(20), MCA, means it is not subject to protection as part of the "contract as contained in statute." Under this reasoning, the base monthly benefit would similarly have no protection. After all, the monthly benefit is established using a formula codified at Section 19-20-804, MCA—which is also not mentioned in Section 19-20-101(20), MCA. The State's narrow reading of the definitional statute would essentially give the State unlimited authority to revise anything not specifically mentioned in Section 19-20-101(20), MCA. Each TRS beneficiary would receive a monthly benefit, but enjoy no protections in how that monthly benefit is calculated or adjusted. Clearly this is not the intent of the law. Under the State's interpretation this Court would read away the substantive nature of the protections afforded under Section 19-20-501(6), MCA, and Montana case law

recognizing the fixed nature of pension benefits. See, e.g., *Clarke v. Ireland*, 122 Mont. 191, 199 P.2d 965 (1948); *St. ex rel. Sullivan v. St. Teachers Ret. Bd.*, 174 Mont. 482, 571 P.2d 793 (1977).

Further, Section 19-20-501(6), MCA, commands contractual recognition to all "benefits and refunds," not simply "retirement benefits" which are separately defined at Section 19-20-101(20), MCA. It is hard to see how a guaranteed annual adjustment is not a "benefit" as that term is commonly understood—especially given that TRS members' contributions increased at the time the GABA was first enacted. The GABA is not merely a benefit, it is something for which TRS members paid consideration.

Next, the Court's holding in *Wage Appeal* is inapplicable here. *Wage Appeal* is not a pension case, but rather demonstrates the difference between retirement benefits and unearned wages. The Montana Supreme Court held the "crux of the whole appeal" was whether the highway patrol officers had a "vested right" to continuation of the 1.0 percent annual longevity pay increases after they were eliminated from the law. *Id.*, 208 Mont. 41, 676 P.2d at 199. The Court determined that "an employee's right to compensation vests or accrues only after he or she has performed the required services for that pay period." Thus, "the government may alter the salary of a public employee prospectively prior to the vesting of the salary right." *Id.*, 208 Mont. 42, 676 P.2d at 199. Because the highway patrol officers had not yet worked for and earned the salaries for future years, they did not enjoy a contractual entitlement to future salary increases. *Id.*, 208 Mont. 43, 676 P.2d at 199.

Wages are not the same as pension benefits. As the Court held in *Wage Appeal*, a government worker's salary may be altered prospectively, before

the work is performed and the right to the wages accrues. Pensions, on the other hand, are benefits that accrue and become a matter of right as the government worker performs her labor and contributes into the pension system. Thus, their rights accrue as they contribute through their labor and wages to the pension system—not after they have completed the work.

> As the employee or officer contributes into the fund and performs services, his rights to a pension vest, and he cannot be deprived of such vested rights by intervening legislation which inequitably operates to the detriment of such accrued rights. Stated another way, a public employee or officer who performs services and contributes to a public pension plan or system contracts in accordance with the legislation in effect governing the plan or system, and the public cannot constitutionally modify the plan or system to the detriment of the employee if such modifications are inequitable.

Leonard v. City of Seattle, 503 P.2d 741, 746-747 (Wash. 1972). See also, *Gulbrandson v. Cary*, 272 Mont. 494, 501, 901 P.2d 573, 578 (1995).

Finally, the State encourages the Court to follow the case law from New Mexico and Colorado, where courts found that COLA (cost-of-living adjustment) statutes were not part of those states' retirement system contracts. *Barlett v. Cameron*, 316 P.3d 889 (N.M. 2013); *Justus v. Colorado*, 336 P.3d 202 (Colo. 2014). Conversely, MEA-MFT identifies cases in which other state courts found COLA statutes were part of the retirement systems contracts. *Booth v. Sims*, 456 S.E.2d 167 (W.Va. 1994); *Strunk v. Pub. Employees Ret. Bd.*, 108 P.3d 1058 (Ore. 2005). Ultimately, these cases are of little assistance to this Court as they are decided based on the specific statutory, constitutional and common law considerations of other states. They are distinguishable, however, in that they all deal with cost-of-living increases that the Colorado court called "a periodic exercise of legislative discretion that takes account of changing economic

conditions in the state and/or nation." *Justus*, ¶ 24. The GABA, by contrast, is a guaranteed annual adjustment that occurs and compounds annually, regardless of changing economic conditions. A COLA could flatten or even decrease depending upon economic conditions at the time. A GABA, however, is a guarantee of annual benefit increases. This guaranteed adjustment does not account for legislative discretion or changing economic conditions.

Accordingly, this Court finds the GABA is part of the TRS benefits subject to protection as part of a "contract as contained in statute."

III. Whether Section 11 of House Bill 377 Violates the Contracts Clause.

Both the state and federal constitutions contain a Contracts Clause. This challenge is brought under the Montana State Constitution, Art. II, section 31, which states in relevant part, "No . . . law impairing the obligation of contract . . . shall be passed by the legislature."

"Although the Contracts Clause appears literally to proscribe 'any' impairment . . . 'the prohibition is not an absolute one and is not to be read with literal exactness like a mathematical formula.'" *U.S. Trust Co.*, 431 U.S. at 20 (citing *Home Building & Loan Ass'n v. Blaisdell*, 290 U.S. 398 (1934)). On one hand, "[t]he States must possess broad power to adopt general regulatory measures without being concerned that private contracts will be impaired, or even destroyed as a result. Otherwise, one would be able to obtain immunity from state regulation by making private contractual arrangements." *U.S. Trust Co.*, 431 U.S. at 22. On the other hand, "complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State's self-interest is at stake. A governmental entity can always find a use for extra money, especially when taxes do not have to be raised." *Id.*, 431 U.S. at 26.

A. Level of Scrutiny and Contracts Clause Test

The parties disagree on the level of scrutiny that applies to a Contracts Clause challenge. Both sides recognize the three-part test the Montana Supreme Court previously employed in *Seven Up Pete Venture v. State*, 2005 MT 146, 327 Mont. 306, 114 P.3d 1009, and *City of Billings v. County Water Dist. of Billings Heights*, 281 Mont. 219, 935 P.2d 246 (1997). However, MEA-MFT observes the Montana Supreme Court recently held all "rights enumerated in the Declaration of Rights (Article II) of Montana's Constitution are fundamental constitutional rights" subject to strict scrutiny and the "narrowly tailored" test. *Kortum-Managhan v. Herbergers NBGL*, 2009 MT 79, ¶ 25, 349 Mont. 475, 204 P.3d 693; *Mont. Cannabis Indus. Ass'n v. State*, 2012 MT 201, ¶ 16, 366 Mont. 224, 286 P.3d 1161. MEA-MFT argues the *Seven Up Pete* three-part test is too deferential and fails to embrace the strict scrutiny afforded to those rights found in the Declaration of Rights. The Court recognizes the tension between the expansive language in recent Supreme Court cases and the second and third prongs of the three-part test that do appear to embrace a lower level of scrutiny. However, given that the parties briefed and argued this matter based on the three-part test from *Seven Up Pete*, the Court will follow that approach. The three-part test is also consistent with the U.S. Supreme Court's application in *U.S. Trust Co.* Historically, Montana has construed its Contracts Clause in step with its federal counterpart. Thus, the Court shall consider the following in this challenge: "1. Whether the law is a substantial impairment of the contractual relationship; 2. Whether the State has a significant and legitimate purpose for the law; and 3. Whether the law imposes reasonable conditions that are reasonably related to achieving the legitimate and public purpose?" *Seven Up Pete*, ¶ 41.

Having established the factors to consider, the State asks the Court to apply a deferential standard to its decision to reduce the GABA, largely because House Bill 377, as a whole, cost the State money and thus it was not motivated by its own self-interest. (Def.s' Combined Resp. Pl.s' Mot. S.J. at 31.) The State analogizes to *Seven Up Pete*, in which a citizen initiative (I-137) banned the cyanide leaching process used in gold mining. The Montana Supreme Court found as a result of the initiative, the State lost an estimated $60 million in mining royalty payments and, thus, the State's financial interests were diminished by I-137 and no heightened scrutiny was applied to the citizen initiative. In the present matter, however, the State is the guarantor of TRS, unlike in *Seven Up Pete*. See Section 19-20-104, MCA ("the payment of all retirement . . . benefits granted under the retirement system are obligations of the state of Montana."). Before House Bill 377, TRS was facing a shortfall of many millions of dollars. The State cannot discharge that obligation in bankruptcy or otherwise. The State's financial self-interest is very much involved when it comes to dealing with an underfunded and actuarially unsound TRS.

Accordingly, the Court will apply the less deferential standard because the State's financial self-interest is implicated in its decision to impair its contractual obligations with House Bill 377. "A higher level of scrutiny is required to assess abrogations of government obligations than in the case of legislative interference with the contract of private parties." *Univ. of Hawaii Prof'l Assembly v. Cayetano*, 183 F.3d 1096, 1107 (9th Cir. 1999) (citations omitted).

B. Substantial Impairment

The first consideration requires the Court to determine whether Section 11 of House Bill 377 constitutes a "substantial" impairment of the

contractual relationship. The State of Montana argues in its briefing that the GABA is not part of the contractual relationship, thus ending the inquiry. However, as set forth above, the Court disagrees and has held the GABA is included in the contract. Thus, the question becomes whether Section 11 of House Bill 377 constitutes a "substantial" impairment. "Total destruction of contractual expectations is not necessary, and a law which restricts a party to gains reasonably expected from a contract is not a substantial impairment. Further, the extent that the particular industry has been regulated in the past will modify the amount of impairment, if any." *Neel*, 207 Mont. 392, 675 P.2d 105 (citing *Energy Reserves Group v. Kansas Power and Light Co.*, 459 U.S. 400, 411 (1983)). However, in the context of public contracts, "(a)n impairment of a public contract is substantial if it . . . alters a financial term." *S. Cal. Gas Co. v. City of Santa Ana*, 336 F.3d 885, 890 (9th Cir. 2003) (citing *Cayetano*, 183 F.3d at 1104).

Courts find substantial impairment to a contract even though the alterations to the financial terms are minimal. *Ass'n of Surrogates & Sup. Ct. Reporters v. St. of New York*, 940 F.2d 766, 772 (2nd Cir. 1991) (payroll lag of two weeks a substantial impairment); *Cayetano*, 183 F.3d at 1096 (one to three-day delay in issuing paychecks a substantial impairment); *Booth v. Sims*, 456 S.E.2d 167 (W.Va. 1994) (reduction in COLA from 3.75 percent to 2.0 percent a substantial impairment); *Strunk v. PERB*, 108 P.3d 1058, 1114-1115 (2005) (elimination of COLA on portion of pension a substantial retirement). Interference with a retiree's source of income "is not an insubstantial impairment to one confronted with monthly debt payments and daily expenses for food and the other necessities of life." *Ass'n of Surrogates v. St. of New York*, 79 N.Y.2d 39, 47 (1992).

The Court concludes Section 11 of House Bill 377 substantially impairs the contract by altering a material financial term. Indeed, if the consequences of changing the GABA were not substantial it is doubtful the Legislature would have sought to include it in House Bill 377. The collective cost to TRS beneficiaries is significant as well. Because the benefit adjustment compounds over time it becomes a significant part of a retiree's pension benefit. The actuarial evaluations of the TRS show the savings the State would realize if the GABA reduction was allowed would exceed $100 million over 30 years. In sum, Section 11 of House Bill 377 amounts to a unilateral downward adjustment in protected pension benefits for TRS members. The nature and quantum of the downward adjustment constitutes a substantial impairment.

The State argues its past regulation of the GABA militates against finding a substantial impairment. However, the presence of past regulation appears most frequently in cases involving government interference with private contracts, not the impairment of the State's own financial obligations. If this were not so, a State may avoid the Contracts Clause by repeatedly passing laws affecting those areas in which it enters public contracts. That is not what the Contracts Clause protects against. Even so, past legislation affecting the GABA never reduced the guaranteed adjustment below 1.5 percent until House Bill 377 was enacted in 2013. The Court is unmoved by the fact the Legislature amended the GABA statute in 2001 and 2007, first raising it from 1.5 percent to 3.0 percent, and then reducing it back to 1.5 percent.

Because Section 11 of House Bill 377 materially and substantially affected a financial term of a public contract, the Court will consider the next element.

C. Significant and Legitimate Purpose

The parties appear to agree the purpose of House Bill 377 was significant and legitimate. (Def.s' Combined Resp. Pl.s' Mot. S.J. Br. Supp. at 30; Br. Supp. Pl.s' Mot. S.J. at 20. ("The overarching purpose of HB377 was significant and important and is not being challenged here.").)

D. Reasonable and Necessary

The third consideration this Court will examine is "[w]hether the law imposes reasonable conditions that are reasonably related to achieving the legitimate and public purpose?" *Seven Up Pete*, ¶ 41. In the case of public contracts, the Courts require a showing that the approach used by a government impairing its own contracts was "necessary." See *City of Billings*, 281 Mont. at 229, 935 P.2d at 252; *Cayetano*, 183 F.3d at 1106; *U.S. Trust Co.*, 431 U.S. at 29.

Federal courts split on who bears the burden of proof in the context of the reasonable/necessary prong. For example, the First Circuit Court of Appeals found "where plaintiffs sue a state . . . challenging the state's impairment of a contract to which it is a party, the plaintiffs bear the burden on the reasonable/necessary prong of the Contract Clause analysis." *UAW v. Fortuno*, 633 F.3d 37 (1st Cir. 2011). By contrast the Ninth Circuit places the burden on the state. "The burden is placed on the party asserting the benefit of the statute only when that party is the state." *Cayetano*, 183 F.3d at 1106 (quoting *Seltzer v. Cochrane*, 104 F.3d 234, 236 (9th Cir. 1996). When arguing necessity, a government is "not completely free to consider impairing the obligations of its own contracts on a par with other policy alternatives." *U.S. Trust Co.*, 431 U.S. at 30-31. "An impairment may not be considered necessary if there is an evident and more moderate course of action" that would serve the State's purpose "equally

well" because the Contracts Clause "limits the ability of a state, or subdivision of a state to abridge its contractual obligations without first pursuing other alternatives." *Cayetano*, 183 F.3d at 1107 (citations omitted).

Despite which side bears the burden, the evidence before the Court manifestly demonstrates Section 11 of House Bill 377 lacks necessity. Before the State impairs its own contractual obligations, it must first consider other policy alternatives. These include raising taxes, spending some of the State's surplus, curbing government services in areas not subject to public contracts, or extending the acceptable amortization period beyond 30 years. There is no evidence the State considered these alternatives before impairing its contracts with TRS members. One possible explanation for the lack of evidence is that these alternatives were not considered because there was no reason to do so: House Bill 377, without Section 11, returned the system to actuarial soundness. The decision to cut benefits and thereby impair public contracts was entirely unnecessary.

The State argues the Legislature may have found it prudent to ensure actuarial soundness in less than 30 years—that which TRS adopted as policy. Nonetheless, the Legislature is bound to consider other policy alternatives before impairing public contracts, even if those alternatives are politically unpopular. Such is the nature of the Contracts Clause. The State further argues the Legislature may not have been aware the other sections of House Bill 377 would be so successful in returning the TRS to actuarial soundness and, therefore, Section 11 was reasonable. However, the mere concern that actuarial unsoundness may exist does not justify impairing public contracts. Before taking significant steps to impair its own contracts, the State must first consider other approaches, which it did not do so.

Accordingly, based upon the foregoing analysis and the complete lack of necessity for passage and implementation of Section 11 of House Bill 377, the Court finds the provision violates the Contracts Clause of the Montana State Constitution, Art. II, section 31.

E. Section 11 is Severable

Having found Section 11 of House Bill 377 unconstitutional, the Court turns to whether the provision is severable from the law as a whole. In Montana, "[i]f a law contains both constitutional and unconstitutional provisions, we examine the legislation to determine if there is a severability clause." *Williams v. Bd. of Co. Comm'rs*, 2013 MT 243, ¶ 64, 371 Mont. 356, 308 P.3d 88. House Bill 377 contains such a severability clause at Section 25. "The inclusion of a severability clause in a statute is an indication that the drafters desired a policy of judicial severability to apply to the enactment." *Williams*, ¶ 64. Only when a statute lacks a severability clause need the Court determine whether the unaffected provisions can stand alone. The main question in such a case is whether the remaining portion of a statute is "complete in itself and capable of being executed in accordance with the apparent legislative intent." Williams, ¶ 64.

Here, even if it did not contain a severability clause, the Court finds the remaining provisions of House Bill 377 can ably serve the legislative intent of returning TRS to actuarial soundness. Because the law does contain a severability clause, the Court defers to the drafters intent and finds that Section 11 of House Bill 377 may be severed from the remaining portions of the law.

IV. Takings Clause Challenge

Having determined that Section 11 of House Bill 377 violates the Contracts Clause, the Court declines to rule on the Takings Clause challenge raised

in MEA-MFT's complaint. On March 5, 2015, MEA-MFT argued that the Court must determine the Takings Clause challenge because the Montana version of the Takings Clause contains a provision making the payment of attorneys' fees to a prevailing party mandatory and a component of a constitutionally required remedy. See Mont. Const. Art. II, section 29. However, the parties have not yet briefed the issue of whether attorney fees are available in this matter. If attorney fees are awarded, then there remains no reason to further address MEA-MFT's arguments.

IT IS THEREFORE ORDERED that:

1. MEA-MFT's motion for summary judgment is GRANTED as to the Contracts Clause challenge.

2. The State's motion for summary judgment is DENIED.

3. The State is permanently enjoined from enforcing the GABA reduction contained in Section 11 of House Bill 377 against any tier one TRS member whose TRS-covered employment began employment before July 1, 2013.

4. MEA-MFT shall file an opening brief explaining why it believes it is entitled to attorneys' fees within 10 days of this Order. The State shall respond ten days thereafter.

DATED this 30th day of June 2015.

MIKE MENAHAN
District Court Judge

c: Karl J. Englund
Jonathan McDonald/Jay E. Suchelsky
Timothy C. Fox/Michael G. Black/Matthew T. Cochenour

MM/d