I. Legal Background

A. Public Employer Pension Were Formerly Treated As Gratuities, But Now Are Generally Considered Contract Rights

As was true with private sector pensions early in the twentieth century, courts during that era typically viewed a government pension “as a mere gratuity” that could be decreased or eliminated even in retirement. Police Pension and Relief Bd. of City and County of Denver v. Bills, 148 Colo. 383, 366 P.3d 581, 583 (Colo. 1961) (citing Albright v. Board of Trustees, 82 P.2d 765 (Colo. 1938). By the 1960’s, however, most states had abandoned this approach and had begun to view public sector pensions in the same way courts had begun to view pensions in the private sector – as a contract right. Courts began to consider the benefits “deferred compensation,” with the retiree satisfying his part of the bargain by doing the work. Currently, Indiana and Texas are probably the only states that generally follow the “gratuity” approach. See Ballard v. Bd. of Tr. of Police Pension Fund of Evansville, 324 N.E.2d 813, 815 (Ind. 1975) and Kunin v. Feofanov, 69 F.3d 59, 63 (5th Cir. 1995).

In fact, several states have actually amended their state constitutions to explicitly provide protections for public pensions, saying that rights to pensions are enforceable contractual rights – and Illinois and New Mexico are examples. At least one appears to have done this by negative inference: Minnesota used to have a statute that said “nothing in these pension laws should be construed as creating a contract,” but it eliminated this provision in 1984. 1984 Minn. Laws, Ch. 564, § 51.

---

1 Illinois: “Membership in any pension or retirement system of the State, any unit of local government or school district, or any agency or instrumentality thereof, shall be an enforceable contractual relationship, the benefits of which shall not be diminished or impaired.” Ill. Const. Art. 13, § 5; New Mexico: “contractual right of public employees to receive accrued benefits according to the terms under which they accrued.” (Cited in Pierce v. State, 910 P.2d 288, 297-298 (N.M. 1995)). See also see N.Y. Const. Art V, § 7.
But even in the vast majority of states that do not have pension-specific constitutional provisions, government workers and retirees can still prevail when they sue to protest cuts in pensions after they retire. The primary source of these rights is the Contract Clause of the federal Constitution and, in many states, a similar contract clause in state Constitutions.

B. Test As To Whether There is a Contract Clause Violation

Article 1, Section 10 of the U.S. Constitution states: “No state shall…pass any…law impairing the obligations of contracts…”. In determining whether there is a constitutional violation, Courts ask:

1. whether there is a contractual relationship,
2. whether a change in law impairs that contractual relationship, and
3. whether the impairment is substantial.

E.g., American Federation of State, County and Municipal Employees, Local 2957 v. City of Benton, Arkansas, 513 F.3d 874, 879-80 (8th Cir. 2008). Most state courts use the same test for similar contracts clauses contained in State Contracts Clauses.

1. Does a Contractual Relationship Exist and Has the Contract Right Become Vested?

There is a body of law saying that in order for a statute to “be deemed a contract for purposes of the Contract Clause,” there must be “a clear indication that the legislature has intended to bind itself in a contractual manner.” But most courts have found that the language of state or municipal pension statutes creates contractual rights protected under the Contracts Clause.

Of course language saying “this is not a contract” shows there’s no “contract” relationship. E.g., Christensen v. Minneapolis Mun. Employees Retirement Bd., 331 N.W.2d 740, 746-48 (Minn. 1983) (decided before the legislature repealed language declaring pensions were not contracts).

Mandatory statutory language (such as pensions “shall” be paid) is usually sufficient. E.g., Police Pension and Relief Board of the City and County of Denver v. McPhail, 338 P.2d 694 (Colo. 1959) (escalator clause saying pension increases “shall be” paid based on future wage increases in retiree’s former occupation was a vested contractual right that city was not free to change).

However, the pension right must “vest” before it is protected. Only after the right has been created and becomes non-forfeitable is it “vested,” and thus “protected from the invasion of the Legislature” under the Constitution.\(^3\)

Depending on the state, vesting occurs at different points in the employee-employer relationship, including the following:

**a.** When an employee begins work and starts making contributions to a pension plan (e.g., Snow v. Abernathy, 331 So.2d 626, 631 (Ala. 1976); Opinion of the Justices, 303 N.E.2d 320 (Mass. 1973); Betts v. Bd. of Admin., 21 Cal. 3d 859, 863 (1978)).

**b.** When the employee has actually retired and begun receiving benefits (e.g., Atchison v. Ret. Bd. of Police Ret. Sys. of Kansas City, 343 S.W.2d 25 (Mo. 1960); City of Louisville v. Bd. of Educ. of Louisville, 163 S.W.2d 23 (Ky. 1942) (no vested rights until individual is a beneficiary); Tait v. Freeman, 57 N.W.2d 520 (S.D. 1953)).


2. **Is the Contract Right Impaired and Is the Impairment Substantial?**

If a pension is reduced by any significant amount, courts will find that there has been a substantial impairment. *E.g.*, Booth v. Sims, 456 S.E.2d 167, 187 (W.Va. 1994) (reduction of the pension cost-of-living adjustments from 3.75% to 2% for active State Troopers who were eligible for retirement constituted a substantial impairment).

3. **Was the Impairment “Reasonable and Necessary”?**

After plaintiffs meet the three-part test, then under the federal constitution (and most state constitutions, but probably excluding Colorado\(^5\)), pension reductions can nonetheless survive a

---

\(^3\) *Pierce v. State*, 910 P.2d 288, 296 (N.M. 1995) (quotation omitted). *See also* Stephen R. Bruce, *Pension Claims Rights and Obligations* 187 (2d ed. 1993) (“When a participant has a vested or nonforfeitable right to accrued benefits it means the participant has a claim to payment, on either an immediate or deferred basis … which is “unconditional, and legally enforceable against the plan” (citing ERISA)).

\(^4\) A New Jersey statute adopts an intermediate position: N.J. Stat. § 43:3C-9.5 (vesting after 5 years of employment).

\(^5\) It appears that under Colorado case law interpreting the state contract clause, a governmental employer may not substantially impair an already vested pension for any reason, *including* (cont’d)
constitutioinal attack if the substantial impairment is “reasonable and necessary to serve an important public purpose.” Parella v. Retirement Bd. of the R.I. Employees’ Retirement Sys., 173 F.3d 46, 59 (1st Cir. 1999); see also non-pension case of U.S. Trust Co. v. N.J., 431 U.S. 1, 25 (1977).

When courts review pension reform legislation, the usual “complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State’s self-interest is at stake.”

In determining whether a substantial impairment is permissible under the federal Contract Clause, the existence of an important public purpose is not necessarily enough. Instead, courts must utilize a “balancing test” that measures the level of impairment against the importance of the public purpose.

“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.

The state has the burden of proof as to the “reasonable and necessary” defense. As part of this burden, the state must establish that there were no “evident and more moderate” policy alternatives available. U.S. Trust Co., 431 U.S. at 25.

II. Proper Forum

Based on court decisions interpreting the interplay between the Eleventh and Tenth Amendments, states and state agencies are generally immune from suit in federal court. See P.R. Aqueduct & Sewer Auth. v. Metcalf & Eddy, Inc., 506 U.S. 139, 144–45 (1993); Ernst v. Rising, 427 F.3d 351 (6th Cir. 2005). In general, Eleventh Amendment sovereign immunity generally applies to actions for money damages against the state and state officials sued in their official capacity. But, Eleventh Amendment immunity does not extend to counties and similar municipal corporations or to lawsuits filed against state officials for purely injunctive relief seeking to enjoin officials from violating federal law or the U.S. Constitution. If a governmental retirement system is held to be an “arm of the state” or a political subdivision, a federal action for money damages (or any state law claim) may not proceed in federal court due to the Tenth and Eleventh Amendments.

For these reasons, claims for benefits under state pension plans generally are brought in state court. Municipalities may be sued in either state or federal court.

(cont’d)

“Actuarial necessity.” Such defense is available only as to partially vested pensions. Police Pension and Relief Bd. of City and County of Denver v. Bills, 148 Colo. 383 (1961).


7 Christensen, 331 N.W.2d at 751.
III. Relief and Section 1983’s Application to Contract Clause and Other Potentially Relevant Theories of Recovery

Contract Clause claims for public pensions can be brought directly against the government entity in question, entitling the plaintiff to injunctive relief. *Mascio v. Public Emples. Retirement Sys.*, 160 F.3d 310 (6th Cir. 1998); *American Federation of State, County and Municipal Employees, Local 2957 v. City of Benton, Arkansas*, 513 F.3d 874, 879-80 (8th Cir. 2008).

Also, because of the broad relief described in the section (“redress,” “equitable” remedy, and attorneys’ fees), federal constitutional claims are typically pursued in conjunction with a claim under Section 1983 of the Civil Rights Act of 1871, 42 U.S.C. § 1983, which provides:

> Every person who, under color of any statute, ordinance, regulation, custom, or usage of any State ... subjects, or causes to be subjected, any citizen of the United States ... to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law, suit in equity, or other proper proceeding for redress.....

Constitutional claims against the public officials responsible for the acts in question (e.g., mayor, governor, head of pension system) are therefore usually included in a lawsuit to restore public pensions. Indeed, state governors are frequently proper defendants in cases brought under Section 1983 that seek injunctive relief. *See, e.g.*, *Burks v. Teasdale*, 603 F.2d 59 (8th Cir. 1979) (prison overcrowding case brought against Missouri Governor and state officials); *Arkansas Day Care Ass’n, Inc. v. Clinton*, 577 F.Supp. 388 (D. Ark. 1983) (claim predicated on Establishment Clause). Such “official capacity” Section 1983 actions may be brought in state or federal courts. See *Martinez v. California*, 444 U.S. 277 (1980); *Mayborg v. City of Bernard*, 2006 WL 3803393 at *12, 2007 U.S. Dist. LEXIS 77492 (S.D. Ohio 2006).

Under a sovereign immunity doctrine, however, Section 1983 actions cannot be brought against the state itself, and monetary damages cannot be recovered as to any defendants in an “official-capacity” Section 1983 actions (*Will v. Michigan Department of State Police*, 491 U.S. 58, 71 n. 10, 109 S.Ct. 2304, 105 L.Ed.2d 45 (1989)), as opposed to “personal capacity” actions which are generally not appropriate in pension suits. In other words, prospective injunctive relief can be the only remedy flowing to the class in such “official-capacity” Section 1983 actions based on the Contract Clause. However, under Section 1988, statutory attorneys’ fees may be recoverable in such actions where injunctive relief is awarded. *Pulliam v. Allen*, 466 U.S. 522, 543-544 (1984) (state judge liable for injunctive and declaratory relief under Section 1983 also liable for fees under Section 1988); *Angeline v. Mahoning County Agricultural Society*, 993 F.Supp. 627 (N.D. Ohio 1998). There may also be common fund attorneys’ fees available, and plaintiffs’ lawyers should check as to whether there is a state law theory of recovery of statutory fees is available.
However, Plaintiffs might be able to obtain monetary damages, not under Section 1983, but through a direct action under the Takings Clause of the federal Constitution, which allows plaintiffs to obtain “just compensation” for the “taking of private property.” Unlike claims for monetary damages under Section 1983, the doctrine of sovereign immunity does not protect the government from a Fifth Amendment Takings Claim because the constitutional mandate is “self-executing.” Hair v. U.S., 350 F.3d 1253, 1257 (Fed. Cir. 2003) (citing U.S. v. Clarke, 445 U.S. 253, 257 (1980)); Manning v. N.M. Energy, Minerals & Natural Resources Dept., 144 P.3d 87 (N.M. 2006) (federal Takings Clause is self-executing as applied to the states); Vokoun v. City of Lake Oswego, 76 P.3d 677, 684 (Or. App. 2003) (same).

Although the Takings Clause generally cannot be invoked for any simple taking of money, on at least one occasion a cut in government retirement benefits was held to constitute an abridgement of a property right that amounts to a Taking (Prof’l Firefighters Ass’n of Omaha v. City of Omaha, 2010 WL 2426446, at *5 (D. Neb. June 10, 2010), akin to the improper retention of interest earned on lawyer trust accounts which was the subject of cases such as Phillips v. Wash. Legal Foundation, 524 U.S. 156 (1998). See also Parella v. Retirement Bd. of Rhode Island Employees’ Retirement System, 173 F.3d 46, 58-59 (1st Cir. 1999) (suggesting that whether a plaintiff has a requisite property right in his pension is the same under the Contract Clause and the Takings Clause: “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.”); Pierce v. State, 910 P.2d 288, 304 (N.M. 1995) (discussing the possibility of such claim but ruling on other grounds.).


9 Another court has found that a retiree’s interest in his postretirement benefits was protectable under the Substantive Due Process Clause of the Fourteenth Amendment:

The Supreme Court has held repeatedly that the property interests in a person's means of livelihood is one of the most significant that an individual can possess.” Ramsey v. Board of Education, Whitley Co., Ky, 844 F.2d 1268, 1273 (6th Cir. 1988) citing Cleveland Bd. of Educ. v. Loudermill, 470 U.S. 532, 543 (1985)). The Court cannot accept the diminution of the retirement benefit as a finite loss. For thirty years on average, the Retirees provided loyal, dedicated and, at times life-threatening, service to the City. In addition to the heart-felt thanks of the citizenry of St. Bernard, these Retirees gave that dedicated service with the reasonable expectation that their retirement from City service would bring a pension and medical benefits. By its actions, the City is effectively taking some part of the years of service of each Retiree. This deprivation causes more than the loss of premium reimbursement and C-9 Trust Fund reimbursement. The Retirees also suffer the social stigma of having the City diminish the value of their public service, reduce the amount of the pension available, and the loss of economic autonomy their public careers were expected to provide.


(cont’d)

IV. **Litigation Examples**

Attempts by state and local governments have led to a number of changes to pension and other retirement benefits. Several common litigation themes are summarized below:

A. **Cost of Living Adjustment Changes**

1. Example: Minnesota Pension Litigation – state legislation reduces, freezes, and eliminates COLA benefits for a variety of state retirement plans. Motion for Summary Judgment filed by Defendants was granted at *Swanson v. State of Minnesota*, 62-CV-10-05285 (County of Ramsey, 2011), and no appeal was filed.


3. Example: South Dakota Retirement System Litigation – state legislation reduces COLA increases by instituting a formula that incorporates the CPI and the funding status of the pension fund each year. Cross-motions for summary judgment pending at *Tice v. State of South Dakota*, 10-225 (Hughes County Circuit Court).

B. **Increased Contribution Rates**

1. Example: Arizona State Retirement System Litigation. Class of teachers filed suit alleging that state legislation that changed the contribution
percentage that teachers have to pay to fund retirement benefits was unconstitutional under the Contracts Clause contained in Arizona’s State Constitution. On February 1, 2012, the Court granted Plaintiffs’ Motion for Summary Judgment, holding that the change in contribution percentage was unconstitutional.

2. Example: Florida State Pension System Litigation. Lawsuit filed by coalition of unions led by the Florida Education Association claiming that 2011 legislation that required 3% contribution of salaries to retirement system for current employees violated state contract clause.

C. Changes in Calculation of Benefits or Eligibility

1. Example: Boston Firefighter Litigation. Class fireman brought federal court litigation claiming that law violated federal and state contracts clause by changing definition of wages to eliminate a loophole that allowed disability pension to be calculated based on wages on a single day.


D. Retiree Health

1. Example: Chicago Transit Authority Litigation – state legislation authorized changes to level of benefits and required retiree contributions to retiree health insurance coverage. Federal court dismissed U.S. Constitutional claims on motion to dismiss. Ongoing litigation in Circuit Court of Cook County on state contract clause and breach of contract claims.