Michigan's Public Educator Retirement System – On the Road to Bankruptcy: A Legal Analysis of Michigan

Brett A. Geier

INTRODUCTION

Most public educators are fortunate to work in states that provide generous and guaranteed retirement benefits. In fact, most educators, especially labor organizations representing them, will pontificate that magnanimous retirement benefits compensate for perceived inequities in salary compared with private industry employees with similar degrees. Until recently, members of these retirement systems could actually calculate their benefit when they retire as part of a defined benefit plan – certainly anathema to private retirement programs. An element within public educator retirement programs is the added benefit of health care. Since 1980, Michigan retirees have been afforded health care benefits for which they were required to pay 10 percent of the premium upon retirement – the remainder was paid for by the state. Recently, the Michigan Legislature reduced the financial obligation of the State for retiree health care benefits, placing it on the individual member. In concert with the increased cost to members is the deterioration of the perceived "promise" that certain health care benefits would be provided at a fixed cost in perpetuity. Public educators, through their respective labor organization, took issue with this course of action, and have sought redress in the courts. Employing the legal technicalities of contracts, unjust enrichment, and due process, these plaintiff employees sought to reverse the enactment of the statutes making these modifications. The plaintiff education members constructed an argument that is lucid and legally viable. However, the Legislative reaction to the initial suit is shrewd, which nullified the plaintiffs' legal theory. As a result, the legislation enacted by the State, while seemingly unfair to the plaintiffs, is ultimately constitutional. Nationally, public educator retirement benefits are being reduced and the cost to the individual and school district is rising. This series of legislation and subsequent litigation occurring in Michigan is a quality analogy that is being witnessed in other states around the country.

Michigan, like many states circa 2010, was faced with a mounting budget crisis as a result of a weak economy. Looking for ways to reduce general operating expenses became a necessity for most state legislatures. An element of many state general budgets targeted for reduction is the retirement benefit offered to public educators. There are two primary components that define the complete benefit:

Dr. Brett Geier is an Assistant Professor of Educational Leadership at Western Michigan University.

the retirement allocation and the health care benefit. Many members of state retirement plans, including Michigan, are now required to pay a percentage of salary for access to retirement benefits upon qualification.[1] In 2010, the national taxpayer obligation for public educator retirement was $1.38 trillion.[2] Of that figure, $757 billion was for pension benefits and $627 billion was for retiree health care.[3] During testimony, Phil Stoddard, Director for the Office of Retirement Services of the Michigan Department of Technology, Management, and Budget amplified a growing concern that public educator retiree health care costs in Michigan exceeds $920 million.[4]

History of Public Educator Retirement in Michigan

Michigan has had a sequence of public acts dating back to the 19th century, which established the retirement system for public school employees. There were, at one time, three separate and distinct public educator retirement funds created by individual statutes:

> Employees in the public school system in Michigan are all subject to one of three retirement plans. One plan covers employees in the Detroit system. Another plan covers public school employees outside the Detroit system who are eligible for Federal social security on account of their employment in the system. The third plan covers public school employees outside the Detroit system who are not eligible for Federal social security by virtue of their employment in the system.[5]

---

[1] Rick Scott, et al. v. George Williams, et al., 107 3d. 379 (Fla. 2013) (the Florida Supreme Court reversed a circuit court judgment, which found SB 2100 (2011) unconstitutional. SB 2100 converted the Florida Retirement System (FRS) from a noncontributory system to a contributory system, requiring current FRS members to contribute 3 percent of their salaries to the retirement system).

[2] Pew Center on the States, *The Widening Gap* (Washington, D.C.: Pew Center, 2012), 1.

[3] Ibid.

[4] AFT Michigan v. State (AFT Mich. I), 825 N.W.2d 595,610 (Mich. App. 2012) (Justice Saad, who dissented in this case, was making the argument that due to increasing costs in healthcare benefits, the retirement system was becoming unsustainable and a burden to public school districts. Ultimately the burden is shifted to the taxpayers).

[5] Advisory Opinion re Constitutionality of 1972 PA 258, 209 N.W.2d 200 (1973) (opining that a statute requiring members pay an increased contribution to pensions with no corresponding increase in benefits is constitutional).

In 1980, PA 300 (The Retirement Act) was enacted, which replaced all statutes regarding public school employee retirement benefits. PA 300 of 1980, codified as M.C.L. 38.1301, established an algorithm to calculate retirement benefits:

$$Annual\ Benefit = YOS * m * FAC$$ [6]

Whereas, YOS is years of service, m is a multiplier and FAC is the final average compensation. Upon enactment, pension benefits were funded exclusively through employer contributions levied on the payrolls of local school districts.[7,8] The Retirement Act was amended in 1986 to invoke a contributory pension plan requiring members contribute 4 percent of their salary to the retirement program.[9] Despite the formation of a contributory pension plan, public schools continued to pay the entire cost of retiree health care until 2010.[10] For nearly 30 years, public educators in Michigan received health, dental, and vision benefits as part of their retirement health care package paid by the local school district.[11] Upon retirement, the Michigan Public Schools Educator Retirement Services (MPSERS)[12] paid 90 percent of the premium for a retiree, while the individual paid 10 percent. Prior to 2010, the 10 percent premium was the only cost to the employee for retiree health care benefits.

The Path of Litigation – Two Tracks For One Answer

With Michigan in the midst of a deep economic recession in 2010, the state legislature sought to reduce expenditures in the operating budget. Reforming the public educator retirement system became a primary objective for the legislative and executive branches during this period. In concert with primary benefit reform, reducing the financial obligation of the State associated with retirement health

[6] Michigan Office of Retirement Services. 2015. "Public Employee Retirement System." Michigan Public Educator Retirement System. Accessed May 28, 2015. http://www.michigan.gov/orsschools/0,4653,7-206-36450_36469---,00.html (showing the algorithm for public educator retirement: the primary factor is 1.5%. In some cases, if the employee works over 30 years, the factor is reduced to 1.25%. Therefore, any employment up to 30 years is based upon 1.5%, but additional years beyond 30 would include a 1.25% multiplier).

[7] Mich. Comp. Law § 38.1341 (1980).

[8] The contribution rate paid by employers in the system has increased from 13% of payroll in FY 2003-04 to 27% in FY 2012-2013 (prior to 2012 statutory changes) with increases projected for future years.

[9] Mich. Comp. Law § 38.1343(a) (1986).

[10] Mich. Comp. Law § 38.1341 (2010).

[11] The Public School Employees Retirement Act of 1979, Public Act 300, § 38.1391 (1980).

[12] MPSERS is comprised of the following groups of employees: employees of traditional local public schools, intermediate school districts, public school academies, district libraries, community colleges and seven public universities (employees hired before January 1, 1996).

care premiums became a collective aspiration for the state government.

This legal analysis provides a description of PA 75 of 2010 and PA 300 of 2012, which modified, and now governs Michigan's public educator retiree health care benefit. The cost for retiree health care benefits increased for employees and retirees, yet it did not provide a concomitant increase in benefits. Employees impacted by this legislation contended the new legislation violates the Federal and State Constitution. The legal position was couched in the sentiment that the Legislature was acting in an unscrupulous fashion: an ill-conceived attempt to balance the state budget by the withholding of salary of individuals. After a review of the details and impact of both public acts, a legal analysis will be provided articulating the employees' contention. Following each point of law, which proffers a violation by the plaintiffs, a refutation by the State will be offered impugning the employees' position. Lastly, concluding remarks will be provided, which synthesizes and analyzes the legal arguments, drawing a conclusion to the dispute.

The case history requires a brief overview to comprehend the primary and residual issues due to the fact that the initial suit condemning 2010 PA 75 was held in abeyance as separate litigation was filed in response to the enactment of 2012 PA 300. In addition, multiple lawsuits contending the same violation filed by different organizations were consolidated in each track as each case represented concordant issues.

The Michigan Court of Claims granted summary disposition in favor of the plaintiffs in each of the three initial cases arguing 2010 PA 75 was unconstitutional in the spring of 2011. The three separate cases introduced in the Michigan Court of Claims were consolidated into *AFT Michigan v. State*[13] *(AFT Mich I)* as they maintained congruous challenges. In August 2012, the Michigan Appeals Court, on a 2-1 vote, held that M.C.L. 38.1343(e) from 2010 PA 75 violated multiple provisions of the State and Federal Constitution. This ruling was held in abeyance due to the enactment of 2012 PA 300 and the ensuing litigation *(AFT Mich II)*. Holding for the State in all of the lower courts, *AFT Mich II* entered the Michigan Supreme Court in October 2014. In April 2015, the Michigan Supreme Court concurred with the lower courts and ruled for the State in *AFT Mich II*.

ISSUE

The enactment of PA 75 on May 19, 2010, was a radical adjustment for members of the Michigan Public School Employees Retirement System (MPSERS). The modifications affected almost 224,000 active employees.[14] Section 38.1343(e)

[13] *AFT Michigan I*, 825 N.W. 2d 595

[14] Michigan Office of Retirement Services. 2012. "Michigan Public School Employees Retirement System: Annual Supplemental Report for Fiscal Year." Michigan Public School Educator Retirement System.

amended by PA 75 of 2010 mandated that all MPSERS members contribute 3 percent of his or her wage[15] to an appropriate irrevocable trust established by PA 77 of 2010.[16] For those members making below $18,000 annually, a 1.5 percent contribution was required for the 2010 – 2011 school year only.[17] In subsequent years, all MPSERS members are required to contribute 3 percent of salary to the trust. The contributions to the irrevocable trust, "may not be refused, refunded, or returned to the employer or employee making such contributions."[18] The trust is allocated to fund current retiree health care with the goal of reducing the unfunded actuarial liability of the retirement system. The trust is not intended to fund the current employees; ergo current employees are not encompassed in an accrued benefit arrangement – a significant element in the State's defense.

As of January 1, 2013, MPSERS, complying with legislative mandate, reduced its financial obligation of the retirement health care premium to 80 percent instead of 90 percent,[19] doubling the retirees' health care premium obligation – further affronting MPSERS members. MPSERS members argued a contract providing retiree health care was established with Public Act 300 of 1980: a covenant, which employees assumed would exist in perpetuity. MPSERS members contended the health care obligation created by Public Act 300 of 1980[20] is being unconstitutionally eradicated by the legislature, which increased tension between public school employees and the state government.

The Legislature, cognizant that the judicial branch was not adjudicating in favor of the constitutionality of 2010 PA 75,[21] enacted 2012 PA 300 in order to avert further nullifications by the state courts. PA 300 of 2012 was the Legislature's remedy to address the infirmities created in 2010 PA 75. While the 3 percent contribution remained, the 2012 provision provided public school employees with a choice to "opt-in" to the health care program, or elect to qualify for a refund of contributions upon retirement if the member does not receive post employment retiree health care[22] – a notable point is that a *voluntary option* (emphasis added) was established. The Legislature directed MPSERS to pay a 1.5 percent interest rate on contributions that are refunded upon retirement at a minimum of age 60, and the payout will be over a five-year period.[23] The AFT Michigan, AFT, AFL-CIO,

---

[15] Mich. Comp. Law § 38.1343(e) (2010).

[16] Mich. Comp. Law § 38.2733 (2010).

[17] Ibid.

[18] Public Employee Retirement Health Care Funding Act of 2010, P.A. 77 § 4(1) (2010).

[19] The Public School Employees Retirement Act of 1979, P.A. 300 § 91(1) (2012).

[20] Mich. Comp. Law § 38.1301.

[21] *AFT Michigan (AFT Mich I)*, 825 N.W. 2d at 595 (holding that the Michigan Legislature has the authority to adopt legislation that seeks to remedy budgetary challenges but it must remain constrained by the Federal and State Constitution).

[22] Mich. Comp. Law § 38.1343(e); § 38.1391(a).

[23] Mich. Comp. Law § 38.1391(a)(8).

et al., the Michigan Education Association, and their members filed action in the Michigan Court of Claims challenging the constitutionality of certain provisions, some of which remained from 2010 PA 75. The Court of Claims found in favor of the State and dismissed the challenges to 2012 PA 300. Upon appeal, the Michigan Court of Appeals affirmed the lower court's decision, and the Michigan Supreme Court concurred with the ruling.

The public school employees affected by this legislation maintain the theory that a contract was created by the State, subsequently prohibiting any changes that adversely impact the members due to the protection of the Contract Clauses in the Federal and State Constitution. As a result of defining the agreement as a contract, the plaintiffs contended the quest by the Legislature to make modifications traverses the demarcation of constitutionality and should be nullified. An ancillary position is that even if an express contract was not created, an implied contract was established, qualifying the agreement for constitutional protection. The State argued that no contract for retiree health care benefits was established, nor implied. The Legislature argued that it did not, nor did it intend, to relinquish its authority to enact law. Logically, no legislature would abdicate its legislative authority, nor be forced to adhere to prior legislation that impeded it from governing for the amelioration of the public good. Amplifying this notion is the statement, "[T]he Legislature, in enacting a law, cannot bind future Legislatures."[24] The primary legal basis for both suits is founded upon the following points: impairment of a contract protected by the State and Federal Constitution, usurpation of private property without compensation, and violation of substantive due process.[25]

LEGAL ANALYSIS

Contractual Impairment

The plaintiffs contended that M.C.L. 38.1343(e) as amended by 2010 PA 75 violated the United States and Michigan Constitution, which prohibits the government from the impairment of contracts. A contract is, "an agreement between two or more parties creating obligations that are enforceable or otherwise recognizable at law."[26] More simply, contracts represent, "a promise or set of promises, to which the law attaches legal obligations."[27] Inclusive in the concept of contract is the notion of "mutual agreement and intent to promise."[28] The U.S. Constitution provides protection of contracts by declaring, "No state shall pass any law impairing the

[24] Ballard v. Ypsilanti Twp., 577 N.W.2d 890 (1998).
[25] AFT Michigan v. Michigan (AFT Mich. II), 297 Mich. App. 597 (2012).
[26] Bryan A. Garner, ed., Black's Law Dictionary (St. Paul, MN: West Publishing Co., 2010), 143.
[27] Samuel Williston, The Law of Contracts, vol. 1, (New York: Baker, Voorhis & Co., 1920), sec. 1.
[28] Ibid., sec. 3.

obligations of contracts."[29] Specifically related to retirement benefits, the Michigan Constitution further expounds upon the notion that the government may not impair contracts:[30]

> The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof, which shall not be diminished or impaired thusly. Financial benefits arising on account of services rendered in each fiscal year shall be funded during that year and such funding shall not be used for financing the funded accrued liabilities.[31] (Emphasis added)

At issue in this clause is the term "accrued financial benefit." An accrued financial benefit is a critical aspect of contention, which requires examination in order to determine whether M.C.L. 38.1343(e) passes constitutional muster.

The court ruled in favor of the employee plaintiffs in *AFT Michigan* declaring 38.1343(e) unconstitutional.[32] The cadre of justices, who composed the holding, included a plethora of rulings at the state and federal level, which amplified the point that constitutional protections exist for retirement benefits because they employ an accrued benefit mechanism.[33] An accrued benefit is dependent upon the specific plan, but is generally defined as a form of annual benefit commencing at normal retirement age.[34] Accrued pension benefits are, "on the same basis as salaries."[35] The Michigan Supreme Court held in *Campbell v. MI Judge's Retirement Bd.* that accrued retirement benefits owed to public employees are contractual.[36] When a public employee meets the criteria for vested pension benefits under state statute, his or her pension rights are contractual and shall not be eradicated by subsequent legislative action.[37]

The Campbell decision is consistent with other cases throughout the Nation, which hold vested retirement benefits are contractual. *Hickey v. Pittsburgh Pension Bd.*[38] held that retirement pay is delayed compensation for services rendered in the

---

[29] U.S. Const. art. 1, §1.

[30] Mich. Const. art. 1, §10.

[31] Mich. Const. art. 9, §24.

[32] *AFT Michigan I*, 825 N.W.2d. 595.

[33] Ibid.

[34] Governmental Accounting Standards Board. (2004). "Summary of Statement No. 45" Accessed January 21, 2015. http://www.gasb.org/st/summary/gstsm45.html.

[35] Alicia H. Munnell, State and Local Pensions: What Now? (Washington, D.C.: Brookings Institution Press, 2012), 50-51.

[36] 143 N.W. 2d 755 (1966) (holding that vested rights acquired under contract may not be destroyed by subsequent state legislation or even by an amendment of the State Constitution. Once a public employee meets the requirement for receiving a pension under state statute, his or her vested pension rights are contractual in nature and cannot be destroyed by subsequent legislative action).

[37] Ibid.

[38] Hickey v. Pittsburgh Pension Bd., 378 PA 300 (1954).

past and that an employee's participation in a public retirement system fulfills the elements of a contract. Thus, an employee's contribution to his or her retirement plan without a commensurate increase in benefits is "an unconstitutional impairment of contractual rights."[39] In *Oregon State Police Officers Ass'n et al. v. State of Oregon et al.*, the state adopted several amendments, which affected public employee pensions. One of those amendments, Ballot Measure 8, required public employees to pay 6 percent of their wages to the Public Employees Retirement System (PERS) and it could not be offset.[40] The Oregon Supreme Court held that the Contracts Clause of the Federal Constitution was violated.[41] It further described:

> The common thread running through the Oregon cases...is that the state may undertake binding contractual obligations with its employees, including benefits that may accrue in the future for work not yet performed. Moreover, the cases recognize that the PERS pension plan is an offer for a unilateral contract, which can be accepted by the tender of part performance by the employee. The Oregon line of cases is consistent with the majority of jurisdictions that have considered the issue and also is consistent with the modern view of the nature of pensions. Most jurisdictions adhering to a contract theory of pensions construe pension rights to vest on acceptance of employment or after a probationary period, with vesting encompassing not only work performed but also work that has not yet begun.[42]

The Oregon Supreme Court noted that if Ballot Measure 8 were implemented, it would, "permit the state to retain the benefit of plaintiffs' labor, but relieve the state of the burden of paying plaintiffs what it promised for that labor."[43] This does not imply that the state may not change pension benefits, even by statute. A state may certainly improve upon the benefits originally established.

In 1993, the Fourth Circuit Court of Appeals adjudicated *Baltimore Teachers Union, American Federation of Teachers Local 340, AFL-CIO v. Mayor and City Council of Baltimore*, which held that a temporary furlough plan under which employees lost .95 percent of their annual salary for one year constituted a substantial impairment of the contract.[44] "In the employment context, there likely is no right both more central to the contract's inducement and on the existence of which the parties more especially rely, than the right to compensation at the

---

[39] Marvel v. Dannemann, 490 F.Supp. 170 (D Del, 1980); Allen v. City of Long Beach, 45 Cal. 2d 128 (1955).

[40] 918 P.2d 765 (1996).

[41] Ibid.

[42] Ibid., 765.

[43] Ibid.

[44] Baltimore Teachers Union, American Federation of Teachers Local 340, AFL-CIO v. Mayor and City Council of Baltimore, 6 F.3d 1012, 1018 (CA 4, 1993).

contractually specified level."[45] The court noted, "because individuals plan their lives based upon their salaries, we would be reluctant to hold that any decrease in an annual salary beyond one that could fairly be termed *de minimis* could be considered insubstantial."[46] *Buffalo Teachers Federation v. Tobe* furthered this postulate by declaring that:

> Contract provisions that set forth the levels at which union employees are to be compensated are the most important elements of a labor contract. The promise to pay a sum certainly constitutes not only the primary inducement for employees to enter into a labor contract, but also the central provision upon with it can be said they reasonably rely.[47]

In the contest between Michigan public educators and the state, the reduction is, "three times as great and in perpetuity, not merely for a single year."[48] The plaintiffs' theory is that they have agreed to provide their labor and expertise to the school districts for wages bargained for and set forth in collective bargaining agreements. For the state to "mandate a three percent reduction in the contractually agreed – upon price of their labor is unquestionably an impairment of contract by the state."[49]

The revenue generated, as a result of this wage reduction, is being used to fund current retiree health care. Generally, courts have held that states may enact statutes, which impair contracts when the impairment is, "the consequence of remedial legislation intended to correct systemic imbalances in the marketplace."[50] The circumstances by which legislation intended to reduce remuneration must be extraordinary and of limited amount and duration. "The severity of the impairment measures the height of the hurdle the state legislation must clear."[51]

In *Baltimore Teachers Union*, the city imposed involuntary furloughs on its employees during the last three months of 1991 as a response to a $37 million dollar budget deficit. The furloughs were not implemented as a long-term funding solution, but as a temporary response to a financial emergency.[52] The city employees were furloughed for one year, which reduced annual salaries by less than 1 percent.[53] Although the furloughs were involuntary, employee work hours were correspondingly reduced according to the reduction in their wages.[54] The

---

[45] Ibid.
[46] Ibid.
[47] Buffalo Teachers Federation v. Tobe, 464 F.3d 362, 368 (CA 2, 2006).
[48] *AFT Michigan I*, 825 N.W. 2d, at 601.
[49] Ibid.
[50] Ibid.
[51] Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 245 (1978).
[52] *Baltimore Teachers Union*, 6 F.3d, at 1021.
[53] Ibid.
[54] Ibid.

Fourth Circuit concluded that the actions taken by the city were an impairment of the contract.[55] However, the wage reduction did violate the Contract Clause because, "the wage reduction was temporary, the amount of the resulting reduction in wages was no greater than necessary to meet the budgetary shortfall, and the city had first taken other actions including a significant cut in city services and laying off employees."[56] Therefore, wages, benefits and working conditions were modified for only a short period for a budget crisis; not a permanent impairment on their salaries with no concomitant reduction in the work provided.

Buffalo Teachers provides further support for this position. The city of Buffalo foisted a temporary wage freeze upon the city employees preventing scheduled wage increases from going into effect.[57] The court held that the action taken, "substantially impairs the workers' contracts with the City."[58] The factors that caused the court to adjudge accordingly were similar to the findings in Baltimore Teachers Union. The freezing of scheduled raises was temporary and did not prevent the raises from occurring – it only delayed them.[59] In addition, the freeze occurred after the city had raised taxes and laid-off staff, which demonstrated a concerted effort on the part of the city to make adjustments prior to modifying the existing contract with the city employees.[60] In *University of Hawaii Professional Assembly v. Cayetano*,[61] Act 355 of 1997 modified the pay schedule for University of Hawaii employees from a semimonthly schedule to a once per month pay to effect a conversion from a predicted payroll to an after the fact payroll.

Even though there was not a reduction in the actual amount of pay, the court determined that a significant impairment of contract had occurred because the timing of the regularly scheduled payment was bound by the collective bargaining agreement. Concurring with *Baltimore Teachers Union and Buffalo Teachers*, the Ninth Circuit Court noted that the legislature made no alternative attempts to raise revenue or constrict expenditures in a more effective and equitable manner.

While the plaintiffs in Michigan compose a cogent argument for constitutional protection of retirement benefits, there is a fatal element within the position – retiree health care benefits are not considered a vested accrued benefit within the law. The legal element of receiving accrued benefits through a vesting system is obscured in the plaintiff's argument, which is necessary in determining the impairment of a contract.

---

[55] Ibid.

[56] Ibid., 1020.

[57] *Buffalo Teachers*, 464 F.3d 362.

[58] Ibid., at 368

[59] Ibid.

[60] Ibid.

[61] University of Hawaii Professional Assembly v. Cayetano,183 F.3d. 1096 (CA 9, 1999).

It's, At Least, An Implied Contract

Even though the public school employee plaintiffs contend an express contract was created, they assert, minimally, an implied contract was established, thus, affording it constitutional protection. An implied contract is:

> An obligation created by law for the sake of justice…an obligation imposed by law because of some special relationship between the parties or because one of them would otherwise be unjustly enriched.[62]

The Supreme Court clarified this topic by declaring an implied contract is an:

> …agreement 'implied in fact' as founded upon a meeting of minds, which although not embodied in an express contract, is inferred, as a fact from conduct of the parties, in showing, in the light of their surrounding circumstances, their tacit understanding.[63]

Michigan courts have provided guidance on this issue as well. An implied contract is a legal fiction to enable justice to be accomplished, even if there was no meeting of the minds and no contract was intended.[64] A contract will be implied-in-law to prevent unjust enrichment.[65] To sustain an unjust enrichment claim, a plaintiff must demonstrate: (1) the defendant's receipt of a benefit from the plaintiff, and (2) an inequity to the plaintiff as a result.[66] Simply, to prevent unjust enrichment, the law will imply a contract when the defendant has been inequitably enriched at the expense of the plaintiff.[67] Implied contracts are analogous to the concept of quasi-contracts. A quasi-contract has obligations arising from: (a) unjust enrichment, (b) record, or (c) statute.[68] A statute is the primary element of concern for the current dispute. Ambiguity has waned in declaring whether a statute, as a component of a quasi-contract, is afforded protection by Article I, section 10 of the Federal Constitution.[69] "This species of quasi-contract is not a contract

---

[62] Bryan A. Garner, ed. Black's Law Dictionary, 9th ed. (St. Paul, MN: West Publishing Co., 2010), 296.

[63] Baltimore & Ohio R. Co. v. United States, 261 U.S. 592 (1923).

[64] Detroit v. Highland Park, 39 N.W.2d 325 (1949).

[65] Martin v. East Lansing Sch. Dist., 483 N.W.2d 656 (1992).

[66] Dumas v. Auto Club Ins. Ass'n., 473 N.W.2d 652 (1991); Karaus v. Bank of New York Mellon, 831 N.W.2d 897 (2013).

[67] Morris Pumps v. Centerline Piping, Inc., 729 N.W.2d 898 (2006).

[68] Paul G. Kauper, "What is a Contract Under the Contracts Clause of the Federal Constitution?," *Michigan Law Review* 31, no. 2 (1932): 187 – 205.

[69] Ibid.

within the meaning of Article I, section 10 of the Constitution."[70] Within this legal paradigm, the Federal Constitution protects only true contracts not quasi-contracts. "To suppose that in speaking of contracts they [the framers] meant to include 'contracts-implied-in-law,' 'quasi-contract,' constructive contracts,' or 'obligations in the nature of a contract,' is a forced and unnatural assumption."[71] The legal position that the Constitution protects only true contracts[72] leaves moot the current argument that contractual protection should be provided.

The State Contends No Contract (Express or Implied) Was Established

The most compelling argument for the State is that the health care benefit enacted in 2012 modifying the 2010 legislation does not constitute a contract with MPSERS members for health care. The state opines that an express or implied contract has not been created; *ipso facto*, no contractual violation can occur. In *Studier v. Michigan*,[73] the Michigan Supreme Court held that public school employees have no contract with the state for retiree health care benefits, nor do public school employees have vested rights in health care benefits. Six public school retirees argued that increases in their prescription drug copayments and deductibles violated the contract clause of the Federal and State Constitution.[74] The court reiterated, "one legislature cannot bind the power of a successive legislature."[75] "The constitutional prohibition in impairment of contracts is not absolute and must be accommodated to the state's inherent police power to safeguard the vital interests of the people."[76] Contained within this ruling is the necessity to narrowly construe public contractual obligations to preserve the sovereignty and democratic vitality of the state, which must remain independent to adjust its statutory commitments except where it has clearly expressed intent to bind itself to a contract.[77] Absent an expression of such intent "courts should not construe laws declaring a scheme of public regulation as also creating private contracts to which the state is a party."[78] The Legislature did not provide any portent in the Retirement Act of 1980 that it intended to bind itself in perpetuity to the terms enacted, and it would be illogical to conjecture otherwise.

---

[70] Ibid., 198.

[71] Ibid., 193.

[72] Garrison v. City of New York, 21 Wall. 196, 22 L. ed. 612 (1874); State of Louisiana v. Mayor of New Orleans, 3 U.S. 285 (1883).

[73] Studier v. Michigan, 698 N.W.2d 350 (2005).

[74] Ibid.

[75] Ibid.

[76] Health Care Ass'n Workers Compensation Fund v. Director of the Bureau of Worker's Compensation, Dep't of Consumer and Industry Services, 694 N.W.2d 761 (2005).

[77] Ibid.

[78] Ibid.

The plaintiffs raise the issue that the Legislature, through MPSERS, published multiple pieces of literature, such as pamphlets, handbooks, and brochures delineating the terms under which public school employees would be eligible for retirement benefits including health care. The plaintiffs contend that these various publications provide terms of a contract, absent a negotiated agreement, nor endorsed by either party's signature. The position held by the plaintiffs is that the courts should acknowledge that an implied contract was established by the nature of the various publications and adjudicate the matter as though an express contract was created.

The theory behind this amplification is to establish the fact that promises were made in the brochures and that the terms of retirement would be available in the future. While certain clauses in the publication provide declarative statements, (example: "your retirement will be determined by the following formula") the published disclaimer is lucid and intentional articulating the program's acquiescence to legislative modifications:

> This booklet was written as an introduction to your retirement plan. ...However, information in this booklet is not a substitute for the law. If differences of interpretation occur, the law governs. The law may change at any time altering information in this booklet.[79] [Emphasis added]

The booklet furthered this notion by providing the following statement:

> Remember this book is a summary of the main features of the plan and not a complete description. The operation of the plan is controlled by the Michigan Public School Employees Retirement Act (Public Act 300 of 1980, as amended). If the provisions of the Act conflict with this summary, the Act controls.[80] [Emphasis added]

The disclaimer confirms the Legislature did not intend to be statutorily or contractually bound, and apprised the reader thusly. If the Legislature intended to establish a contract, it would have inserted terms such as "contract," "covenant," or "vested rights." *Prima facie*, the disclaimers compel a reasonable individual to conclude that the pamphlets were intended to provide information only, and were never created as a contractual tool.

The *Studier* court held that the clauses in the Michigan Constitution pertaining to retirement benefits "prohibit the state and its political subdivisions from diminishing or impairing 'accrued financial benefits,' and during the fiscal year for which corresponding services are rendered."[81] The Michigan Supreme

[79] Michigan AFT, et al. v. State of Michigan, et al., Nos. 313960, 314065 (Mich. App. Jan. 14, 2014).
[80] Ibid.

Court, twice before, considered whether retiree health care was included within the scope of accrued financial benefit. In *Musselman v. Governor*[82] (*Musselman I*), a four-member majority of the Michigan Supreme Court held that health care benefits are included within the term "accrued financial benefit." Subsequently, the State Supreme Court granted a rehearing, *Musselman II*[83]. One justice no longer agreed with the majority, effectuating a 3-3 tie, which left unresolved the issue of whether health care benefits can be included within the phrase, "accrued financial benefits." The dissent produced a lengthy elucidation as to its rationale for couching their conclusion in an intentionalist perspective. The dissenters position was that, "statements by constitutional convention delegates show that they had employed the phrase 'accrued financial benefits' for the specific purpose of limiting the contractual right of public school employees under Article 9, section 24 of the State Constitution to deferred compensation embodied in a pension plan."[84] The dissenters furthered the argument that "The primary objective in interpreting a constitutional provision is to determine the text's original meaning to the ratifiers, the people, at the time of ratification."[85] To sum, the Michigan Supreme Court held that "health care benefits are not protected by Article 9, section 24 of the Michigan Constitution, because they neither qualify as 'accrued' benefits nor 'financial' benefits as those terms were commonly understood at the time of the Constitution's ratification and, thus, are not "accrued financial benefits."[86]

The Plaintiffs Contend an Unconstitutional Taking and Unjust Enrichment

Another point of contention Michigan public educators argue is that M.C.L. 38.1343(e) violated the Takings Clause found in the Federal and State Constitution.[87] Each of these clauses prohibits the taking of private property for public use without just compensation.[88] The State of Michigan has confiscated 3 percent of employees' wages – a point, which the state does not dispute.[89] In addition, the MPSERS members contend the 1.5 percent interest on contributions is not an acceptable return if an employee elects to not participate in retiree health care. Employee salaries "are specific funds in which they unquestionably have a property interest...[making] it quite clear, generally, that accrued salaries are property."[90] The residual debate is whether the action of withholding 3 percent

[81] *Studier*, 698 N.W.2d at 355.
[82] Musselman v. Governor, 533 N.W.2d 237 (1995).
[83] Musselman v. Governor, 545 N.W.2d 346 (1996).
[84] Ibid., 580.
[85] People v. Nutt, 469 N.W.2d 1 (2004).
[86] *Studier*, 698 N.W.2d at 360.
[87] U.S. Const., amend. V; Mich. Const., art. 10, §2.
[88] Ibid.
[89] *AFT Michigan I*, 825 N.W.2d, at 604.

of salary for retiree health care qualifies as a "taking" as defined by the Fifth Amendment and Michigan Constitution. Holding to the principle of res judicata:

> [I]t is well settled that when the government directly seizes property in which a person has a property interest, a Fifth Amendment taking occurs, requiring that the government pay compensation. However, taking cases involving a direct seizure of property typically involve real property and the exercise of eminent domain. Taking jurisprudence also commonly deals with claims that governmental regulatory actions impose such limits on the use of property that they amount to a taking.[91]

The discrepancy between real property and money supports the State's argument that the seizure of money does not constitute a "taking." *McCarthy v. City of Cleveland* held that the general imposition of monetary assessments by the government does not raise Fifth Amendment concerns. Case law provides clarity that "where the government does not merely impose an assessment or require payment of an amount of money without consideration, but instead asserts ownership of a specific and identifiable 'parcel' of money does implicate the Takings Clause."[93] The U.S. Supreme Court interjected its philosophy into the Takings Clause contention and termed such actions violations *per se*.[94] In *Brown v. Legal Foundation of Washington*, the Court held that where the government asserted a right to control the interest accrued on lawyer trust accounts (IOLTAs), even where such amounts were *de minimis*, it constituted an unconstitutional taking.[95] Similarly, in *Butler v. State Disbursement Unit*, the court:

> Found an unconstitutional taking of property when the state disbursement unit that collects and disburses child support payments deposited into the state treasury interest on the amounts awaiting disbursement...However, because the money was part of a definable and distinct parcel of money in which the eventual recipient had a property interest, it could not be taken without payment of just compensation.[96]

The Supreme Court held in *Webb's Fabulous Pharmacies, Inc., et al. v. Beckwith, Clerk of the Circuit Court of Seminole County, et al.* that it was inappropriate for a Florida county court to retain the interest from a fund in its custody intended for the payment of private creditors.[97] A Florida statute authorizing the retention of

---

[90] Sims v. United States, 359 U.S. 108, 110 (1959).
[91] *AFT Michigan I*, 825 N.W.2d, at 604.
[92] McCarthy v. City of Cleveland, 626 F.3d 280 (CA 6, 2010).
[93] *AFT Michigan I*, 825 N.W.2d, at 604..
[94] Brown v. Legal Foundation of Washington, 538 U.S. 216, 235 (2003).
[95] Ibid.
[96] Butler v. State Disbursement Unit, 275 Mich. App. 309 (2007).

the interest "has the practical effect of appropriating for the county the value of the use of the fund for the period in which it is held."[98] A state may not transform private property into public property without compensation.[99] The Supreme Court furthered this postulate by holding the Coal Industry Retiree Health Benefit Act of 1992[100] unconstitutional when the plaintiff alleged that the Act required the plaintiff to pay premiums into a fund to cover benefits for retirees it had not employed.[101]

The plaintiffs contend that pursuant to M.C.L. 38.1343(e), the State unlawfully confiscated members' property and the State is unjustly enriched by this action. The Federal Constitution speaks to this issue by providing the clause, "[N]or shall private property be taken for public use, without justification."[102] Comparably, the Michigan Constitution reinforces the takings argument by stating, "Private property shall not be taken for public use without just compensation therefore being first made or secured in a manner prescribed by law."[103]

Not So Fast – Everybody Has A Choice

The argument proffered by the State countering the plaintiffs' contention of a "Takings" violation is that there is a voluntary choice to "opt in" for retiree health care benefits or to "opt out," which allows the member to receive a reimbursement plus 1.5 percent interest upon retirement. PA 300 of 2012 was the legislation that corrected the infirmities found in 2010 PA 75. A fundamental element of disproving a Takings violation is the involuntary deprivation of private property – the transfer of property must be compelled.[104] "[Where] a property owner voluntarily participates in a regulated program, there can be no unconstitutional taking."[105] There are individuals who have ambivalent feelings about the action taken by the Legislature, yet are forced to recognize the rule of law. An example of this posture can be seen in the opinion delivered by Justice Rosemarie E. Aqulina on the contest filed in relation to the action taken against 2012 PA 300. Justice Aqulina stated:

As much as I would like to strike the section that deals with the state keeping money

[97] Webb's Fabulous Pharmacies, Inc., et al. v. Beckwith, Clerk of the Circuit Court of Seminole County, 449 U.S. 155, 156 (1980).

[98] Ibid., 164.

[99] Ibid.

[100] The Coal Industry Retiree Health Benefit Act of 1992, 26 U.S.C. 9701 §§ 9701-9722 (1994).

[101] Eastern Enterprises v. Apfel, 524 U.S. 498, 503-504.

[102] U.S. Const., amend.V.

[103] Mich. Const., art. 10, § 2.

[104] Yee v. City of Escondido, 503 U.S. 519, 527 (1992).

[105] Franklin Mem. Hosp. v. Harvey, 575 F.3d 121, 129 (2009).

> on the health care and find that it's an unjust enrichment or a taking...[my] problem is this, if it were the only choice I would strike it down. The problem is we have informed consent and there are a number of choices, so the legislature in putting together this law thought about that....They are giving choices and they are saying be careful, because if you leave early, for whatever reason, we're going to hang on to your money...Now, I'm not happy about that and it's probably usury, but it's with the party's consent.[106]

The voluntary nature of the employee contributions impugns the contention of a violation of the Takings clause by MPSERS members.

An unjust enrichment is the retention of a benefit conferred by another, without offering compensation, in circumstances where compensation is reasonably expected.[107] "Unjust enrichment of a person occurs when he or she has and retains money or benefits which in justice and equity belong to another."[108] The Michigan Court of Appeals declares that no members' wages have been confiscated due to the voluntary nature of M.C.L. 38.1391(a)(8), which provides for the repayment of members that fail to qualify for health care benefits.

The Plaintiffs Claim A Substantive Due Process Violation

The plaintiff employees contend that the 2010 legislation violates the Due Process Clause in the Fourteenth Amendment and Michigan Constitution:[109]

> [N]o state shall deprive any person of "life, liberty or property, without due process of law. Textually, only procedural due process is guaranteed by the Fourteenth Amendment; however, under the aegis of substantive due process, individual liberty interests likewise have been protected against certain government actions regardless of the fairness of the procedures used to implement them. The underlying purpose of substantive due process is to secure the individual from the arbitrary exercise of governmental power.[110]

"The essence of a claim of violation of substantive due process is that the government may not deprive a person of liberty or property by an arbitrary exercise of power."[111] The term "taking" encompasses, "governmental interference with rights to both tangible and intangible property. However, governmental action creating general burdens...will not form the basis for a cognizable taking

---

[106] Michigan AFT, et al. v. State of Michigan, et al., Nos. 313960, 314065 (2014).
[107] Garner, Black's Law Dictionary 1326.
[108] McCreary v. Shields, 657 N.W.2d 759 (2002).
[109] U.S. Const., amend. XIV; Mich. Const., art. 1, § 17.
[110] People v. Sierb, 581 N.W.2d 219 (1998).
[111] Landon Holdings, Inc. v. Grattant Twp., 667 N.W.2d 93 (2003).

claim."[112] The plaintiffs argue that the withholding of 3 percent of salary is an arbitrary contribution, which violates substantive due process.

AFT Michigan I held that a 3 percent withholding for retiree health care violated substantive due process principles. The court determined:
The mandatory contributions imposed on current public school employees, do not go to fund their own retirement benefits, but instead to pay for retiree healthcare for already-retired public school employees.

> While present employees and retired employees share a common employer, that does not mean that their interests as individuals (or even as groups of employees) are identical. Defendants have offered no legal basis for the conclusion that it comports with due process to require present school employees to transfer three percent of their incomes in order to fund retirement benefits of others. Rather, it is a mandatory, direct transfer of funds from one discrete group, present school employees, for the benefit of another, retired school employees. The fact that these groups share employers does not render the scheme outside the constitutional protection of substantive due process.[113]

Accordingly,

> it is a question of the government meeting a particular set of its own fiscal obligations. Here, the government seeks to do so by requiring a small subset of Michigan's population to surrender 3 percent of their wages, above and beyond that which they pay in taxation, with no guarantee of anything in return, to meet the government's obligation to other individuals. Defendant posits no evidence or even argument to suggest that the funding of these retirement benefits cannot be satisfied by measures that do not raise due process concerns.[114]

This decision opined the 3 percent obligation was not a "mechanism that requires individuals to fund benefits they themselves have a vested right to receive."[115] Summing that the statutory change permitted the government to "confiscate the income of one discrete group in order to fund a specific government obligation to another discrete group," the court found the 3 percent requirement of Section 43e "unreasonable, arbitrary and capricious, and violates the Due Process Clause."[116]

The State tried to obfuscate the issue by pontificating that it is only fair for those who receive a health care benefit to help pay for it. As the court stated in *AFT Michigan*, "[This] is as irrelevant as it is self-evident...the statute does not

---

[112] Corbin R. Davis, AFT Michigan v. State of Michigan: Syllabus (Lansing: Michigan Supreme Court, 2015), 1.

[113] *AFT Michigan I*, 825 N.W. 2d, at 623.

[114] Ibid., 626.

[115] Ibid., 627.

[116] Ibid.

provide that the monies obtained by the involuntary collection of three percent of the workers' wages will be used to fund the retiree health care benefits of those whose wages are being taken." The point being clarified is that members, who are required to forfeit 3 percent of their salary, will not receive a benefit in return for their contribution. In addition, there is no guarantee that health care will be provided by the State when the paying members become eligible.

The United States Supreme Court has taken issue with denying substantive due process to legislation that imposes an economic burden. In *Usery v. Turner Elkhorn Mining Co.*,[117] the Court applied due process tenets in considering a statutory provision, which required coal miners to compensate former employees disabled by pneumoconiosis. In *Pension Benefit Guaranty Corp. v. R. A. Gray & Co.*,[118] the principles of due process were applied to consider the legislative intrusion of withdrawal liability on employers who withdrew from pension plans before the effective date of such amendatory enactments. The Court cited both of these cases in *Connolly v. Pension Benefit Guaranty Corp.*,[119] whereby, it recognized the correlation between claims under the Takings Clause and claims based on substantive due process violations.[120]

Congruently, the Michigan Supreme Court acknowledged the potential of amalgamating the takings claims and substantive due process issues. In *Electro-Tech, Inc. v. H.F. Campbell Co.*, the court held:

> We are not suggesting, however, that Electro-Tech was foreclosed from a substantive due process claim in the instant case. In fact, we agree with Justice Brickley that both the United States Supreme Court and this Court have acknowledged the possibility of substantive due process claims in response to governmental regulation of property.[121]

The holding in this case is contrary to the theory proffered by the state that the constitutionality of a statute may not be scrutinized under the substantive due process standard and a takings analysis.

The State's Response To The Substantive Due Process Violation Claim

The Michigan Supreme Court clearly juxtaposes its affirmation of the holding for the State in *AFT Michigan II* with that of *AFT Michigan I*. The court forcefully delineates a major cause between the rulings was the inclusion of a voluntary

---

[117] Usery v. Turner Elkhorn Mining Co., 96 S. Ct. 2882 (1976).
[118] Pension Benefit Guaranty Corp. v. R. A. Gray & Co., 104 S. Ct. 2709 (1984).
[119] Connolly v. Pension Benefit Guaranty Corp., 106 S. Ct. 2709 (1984).
[120] Ibid., 223.
[121] Electro-Tech, Inc. v. H. F. Campbell Co., 445 N.W.2d 61, 69-70 (1989).

option to participate. In the 2010 iteration, the State made contributions mandatory for current employees and those contributions did not go to fund their own health care benefits but, instead, to pay for health care benefits of those who already retired. Commenting upon the fairness of this issue, the Michigan Court of Appeals stated:

> We cannot envision a court approving as constitutional a statute that requires certain individuals to turn a portion of their wages over to the government in return for a 'promise' that the government will return the monies, 'cancel' the 'promise' at any time and does not even agree that, if they do so, the required 'loan' money to their employer school districts, with no enforceable right to receive anything in exchange and without even a binding guarantee that the 'loan will be repaid.[122]

This segment of the *AFT Michigan I* opinion clearly articulates that state jurisprudence supported a substantive due process violation when the employees were ensnared in an involuntary taking of private salary. The court duly noted that constitutional infirmities existed in PA 300 of 2010.

When addressing the disputation of PA 300 of 2012, the Michigan Court of Appeals deviated from its original opinion that PA 300 of 2010 violated substantive due process. Amplifying the lower court's ruling, the Court of Appeals noted that the legislature carefully crafted PA 300 of 2012 with the infirmities noted by the plaintiffs regarding their complaint regarding the 2010 legislation. The most significant issue in that complaint – the fact that the state required a payment without consideration – was resolved when the legislature provided an option to participate with those receiving a reimbursement for "opting out." The court reasoned that in spite of the absence of a guarantee that retirees will receive health care benefits, the legislature maintains a duty to enact legislation. Courts do not render judgments on the wisdom, fairness, or prudence of legislative enactments.[123] The Michigan Supreme Court was not oblivious to the fact that many school employees intensely disliked the policies enacted by 2012 PA 300, however decisions concerning the allocation public resources will leave some parties disappointed.[124]

---

[122] *Michigan AFT II*, 297 Mich.App., at 625.

[123] Lansing Mayor v. Pub. Serv. Comm., 680 N.W.2d 840 (2004).

[124] AFT Michigan, et al. v. State of Michigan et al., ___ N.W.2d___ (2015)

CONCLUSION

States throughout the Nation are struggling with budget deficits while needing to maintain public services. Due to multiple economic factors, public educator retirement programs are becoming less solvent and necessitate restructuring. In many states, restructuring means members are required to assume more financial responsibility or lose benefits. Members of these retirement programs are seeking redress in court hoping to demonstrate contractual and constitutional violations as a result of the legislative modifications. The trend continues that courts are siding with state governments permitting them to modify public educator retirement programs reducing benefits and increasing individual costs. The Michigan public educator health retirement benefit contest is a prime example of this dispute.

Fairness and constitutionality are separate concepts. Fairness as perceived by Michigan's public educators remains allusive in regards to the State usurping 3 percent of their salary for retiree health care. The plaintiff public employees' argument fails on multiple points. First, no contract, expressed or implied, was created. The mechanism used by the plaintiffs to prove a contract was created – a brochure – is a weak legal theory. Compounding the lack of standing, the brochure included a disclaimer deferring the terms of the retirement program to legislative modification – the brochure was informational only. It is problematic to the plaintiffs' argument that a legislature would position itself to terms such as this in perpetuity. Second, the Michigan Constitution addressed directly the notion of vesting and accrued financial benefits – to which health care benefits do not qualify. Consequently, it is in error to make the claim that the financial obligation enacted by the Legislature on health care benefits is unconstitutional through the Contract Clauses. Third, and the most compelling defense position is the prophylactic nature of 2012 PA 300. By providing members with a choice to participate in retiree health care, the legislature ensured that a court could not hold that the legislation violated the Takings Clause of the State or Federal Constitution. As the plaintiffs created a quality argument in response to 75 PA 2010, as supported by lower courts' affirmation, 300 PA 2012 corrected the infirmities found in the 2010 legislation and nullified any conflicts.

REFERENCES

Davis, Corbin, R. *AFT Michigan v. State of Michigan: Syllabus*. Lansing: Michigan Supreme Court, 2015.

Garner, Bryan A., ed. *Black's Law Dictionary*. Pocket Edition. St. Paul: West Publishing Co., 2010.

Garner, Bryan A., ed. *Black's Law Dictionary*. 9th ed. St. Paul: West Publishing Co., 2012.

Kauper, Paul G. "What is a Contract Under the Contracts Clause of the Federal Constitution?" *Michigan Law Review 31*, no. 2 (1932): 187 – 205.

Michigan Office of Retirement Services. *Public Employee Retirement System*. 2015. http://www.michigan.gov/orsschools/0,4653,7-206-36450_36469--,00.html.

Michigan Office of Retirement Services. *Michigan Public School Employees Retirement System: Annual Supplemental Report for Fiscal Year*. Lansing: Michigan Office of Retirement Services, 2012.

Munnell, Alicia, H. *State and Local Pensions: What Now?* Washington, D.C.: BrookingsInstitution Press, 2012.

Pew Center on the States. *The Widening Gap*. Washington, D. C.: Pew Center, 2012.

Willston, Samuel. *The Law of Contracts* 1. New York: Baker, Voorhis & Co., 1920: sec.1 – 3.