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Kristen Barnes

THE PUBLIC PENSION CRISIS THROUGH THE LENS OF STATE CONSTITUTIONS AND STATUTORY LAW

KRISTEN BARNES*

I. INTRODUCTION

A study of cities and states in crisis would not be complete without analyzing public pensions. Public pension debt is a major contributing factor to the economically precarious condition of many states and municipalities.[1] With financial disaster looming, cities and states are devising creative ways to reduce their pension debt liabilities or to escape payment entirely,[2] and insulate themselves from any legal repercussions.[3] Increasingly, governments are fixating on state constitutions in an effort to identify solutions to their fiscal dilemmas, which have been exacerbated by public pension obligations.[4] The state constitution is one logical site of interest given its position in creating, structuring, and preserving pension rights. State statutes delineating pension rights are also relevant to this analysis.

This Article has three primary objectives. First, it seeks to identify the legal nature and limits of pension rights by examining them primarily through the frames of state constitutional and statutory law. Specifically, the emphasis is on the formulation of pension rights and the state's, and to some extent cities, obligations under publicly managed retirement systems.

* Associate Professor of Law, University of Akron School of Law, J.D. Harvard Law School, Ph.D. Duke University.

1. *See* THE PEW CHARITABLE TRUSTS, THE STATE PENSIONS FUNDING GAP: CHALLENGES PERSIST, 1–10, (2015), http://www.pewtrusts.org/~/media/assets/2015/07/pewstates_statepensiondebtbrief_final.pdf [https://perma.cc/YRD2-4U33]. *See also* THE PEW CHARITABLE TRUSTS, A WIDENING GAP IN CITIES: SHORTFALLS FOR FUNDING FOR PENSIONS AND RETIREE HEALTH CARE, 1–56 (2013), http://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2013/pewcitypensionsreportpdf.pdf.

2. *See* Mark Brown, *Could the City Walk Away From Pension Obligations*, CHI. SUN TIMES (May 19, 2015), http://chicago.suntimes.com/columnists/brown-could-the-city-walk-away-from-pension-obligations/ [https://perma.cc/QMQ5-E9WQ].

3. *See* Eric Madiar, *Is Welching on Public Pension Promises an Option for Illinois? An Analysis of Article XIII, Section 5 of Illinois Constitution*, 48. J. MARSHALL L. REV. 167, 242–85 (2014) (discussing legality of proposal to revise state pensions).

4. Finance Professor Joshua Rauh, who has written extensively about pensions, has been quoted as advocating the amendment of state constitutions for "current employees." *See* Monica Davey & Mary Williams Walsh, *Pensions and Politics Fuel Crisis in Illinois,* N.Y. TIMES (May 25, 2015), http://www.nytimes.com/2015/05/26/us/politics/illinois-pension-crisis.html?_r=0 [https://perma.cc/5SJL-B4A8].

The paper scrutinizes how different constructions impact the strength of pension-holders' rights by analyzing and comparing statutory language and key state constitutional provisions grounded in the law of contract, property, and due process guarantees. Second, this piece references several cases involving the restructuring of pension benefits to consider how state courts have interpreted the relevant constitutional and statutory provisions and how judges have responded to legislative attempts to restructure pensions. The cases include *In re Pension Reform Litigation*,[5] *Kanerva v. Weems*,[6] *Smith v. Board of Trustees of Louisiana Employees' Retirement System,*[7] *State ex rel. Horvath v. State Teachers Retirement Board*,[8] and *In re City of Detroit, Michigan*.[9] They cover the jurisdictions of Illinois, Louisiana, Ohio, and Michigan. Regarding Michigan, the paper is concerned with how the federal government's intervention in this realm affects state constitutional provisions designed to provide protection to pension-holders' rights. Under this heading, this paper explores the legal limit of pension rights in the context of bankruptcy; it further offers a brief discussion of the role the federal government may play in resolving pension battles, but only to give some attention to mechanisms that may be needed if there is a stalemate between unassailable, constitutionally-grounded pension rights and state or municipal insolvency. Third, the paper considers the ability to influence the fiscal behavior of government officials through state constitutions.

Richard Briffault's work on spending and tax limits in state constitutions is relevant to the paper's third objective. In "The Disfavored Constitution: State Fiscal Limits and State Constitutional Law," Briffault concludes that there is a disjuncture between a strategy of placing spending limits within constitutions in order to curtail the practice of directing state finances towards the benefit of private entities, and a political reality defined by government officials who successfully evade the restrictions imposed upon them.[10] Advocates of fiscally restrictive measures, such as spending and taxation limits, maintain that they are needed so that public finances will be available for public resources such as education, infrastructure, and health

5. 2015 IL 118585 1 (Ill. 2015).
6. 2014 IL 115811 1228 (Ill. 2014).
7. 851 So. 2d 1100 (La. 2003).
8. 697 N.E.2d 644 (Ohio 1998).
9. 504 B.R. 97 (E.D. Mich. 2013).
10. According to Briffault, "[t]here is an enormous gap between the written provisions of state constitutions and actual practice. State legislatures and local governments have repeatedly sought to expand the scope of 'public purpose' and to slip the restraints of tax and debt limits." Richard Briffault, *The Disfavored Constitution: State Fiscal Limits and State Constitutional Law,* 34 RUTGERS L.J. 907, 909 (2003) (citation omitted).

care costs.[11] Rather than accomplishing responsibly restrained fiscal governance, however, "[d]ebt limits have affected the form of state and local debt, but they do not appear to have significantly affected the total amount of debt."[12] Correlatively, instead of state constitutions being insulated from the politics that can undermine the public interest, Briffault argues that the monetary restraining provisions designed to protect public goals end up being re-entangled in politics.[13] State government officials and legislators ultimately frustrate the provisions by crafting laws to circumvent them. Judges further facilitate the evasion of revenue constraints by deferring to the legislature when interpreting the laws.[14]

This paper reflects on whether Briffault's conclusion—that regardless of the constitutional fiscal protections designed to benefit the public, government will find a way to navigate around them—also holds true with respect to constitutional protection for pensions. The piece probes the issue of whether having pension protections grounded in the state constitution actually helps public employees—by ensuring that state and local governments remain legally obligated to pay them the benefits they were promised when they were hired—or whether the protections are nullified by the evasive actions of state legislatures and other government officials.

State constitutional provisions can function as effective barriers to legislative maneuvers that are aimed at revising pension plans to the detriment of existing plan participants. The efficacy of the provisions depends upon several matters: (i) whether the provisions delineate a contractual relationship between the public employer (i.e. the state or related governmental entity) and employee; (ii) whether the pension clearly defines the vesting of the employee's interest in the pension, or leaves such terms open to interpretation; and (iii) whether the state constitution addresses the ability of legislative powers to diminish pension rights or the applicability of the state's sovereign police powers to those rights. Finally, the influence of the judiciary in construing the scope of the enforceable rights of public workers should not be discounted.

Without clearly defined rights and restrictions, there is no decisive answer regarding the course of action courts will pursue. Case law across jurisdictions bifurcates on interpreting protective provisions broadly to hold laws that negatively revise public pensions, constitutionally invalid, or finding persuasive the ominous financial forecasts of government officials

11. *Id.* at 908–09.
12. *Id.* at 925.
13. *Id.* at 956.
14. *Id.* 955–57.

and the lack of clarity in defining pension rights to uphold legislative revisions. Finding viable solutions is a matter of critical urgency related to the financial solvency of local and state governments. The crisis calls for governments to adopt sage well-balanced strategies that are prospective looking, in that they consider the stability and health of the region, and they do not severely harm pensioners, economically. This means that if the state constitution lacks protection pension language, it should be amended, where possible, to add the recommendations proposed herein. If there are constitution-based protections but legislators, mayors, and governors may exploit their deficiencies, the protections should be reinforced to guard against such political gamesmanship. Even though these recommendations require the requisite political will and legally and formally commit governmental entities to satisfying pension obligation costs, this is the proper course of action, as it requires governments to fulfill the promises they made to their workers. Unless the government apprised job candidates that the proposed benefits were conditional, rather than guaranteed, it is likely that candidates evaluated their offers based upon the full range of benefits (*e.g.*, cost of living adjustments, health care) that were presented to them, at the time of the offer. In general, states should identify solutions that do not eviscerate pension obligations. To ensure that pension rights are firmly established, drafters of the constitutional provisions should take heed of this Article's critical advice. If states and municipalities treat pensions in the manner advocated herein, it would not only benefit public sector workers but also, stabilize regional economies.

This paper proceeds as follows: Part II discusses the scope of the problem by focusing on four states, Illinois, Louisiana, Ohio, and Michigan; next, Part III analyzes the various approaches states have taken towards pensions rights in state constitutions and statutes and the different strategies deployed to restructure public pensions; this section also offers recommendations for balancing the interests of pensioners and state and local governments; finally, Part IV concludes the paper.

II. THE SCOPE OF THE PUBLIC PENSIONS PROBLEM AND STATE AND LOCAL GOVERNMENT STRATEGIES FOR TACKLING IT

Many cities and states are experiencing a crisis related to their public defined benefit pension plans.[15] The Pew Charitable Trusts reports that in

15. THE PEW CHARITABLE TRUSTS: THE STATE PENSIONS FUNDING GAP, *supra* note 1, at 1. Michelle Wilde Anderson comments that "[e]ven with the recovery of pension assets on the stock market and the passage of legal reforms that require more cautious pension fund valuation going forward, a worrisome number of local budgets are dragged down by unfunded liabilities for pensions and

2013, state pension deficits for the nation were at "$968 billion."[16] The deficit refers to the gap between the retirement benefits the government has already promised to public workers at the time of their employment and "the funding available to meet those obligations."[17] Courts, political constituencies, the legislature, and government officials should be well informed of the intricacies related to financing public pensions and the primary factors fueling the crisis in order to properly address this massive complex problem. A preliminary step to gaining a firm grasp of the matter is acquiring an understanding of the component parts of pensions and the historical, social, and economic context in which public employers developed plans of this type to achieve several goals. These objectives include managing budgets, deferring compensation, and competing effectively with other jurisdictions for workers by offering a secure financial package for the future.

Robert Novy-Marx and Joshua Rauh explain the mechanics of a defined benefit ("DB") pension:

> In a defined benefit pension plan, the employer promises the employee an annual payment that begins when the employee retires, where the annual payment depends on the employee's age, tenure, and late-career salary.[18]

Funding for defined benefit plans is composed of monetary contributions from a public sector employer and its employees, and the investment returns on the contributions.[19] There are various aspects to public pension governance. Depending upon whether municipal or state pensions are at issue, the entities responsible for governance may include governors, mayors, pension boards, and the state legislature.[20] Ideally, the participants (i.e. state or local governing entities and the employees) make the requisite contributions over a period of time, and their contributions are invested periodically and responsibly so that, as each employee-participant retires, there are sufficient funds to pay the pension benefits. Employers also may

other post-employment benefits." Michelle W. Anderson, *The New Minimal Cities*, 123 YALE L.J. 1118, 1146 (2014).

16. THE PEW CHARITABLE TRUSTS: THE STATE PENSIONS FUNDING GAP, *supra* note 1, at 1.

17. *Id.*

18. Robert Novy-Marx & Joshua D. Rauh, *The Liabilities and Risks of State-Sponsored Pension Plans*, 23 J. ECON. PERSP. 191, 191 (2009).

19. LANCE CHRISTENSEN & ADRIAN MOORE, PENSION REFORM HANDBOOK: A STARTER GUIDE FOR REFORMERS, 1–132 (2014), http://reason.org/files/pension_reform_handbook.pdf [https://perma.cc/ANY9-RKC4].

20. *See* Madiar, *supra* note 3 at 170. *See also* CHRISTENSEN & MOORE, *supra* note 19, at 51.

include, *inter alia*, cost of living adjustments to address inflation, and health care benefits as part of an employee's benefits package.[21]

There are numerous assumptions built into this ideal model. For a public pension retirement system to operate properly, the necessary level of contributions must be accurately calculated. The state government must actually make the contributions so that the invested amounts can accumulate earnings, and the investment vehicles selected must be ones that are likely to yield sufficient returns.[22] Often this is not the case.[23] In addition to using imprecise metrics, some cities[24] and states have failed to make their requisite contributions consistently in the proper amounts.[25]

The Government Accounting Standards Board ("GASB") is one of the chief contributors to the current prevailing pension issues. GASB is a private non-profit entity. It is responsible for issuing generally accepted accounting principles, known as GAAP. Many public pension systems adhered to the policies and procedures of GASB,[26] even though, during the primary years when pension debt was exponentially growing, the accounting principles "were not federal laws, nor was the SEC allowed to enforce them."[27] There were two essential problems with GASB's old framework[28]: first, contributions to fund the system, and second, the calculation of liabilities—which relates to the level of contributions participants need to make to ensure solvency. GASB did not mandate that public entities make con-

21. CHRISTENSEN & MOORE, *supra* note 19, at 55.

22. Regarding the latter point, unless the investments are fixed income investments or savings instruments, such as certificates of deposit or some bonds, they will have an appreciable degree of risk. The plan administrator's task then is to find investment vehicles that offer a reasonable amount of risk and return. There are financial consultants that can help identify the appropriate investments and to assess the risks associated with each of them.

23. Anderson, *supra* note 15, at 1145–51. *See also* THE PEW CHARITABLE TRUSTS, A WIDENING GAP IN CITIES, *supra* note 1, at 1–54.

24. THE PEW CHARITABLE TRUSTS, A WIDENING GAP IN CITIES, *supra* note 1, at 25–26.

25. Illinois, for example, has consistently lapsed in its obligations to make the state's required contributions to the pension fund. *See* Madiar, *supra* note 3 at 168 (commenting that Illinois' "pension liabilities stem from the State's decades-long failure to make its required contributions to the five pension systems.").

26. Robert Novy-Marx & Joshua D. Rauh, *The Liabilities and Risks of State-Sponsored Pension Plans*, 23 J. ECON. PERSP. 191.

27. Robert Pozen & Bhrij Khuruna, *Tough Choices for the Illinois Pension System*, HARV. BUS. REV., June 2011, at 2.

28. Since 2009, GASB has updated its guidance standards to identify approaches that will provide a more accurate assessment of unfunded pension liabilities. The latest standards may be found on their website at http://www.gasb.org. *See also* THE PEW CHARITABLE TRUSTS, THE STATE PENSIONS FUNDING GAP, *supra* note 1, at 7 ("Starting with the reporting of 2014 data, new standards required by GASB will provide additional data that policymakers can use to supplement the ARC [Actuarial Required Contribution] and evaluate the fiscal health of plans as well as policies' sufficiency to reduce pension debt.").

tributions to cover all of its DB plan participants.[29] It only required that the system have sufficient funds to pay present retirees.[30] Thus, the GASB approach was setting up a serious issue as to the sustainability of retirement systems (i.e. whether the plans would be able to deliver the promised benefits to all retirees, as they became due).

Regarding the second matter of GASB's endorsed method for calculating pension liabilities, Robert Novy-Marx and Joshua Rauh argue that GASB's method has resulted in the gross understatement of pension liabilities by many states.[31] Cities are also suffering under the weight of similar understating problems.[32] Specifically, under GASB's rules in effect in 1995, "government units were allowed to calculate the net present value of their pension liabilities using a discount rate based on the expected return of assets, instead of on US Treasury bonds as required for corporate pension plans."[33] Since the projected rate of return is used to discount present pension liability, an estimated high rate of return on the pension fund investments affects the number governments may present as their pension debt obligation.[34] GASB's recommended practice incentivized government entities to overstate the likely return on their investments, which in turn impacted the characterization of their pension liability and resulted in a distorted view of the amount of contributions needed to meet pension obligations over time.[35] For example, as Robert Pozen and Bhrij Khurana note:

> Illinois used an 8.5% rate to discount its pension liabilities, a rate that reflected its expectations about its long-term investment return. This was

29. Pozen & Khuruna, *supra* note 27, at 2 (recounting the history of Illinois' defined benefit plans).

30. Pozen and Khurana note that, prior to 1986 "GASB had not required states to make contributions to their DB plans based on their future retiree claims, only that they make the payments required for current retirees." Pozen & Khuruna, *supra* note 27, at 2.

31. Novy-Marx & Rauh, *supra* note 18, at 192 (arguing that states should not be permitted to underreport their pension liabilities based upon an inappropriate government accounting standard that "require[s] them to discount their liabilities at the expected return on their assets" and noting that "state pension funds are invested in risky assets.").

32. Stanley J. Garstka & Rick Antle, *Can Better Accounting Avert a Pension Crisis?*, YALE INSIGHTS, (2013), 1–9, http://insights.som.yale.edu/insights/can-better-accounting-avert-pension-crisis.

33. Pozen and Khuruna, *supra* note 27, at 4.

34. The connection between the discount rate and decision-making regarding public pension fund investments is:

> American public pension funds are allowed (under rules from the Government Accounting Standards Board) to discount their liabilities by the expected return on their assets. The higher the expected return, the higher the discount rate. That means, in turn, that liabilities are lower and the amount of money which the employer has to put aside today is smaller.

Buttonwood: Putting it all on red, THE ECONOMIST (July 30, 2016), http://www.economist.com/news/business-and-finance/21702623-rules-encourage-public-sector-pension-plans-take-more-risk-putting-it-all.

35. Pozen & Khuruna, *supra* note 27, at 6.

much higher than the interest rate on 10-year US Treasury bonds of 3.5% in 2003.[36]

Whether pension systems are able to meet their stated expected rate of return depends upon the performance of their investments. The returns on the equity investments fluctuate with the market. Some years will be stellar with high earnings while others will be marked by precipitous declines. Another aspect then of whether governments are following sound pension practices is the management of pension funds so that monetary surpluses are retained to cover the down cycle periods. In the wake of the impending crisis and the high level of attention being given to pension deficits, GASB updated and clarified the accounting method for properly measuring pension debt by issuing a new rule in June 2012.[37] Applying accounting measures that accurately assess the value of pension funds is an important step towards addressing the current condition of public pension debt obligations and averting similar future crises. Presumably, if municipal and state governments have a realistic assessment of the status of their pension funds they will comprehend the urgency of making the necessary annual contributions and will identify strategies (e.g., various taxes) to meet their obligations.

The literature shows that where there are issues with the financing of pension obligations, shortfalls are often due to matters firmly within the control of government entities, appointees, designated pension boards, and legislatures ("Government Public Pension Decision-makers"). In addressing the challenges of public pension systems, it is important to bear in mind that, even though pension-holders have input through voting for government representatives and pension board representatives or through actually serving on the boards, Government Public Pension Decision-makers have decisive control over numerous functions which relate to the operation of pension systems and their performance.[38] For example, according to their respective scope of authority, the decision-makers are responsible for deciding the content of pension benefits, contributing the requisite amount to

36. Pozen & Khuruna, *supra* note 27, at 4.

37. GASB Rule 68 can be found on its website, http://www.gasb.org/jsp/GASB/Pronouncement_C/GASBSummaryPage&cid=1176160219492.

38. Typically, boards of trustees manage public pension funds. *See Public Employee Retirement System Investments*, GOV'T FIN. OFFICERS ASS'N (Oct. 2009), http://www.gfoa.org/public-employee-retirement-system-investments ("Subject to applicable federal, state, and local laws, and judicial decisions, PERS investment programs are governed by investment policy objectives and constraints established by pension fund fiduciaries (individuals who are given the authority to hold assets for another party according to a trust agreement). For most public-sector pension plans, investment decisions are made by a PERS [Public Employee Retirement System] board of trustees comprising elected and/or appointed fiduciaries.").

the pension funds or allocating the requisite amounts to other areas, and the amount of the contribution. The designated decision-makers also enter into contracts with pension fund managers, who then select investments and agree to the payment of investment companies' fees.[39]

How governments perform these duties directly impact the overall health of pension funds and the financial health of state and local economies. With respect to factors that are outside the control of government officials—such as severe economic downswings like the Great Recession—these cyclical aspects should be accounted for by the plan manager's risk assessment of the portfolio. Negative economic fluctuations should not serve as an acceptable reason for restructuring pension plans for existing plan participants.

The fears regarding the public pension crisis are wide-ranging and run deep, with some states concluding that if they can find no relief from their pension debt some time in the near future, most, if not all, of their revenues will need to be directed towards paying pension obligations rather than providing vital services for residents.[40] For public employment retirees who are in those states that do not even have the back-up support of social security, their circumstances are worse; Illinois,[41] Louisiana, and Ohio fit in this category.[42] If state legislatures are permitted to restructure accrued pension obligations, pensioners in these jurisdictions will need to find an alternative means to fund their retirement. At some point, the costs are likely to fall on the larger population in the form of taxes.

39. *See* Novy-Marx & Rauh, *supra* note 18, at 202–04 (analyzing the dismal condition of many state pension funds and attributing the problems in part to "investment in risky assets that have performed very poorly in the last few years."). Aleksander Andonov, Yael V. Hochberg, and Joshua D. Rauh, in their study of municipal and state public pension systems comment that "[t]he Board of administration for a public pension fund is responsible for the management and control of the pension fund . . . [The board's responsibilities may include] setting employer contribution rates, determining investment asset allocations, providing actuarial valuations, and much more." They conclude that "[w]ithin fund types . . . the share of state government officials and the share of elected participants is strongly correlated with several known proxies for poor investment selection in private equity." Aleksander Andonov, Yael V. Hochberg, & Joshua D. Rauh, Pension Fund Board Composition and Investment Performance: Investment from Private Equity 4, 8 (Hoover Inst., Working Paper No. 16104, 2016), http://www.hoover.org/sites/default/files/research/docs/16104_-_pension_fund_board_composition_and_investment_performance_-_andonov_hochberg_and_rauh.pdf

40. *See* THE PEW CHARITABLE TRUSTS, THE STATE ROLE IN LOCAL GOVERNMENT FINANCIAL DISTRESS 8 (2013). *See also* Davey & Walsh, *supra* note 4, at 4.

41. Not only do participants in non-Social Security states lack the financial cushion that federal social security funds can provide, the pension plans in those states "are more underfunded than in Social Security states." T. Leigh Anenson et al., *Reforming Public Pensions*, 33 YALE L. & POL'Y REV. 1, 10 (2014).

42. NATIONAL ASSOCIATION OF STATE RETIREMENT ADMINISTRATORS ("NASRA"), ISSUE BRIEF: STATE AND LOCAL GOVERNMENT SPENDING 4 (Mar. 2016), http://www.nasra.org/files/Issue%20Briefs/NASRACostsBrief.pdf [https://perma.cc/56KF-Y89Q].

States and municipalities may attempt to evade or restructure their pension obligations in numerous ways.[43] To appreciate the different strategies, one should recognize that pension benefits are often calculated according to formulas that are tied to age, credited service, and salary.[44] Some states have succeeded in revising their plans by distinguishing its parts. For example, they may take the position that base payments are protected benefits that are concretized at the moment when an employee accepts employment, whereas cost of living adjustments are subject to change or elimination.[45]

43. KEITH BRAINARD & ALEX BROWN, NAT'L ASS'N OF STATE RET. ADM'RS, SPOTLIGHT ON SIGNIFICANT REFORMS IN STATES, 1–76 (2016).

Leigh Anenson, Alex Slabaugh, and Karen Lahey provide an in-depth analysis of the varied approaches which may include: (i) raising the amount of employee contributions: (ii) raising the age required to draw retirement benefits, (iii) arguing that the debts of the pension funds are ultimately those of the funds not those of the city, state, or county government and, therefore, if there are any shortfalls that cannot be covered by the funds, retirees under the relevant fund would suffer the loss, not the taxpayers, (iv) reducing retirement benefits, inserting timed pauses, or eliminating annual cost of living adjustments, (v) redefining "benefit" to mean contingent (discretionary) future supplement to income rather than deferred compensation, (vi) changing the health insurance source to coverage under the Affordable Care Act, (vii) imposing surcharges on utilities such as telecommunications services, (viii) calling for a state constitutional convention to appeal provisions designed to protect the impairment of benefits, and (ix) approving municipal bankruptcy for cities that lack any alternative recourse. *See* Leigh Anenson, et al., *Reforming Public Pensions*, 33 YALE L. & POL'Y REV. 1, 11–14 (2014).

For legislative examples and judicial treatment of some of the proposals, *see e.g.*, S. 1922 98th Gen. Assemb., Reg. Sess. (Ill. 2014), http://www.ilga.gov/legislation/BillStatus.asp?DocNum=1922&GAID=12&DocTypeID=SB&LegId=73354&SessionID=85&GA=98; Joanna Bartlett, et al. v. Cameron, 316 P.3d 889, 891 (N.M. 2013) (holding that New Mexico's Constitution did not "grant[] Retirees a right to an annual cost-of-living adjustment to their retirement benefit, based on the COLA formula in effect on the date of their retirement, for the entirety of their retirement."). Regarding item (iii) above, Stephen Patton, Chicago's Corporation Counsel advanced this unsuccessful argument in connection with the City's defense of its 2014 plan, which was passed by the legislature but the struck down by the state supreme court, substantially changing two of the city's pension funds. *See* Hal Dardick, *Illinois Supreme Court Ruling Forces City to Find New Fix for 2 Pension Funds*, CHI. TRIB. (Mar. 24, 2016), http://www.chicagotribune.com/g00/news/local/politics/ct-chicago-pension-law-ruling-0325-20160323-story.html?i10c.referrer=https%3A%2F%2Fwww.google.com%2F. Moody Investors Service lent support to this position in the context of rendering its risk evaluations. In its May 2015 report, downgrading Chicago's bond rating to junk status Moody's commented that, "Chicago's ability and willingness to fund annuitant payments, should they be required of the city, is uncertain." *See generally* MOODY'S INVESTORS SERVICE, RATING ACTION: MOODY'S DOWNGRADES CHICAGO, IL TO BA1, AFFECTING $8.9B OF GO, SALES, AND MOTOR FUEL TAX DEBT; OUTLOOK NEGATIVE, https://www.moodys.com/research/Moodys-downgrades-Chicago-IL-to-Ba1-affecting-89B-of-GO—PR_325213.

44. Pozen & Khuruna, *supra* note 27, at 1–2. *See also* Smith v. Bd. of Tr. of Louisiana State Emp.s' Ret. Sys., 851 So. 2d 1100, 1107 (La. 2003) (discussing the vesting of pension rights and the components of the states' pension plans).

45. Bartlett, et al. v. Cameron, 316 P.3d 889, 896 (N.M. 2013) ("in the absence of any contradictory indication from our Legislature, any future cost-of-living-adjustment to a retirement benefit is merely a year-to-year expectation that, until paid, does not create a property right under the Constitution.").

Much can be learned from Illinois and its largest municipality, Chicago,[46] regarding the connections between state and local governance, constitutional protection of pension rights, and tenable strategies to avoid fiscal crisis. With unfunded pension deficits of approximately $111 billion,[47] Illinois is experiencing fiscal distress of historic proportions. Substantial financial difficulties plague Illinois' state pension system and the four pension funds controlled by Chicago.[48] Facing mounting pressure from creditors and credit rating agencies,[49] the Illinois General Assembly passed Public Act 098-0599[50] in 2014, which amended aspects of the state pension code for current participants.[51] Public Act 098-0599 was also the focus of the *In re Pension Reform* case, discussed in Parts III and IV.

Louisiana is suffering considerable pension challenges of its own.[52] According to one report, in 2013 the state's unfunded pension liability to-

46. Chicago with its estimated population 2,720,546 people in 2015 according to the Census figures, substantially impacts the economic welfare of the entire state. *Quick Facts, Chicago, Illinois*, U.S. CENSUS BUREAU (last visited Dec. 19, 2016, 1:45 PM), http://www.census.gov/quickfacts/table/PST045215/1714000 [https://perma.cc/8KP8-LS4X].

47. *See* Greg Hinz, *There's No Escape Illinois: It's Time to Pay for Those Pensions*, CRAIN'S CHI. BUS. (Oct. 1, 2016), http://www.chicagobusiness.com/article/20161001/ISSUE05/310019998?template=printart [https://perma.cc/M89F-MJ43].

48. *See also* THE PEW CHARITABLE TRUSTS: A WIDENING GAP IN CITIES, *supra* note 1 at 4, 14, 19, 21. (according 2009 figures, Chicago's pensions were only 52% funded and in 2010 they were 47% funded).

49. In 2014, Moody's Investor Service lowered Chicago's credit rating from A3 to Baa1. Moody's forewarned that the city's bonds were headed for a junk status rating. *See Moody's Downgrade: Chicago's Path Toward Junk* (Mar. 15, 2014), https://www.illinoispolicy.org/moodys-downgrade-chicagos-path-toward-junk/ [https://perma.cc/NK3S-59BS]. In May 2015, Moody Investor's issued a junk status rating for the city bonds. Everett Rosenfeld, *Moody's Downgrades Chicago Debt to 'Junk' with Negative Outlook*, CNBC (May 12, 2015), http://www.cnbc.com/2015/05/12/moodys-downgrades-chicago-debt-to-junk-with-negative-outlook.html [https://perma.cc/C3U7-VQYV].

50. 2014 Ill. Laws Pub. Act 98-599, http://www.ilga.gov/legislation/publicacts/98/098-0599.htm [https://perma.cc/7WK5-93PH].

51. Although the law was scheduled to take effect on June 1, 2014, it did not due to the numerous lawsuits that were filed challenging its validity. Chicago's mayor, Rahm Emmanuel, also has made several attempts to tackle the fiscal problems plaguing the municipality's pension funds. These attempts have been successfully challenged in court. *See* Mary J. Jones v. Municipal Employees' Annuity and Benefit Fund of Chicago, 2016 IL 119618, ¶61. Because the reasoning of the state supreme court regarding the city's funds follows that of the court's decision in the state pension funds case, this paper does not address the city fund decision in detail. While the case outcome is favorable for pensioners and one that this paper endorses, one unfortunate downside to the court's 2016 ruling striking down the mayor's plan is that it exacerbates the pension funding problem. Rather than the city paying the $90 million earmarked for the city pension funds into the funds, it is likely to be diverted elsewhere, until an alternative plan is approved. This is an absurd result. If the city has $90 million available for pension funds, it should invest the money accordingly, regardless of whether there is a modification plan in place. *See* Dardick, *supra* note 43 (discussing the negative aspects of the court's ruling).

52. *See* OWEN HAAGA ET AL., URBAN INST., THE STATE OF PUBLIC PENSION REFORM IN LOUISIANA 1 (June 2015), http://www.urban.org/sites/default/files/publication/54231/2000267-The-State-of-Public-Pension-Reform-in-Louisiana.pdf [https://perma.cc/ZN2K-F2R6]; THE PEW

taled $74.9 billion.[53] In contrast to Illinois, Louisiana's constitution-based pension rights have been formulated to afford the state significant flexibility for addressing its budget shortfalls. As discussed in Parts III and IV, there is often a tradeoff between structuring malleable plans that permit legislators and governing officials to make adjustments where necessary for sustainability and financial soundness and achieving plan integrity that addresses the protection of public employees in their retirement. For that reason, it is necessary to examine closely Louisiana's constitutional language for any cautionary tales it provides to current and future state and city employees and for lessons it can offer regarding good governance in the design and administration of pension systems.

Commentators on the financial condition of Ohio's pension funds offer conflicting assessments. Some reports opine that Ohio is experiencing staggering shortfalls[54] while others conclude that the state's pensions are solvent and relatively stable. [55] The discrepancy may be explained in part by the assumed level of return on pension investments. Ohio's relevance to this analysis is two-fold. First, because Ohio's constitution does not include provisions dedicated to protecting pension rights, instead relying upon a statutory scheme for the regulation and administration of its pensions, the

CHARITABLE TRUSTS: THE STATE PENSIONS FUNDING GAP, *supra* note 1, at 3. *See also* Will Sentell, *Report: Teacher Retirement Underfunded*, ADVOCATE (Dec. 17, 2012), http://www.theadvocate.com/baton_rouge/news/education/article_f1fe18fd-eca5-52c4-89a4-e0f6b8e6ee69.html [https://perma.cc/6E9H-BW2N].

53. As one reporter characterized it, "[f]or every dollar in retirement benefits owed to state employees, Louisiana has just 31 cents in the kitty." JR Ball, *Louisiana Can No Longer Hide from the Need to Reform Its State Retirement Systems*, TIMES-PICAYUNE (Sept. 5, 2013), http://www.nola.com/opinions/baton-rouge/index.ssf/2013/09/what_do_we_want_pension_reform.html [https://perma.cc/M2ZN-DSPG] (citing Cory Eucalitto, *State Budget Solutions, Promises Made, Promises Broken–The Betrayal of Pensioners and Taxpayers*, AM. LEGIS. EXCH. COUNCIL (Sept. 3, 2013), https://www.alec.org/article/promises-made-promises-broken-the-betrayal-of-pensioners-and-taxpayers/ [https://perma.cc/YK5Q-9SHK]). *See* Joe Luppino-Esposito, *Promises Made, Promises Broken 2014: Unfunded Liabilities Hit $4.7 Trillion*, AM. LEGIS. EXCH. COUNCIL (Nov. 12, 2014), https://www.alec.org/article/promises-made-promises-broken-2014-unfunded-liabilities-hit-4-7-trillion/ [https://perma.cc/RSB5-3XAU].

54. Maggie Thurber, *Ohio's unfunded pension liability more than $25K per resident*, OHIOWATCHDOG.ORG (Nov. 14, 2014) (citing to Luppino-Esposito, *supra* note 53), http://watchdog.org/183105/ohio-pension-liability/ [https://perma.cc/TH5K-VLXU]. Thurber writes that as of 2014, "Ohio's public pension plans have so much debt that paying it off today would cost each resident $25,080." *Id.* Novy-Marx and Rauh's 2008 assessment of Ohio's pension debt was equally sobering. They concluded that: "At its current level [i.e. 2008[of tax collection, Ohio would need to devote 8.75 years of tax revenue to pension funding simply to catch-up on already made promises." Novy-Marx & Rauh, *supra* note 18, at 197.

55. *See* THE PEW CHARITABLE TRUSTS: THE STATE PENSIONS FUNDING GAP, *supra* note 1, at 4. *See also* MORNINGSTAR, THE STATE OF STATE PENSION PLANS 2013: A DEEP DIVE INTO SURPLUSES AND SHORTFALLS 3 (2013),
http://images.mscomm.morningstar.com/Web/MorningstarInc/%7B43f240a0-4c8f-47b5-bc01-45cbc9e9d33b%7D_StateofStatePensionsReport2013.pdf [https://perma.cc/7ADM-D9CJ].

Ohio case study makes for a valuable contrast to states that establish pension rights in their constitutions. Second, because courts have considered, at times, a property-based approach in resolving cases concerning the pension rights of Ohio public employees, the state court decisions are useful for contemplating whether conceptions of property are useful for establishing and preserving pension rights.

For the discussion of Michigan's pensions, Detroit is the focal point. Detroit represents the extreme because of its Chapter 9 bankruptcy filing on July 18, 2013.[56] Having a municipality within the state of Michigan file for bankruptcy places significant financial pressure on the state. Detroit's filing is noteworthy because it is "the largest municipal bankruptcy filing in history in terms of debt."[57] At the time it declared bankruptcy, the city's debt level had reached a staggering $18 to $20 billion.[58] The bankruptcy was a culmination of the disastrous economic trajectory the city had been on for years.[59] The years prior to 2013 where characterized by the steady decline of Detroit's population, shrinking from a high of 1.8 million to 700,000.[60] The Detroit of 2013 represents how municipalities can go spectacularly wrong if they fail to develop responsible strategies for managing public pension debt and fail to establish effective plans of fiscal and social governance.

Detroit is also relevant to this analysis because it foregrounds a highly controversial issue: whether the federal government has a role in addressing the public pension crisis. *In re City of Detroit, Michigan,* sheds light on the legal limits of public pension rights. In that case, the United States Bankruptcy Court for the Eastern District of Michigan held that the state constitution did not prohibit bankruptcy courts from modifying the municipality's public pension obligations in the context of federal bankruptcy proceedings.[61] While states are not permitted to file for bankruptcy,[62] mu-

56. *City of Detroit Bankruptcy Filing*, UNITED STATES BANKRUPTCY COURT, EASTERN DISTRICT OF MICHIGAN (July 18, 2013), http://www.mieb.uscourts.gov/news/city-detroit-bankruptcy-filing [https://perma.cc/YDE8-E4HN].

57. Monica Davey & Mary W. Walsh, *Billions in Debt, Detroit Tumbles Into Insolvency*, N.Y. TIMES (July 18, 2013), http://www.nytimes.com/2013/07/19/us/detroit-files-for-bankruptcy.html?pagewanted=all&_r=0 [https://perma.cc/R9PV-ZWLD].

58. *Id. See* Pete Saunders, *Detroit After Bankruptcy*, FORBES (Apr. 24, 2016), http://www.forbes.com/sites/petesaunders1/2016/04/24/detroit-after-bankruptcy/#6b50e54e38e4.

59. Amy Padnani, *Anatomy of Detroit's Decline*, N.Y. TIMES (Dec. 8, 2013).

60. Davey & Walsh, *Billions in Debt, Detroit Tumbles into Insolvency*, *supra* note 57.

61. The bankruptcy court reasoned that:

> the State of Michigan cannot legally provide for the adjustment of the pension debts of the city of Detroit. This is a direct result of the prohibition against the State of Michigan impairing contracts in both the United States Constitution and the Michigan Constitution, as well as the prohibition against impairing the contractual obligations relating to accrued pension bene-

nicipalities, with the permission of their state can.[63] When a state authorizes a municipality to take this step, it impacts the overall financial condition of the state.

III. THE ARTICULATION OF PENSION RIGHTS IN STATE CONSTITUTIONS AND STATUTES

This section examines certain constitutions and statutes to understand how states have articulated pension rights for public employees. Provisions regarding substantive pension benefits, the funding of plans, and the administration of the plan are contained in the various pension statutes and codes of each state.[64] Drawing upon their state constitutions or statutes, public employees have presented arguments sounding in the law of contracts, property, and due process.[65] Illinois is an appropriate beginning point for this discussion because the state is facing formidable budget challenges due in large measure to its pension deficits, but also because of sections within the state constitution related to public pensions. The most significant of these constitutional provisions is known as the Pension Protection Clause. The clause, which is contained in Article XIII, § 5, did nothing less than create a new right.[66] In fact, this is exactly how the Illinois Supreme Court in its 2015 decision, *In re Pension Reform Litigation*, characterized it.[67] The pension protection clause provides that "[m]embership 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

> fits in the Michigan Constitution. The federal bankruptcy court, however, is not so constrained.

In re City of Detroit, Michigan, 504 B.R. 90, 150 (E.D. Mich. 2013).

62. States are precluded from filing for bankruptcy by the federal bankruptcy code, 11 U.S.C.A. §109, and the Contracts Clause of the United States Constitution, U.S. CONST. art. I, §10, cl. 1.

63. THE PEW CHARITABLE TRUSTS, *supra* note 40, at 12.

64. *See e.g.*, 40 ILL COMP. STAT. ANN. 5/1 et seq. (Westlaw through Pub. Act 99-930 of 2016 Reg. Sess.); MICH. COMP. LAWS ANN. §38.551 et seq. (Westlaw through Pub. Act 2016 No. 563 of 2016 Reg. Sess.) (Firefighters and Police Officers Retirement Act); LA. STAT. ANN. § 11:1 et seq. (Westlaw through 2016 First Extraordinary, Reg., and Second Extraordinary Sess.); OHIO REV. CODE ANN. § 3307.01 et seq. (Westlaw through 2015–2016 Leg. Sess.) (State Teacher's Retirement System).

65. *See In re* Pension Reform Litigation, 2015 IL 118585, ¶62; Kanerva v. Weems, 2014 IL 115811, ¶22; Smith v. Bd. of Tr. of Louisiana State Emp.s' Ret. Sys., 851 So. 2d 1100, 1105–06 (La. 2003); In re City of Detroit, Michigan, 504 B.R. 97, 137 (E.D. Mich. 2013);

66. The Illinois Supreme Court concluded with respect to the Article XIII, section 5 that "[t]hose provisions not only created a new right of constitutional dimension, conferring enforceable contractual status on the benefits of membership in public retirement systems, they also defined the scope of protections afforded such benefits." *In re* Pension Reform Litigation, 2015 IL 118585, ¶¶70–71.

67. *Id.*

shall not be diminished or impaired."[68] The Illinois legislature approved adding the aforementioned language to the 1970 constitution by a vote of fifty-seven to thirty-six.[69] The goal was to insulate Illinois pensions from the political maneuvering that made them vulnerable to modification without obtaining the consent of the affected groups (i.e. public school teachers, firefighters, police officers, and other government employees).

Prior to the adoption of the law, Illinois had received repeated warnings from the Securities Exchange Commission, the Illinois Public Employees Pension Laws Commission,[70] financial consultants, crediting agencies, and creditors that its practices regarding the chronic underfunding of its pensions were reckless and unsound.[71] For years, Illinois politicians refused to heed the advice recommending that they take proper action and make the necessary appropriations to fund the pensions.[72] In essence, government officials were sending the message that, if the pensions needed to be sacrificed, they would sacrifice them.[73] So, when the delegates met for the 1970 constitutional convention, they designed a provision to protect public employees from the political games that consistently threatened their retirement interests. Illinois based its pension clause on similar language in New York's 1938 constitution.[74] Not only did the state supporters of the provision seek to protect pensioners, they also sought to motivate the legislature to address the pension fund shortfalls in a timely manner. Despite the latter objective, the Pension Clause has thus far failed to incentivize the state to make the yearly appropriations necessary to close the gap between pension assets and liabilities.[75] Now—some forty-six years later—Illinois will have to develop multiple, creative solutions to ameliorate the problem.

There are three key features to highlight about Illinois' pension clause. First, it is a separate provision dedicated towards the protection of pension rights. The significance of having a separate clause for this purpose will be

68. IL CONST. art. XIII, § 5.

69. Bob Sector & Rick Pearson, *Pension Debate at 1970 Convention Echoes in Today's Crisis*, CHI. TRIB. (Sept. 22, 2013), http://www.chicagotribune.com/news/ct-met-public-pensions-1970-20130923-story.html.

70. *In re* Pension Reform Litigation, 2015 IL 11858, ¶¶11–14.

71. *Id*. *See* Sector & Pearson, *supra* note 69.

72. The conventional recommendation is that when money has been set aside through investments to cover at least eighty percent of the outstanding pensions obligations, the funding is at a financially sound level. *See* Christensen & Moore, *supra* note 19, at 35 (noting the industry standard but questioning its soundness).

73. *See* Ann Lousin, *The 1970 Illinois Constitution: Has it Made a Difference?*, 8 N. ILL. U. L. REV. 571,
605–06 (1988) (discussing the origins of the pension clause and cases concerning it).

74. Sector and Pearson, *supra* note 69.

75. *Id.*

apparent in the analysis comparing the laws of Louisiana, Ohio, and Michigan in Part IV. Second, Illinois' provision enshrined a new right in that it recognized a contractual relationship between the government[76] and public employees that may be mutually enforced.[77] Prior to this, pensions were treated as gratuities.[78] Consequently, the state and related government entities had the power to modify, revoke, and deny benefits at their discretion.[79] Establishing the existence of a contractual right immediately confers advantages and places limitations on the bound parties. Third, the declaration that pension benefits may not be "diminished or impaired" preserves the contractual bargain that was struck between public employer and employee at the time the employee was hired. The fact that there is a provision combining all these elements gives the clause its strength.

The Illinois Constitution's Contracts Clause is another provision that public employees have relied upon to guard against modifications to their plans. The clause is an ex post facto prohibition like the one contained in the federal constitution.[80] Illinois' Contracts Clause provides that "No ex post facto law, or law impairing contracts or making an irrevocable grant of special privileges or immunities, shall be passed."[81] In past cases, state employees within Illinois' system have framed their claims in terms of the state's contracts clause to argue that any attempts by the state to alter the base benefits in their plans (measured at the time they entered employment) or that are designed to decrease or eliminate the cost of living adjustments or health coverage associated with their benefits packages, infringed upon their contractual rights.[82] Illinois pensioners have also resorted to the state constitution's takings clause to argue that any change to benefits plans would constitute an unlawful taking without just compensation. The takings clause provides that "[p]rivate property shall not be taken or damaged for public use without just compensation as provided by law. Such compensation shall be determined by a jury as provided by law."[83] For the reasons discussed in Part IV, out of the three main arguments grounded in the

76. The term government is meant in the inclusive sense of all its associated entities.

77. *In re* Pension Reform Litigation, 2015 IL 118585, ¶72.

78. Kanerva v. Weems, 2014 IL 115811, ¶45.

79. *Id.* ("Where an employee's participation in a pension plan was mandatory, the rights created in the relationship were considered to be in the nature of a gratuity that could be revoked at will.").

80. Article I, Section 10, Clause 1 of the United States Constitution provides in relevant part: that "No state shall . . . pass any Bill of Attainder, ex post facto Law, or Law impairing or Law impairing the Obligations of Contracts . . . ." U.S. CONST. art. I, §10, cl. 1.

81. ILL. CONST. art. I, § 16.

82. *See In re* Pension Reform Litigation, 2015 IL 118585, ¶38–40; *Kanerva*, 2014 IL 115811, ¶22 (relying upon the state's contracts clause).

83. ILL. CONST. art. I, § 15.

state constitution, Illinois courts have rendered decisions in favor of public pensioners based upon the Pension Protection Clause.

Alongside Illinois, Louisiana shares a special constitutional provision dedicated to preserving pension rights. Its language, found in Article X, § 29(E)(5), provides in relevant part:

> The accrued benefits of members of any state or statewide retirement system shall not be diminished or impaired. Future benefit provisions of the state and statewide public retirement systems shall only be altered by legislative enactment.[84]

Louisiana's legislature added this provision in 1987, relatively late compared to the adoption of Illinois' and Michigan's clauses. While the Louisiana Supreme Court recognized that the pension clause grants some protection, public workers whose benefits have been threatened have not met with the same success as participants in Illinois in preventing the erosion of their plan benefits.[85] The difference in treatment, as discussed in Part IV, is due in large measure to how the right was constructed.

Two other relevant sections under Article X that pertain to pension rights are sections 29(A)[86] and 29(B). Both establish that membership in Louisiana's retirement system constitutes a contractual relationship.[87] For example, Section 29(B) recognizes that membership in the state retirement systems "shall be a contractual relationship between employee and employer" and that "the state shall guarantee benefits payable to a member . . . or retiree or to his lawful beneficiary."[88]

Like the United States Constitution and that of Illinois', Louisiana's constitution contains a contracts clause prohibiting the adoption of an "ex post facto law, or law impairing the obligation of contracts."[89] Despite its proscriptions, arguments that this provision precludes changes to retirement benefits packages once the employee commences work have been unsuccessful.[90] In connection with asserting property-based arguments, pensioners in Louisiana have relied upon the constitution's due process provision to argue that proposed adjustments to their benefits violate the restriction prohibiting states from depriving individuals of their property "except by due process of law."[91] Actuarially sound mandates are another avenue by

84. LA. CONST. art. X, § 29(E)(5) ("added pursuant to Act 947 of the 1987 Regular Session").

85. *See e.g.*, Smith v. Bd. of Tr. of Louisiana State Emp.s' Ret. Sys., 851 So.2d 1100, 1111 (La. 2003).

86. Section 29(A) applies to public school teachers. LA. CONST. art. X, § 29(A).

87. *Id.* § 29.

88. *Id.* § 29(B).

89. *Id.* art. I, § 23.

90. *See e.g.*, Smith v. Bd. of Tr. of Louisiana State Emp.s' Ret. Sys., 851 So. 2d 1100, 1108–10.

91. LA. CONST. art. I, § 2.

which Louisiana has sought to constitutionally protect pensions.[92] The logic informing such directives is that if pension funds are fiscally sound, then governments will be able to pay retirement benefits as they become due. This is one interpretation of actuarial directives. Another view is that actuarially sound provisions are not protective of pension rights, but instead render them more vulnerable because this type of language places pressure on legislatures to revise pension plans to meet whatever requirements are imposed.

In contrast to Illinois, Louisiana, and Michigan, Ohio's constitution does not contain an express provision dedicated to the protection of public pension rights. Rather, statutory law governs the state's pensions.[93] In 2015, Ohio had eight public pensions; seven are administered by the state, and one is under local control.[94] Some of the significant rulings regarding Ohio's pensions have concerned the State Teachers Retirement System ("STRS").[95] This paper analyzes the Ohio Supreme Court's interpretation of key sections of STRS statutes to gain a sense of whether they offer plan participants any protection from subsequent benefits changes. The relevant statutory provisions for STRS are contained in Chapter 3307 of Ohio's Revised Code.[96] For purposes of this discussion, the essential statutory provisions are the STRS vesting rights statute,[97] and R.C. § 3307.03, which establishes that retirement funds are "statutory benefits."[98]

92. Louisiana constitution's Article X, §29(E) requires that "the actuarial soundness of state and statewide retirement systems shall be attained and maintained and the legislature shall establish by law, for each state or statewide retirement system, the particular method of actuarial valuation to be employed." LA. CONST. art. X, § 29(E).

93. *See* State ex rel. Horvath v. State Teachers Retirement Board, 697 N.E.2d 644, 647 (Ohio 2007) ("Public school teachers do not possess contract rights in any State Teachers Retirement System benefit unless and until the benefit vests by operation of R.C. 3307.711"). *See also* Herrick v. Lindley, 391 N.E.2d 729, 732–33 (Ohio 1979) ("retirees have a vested right to receive a retirement allowance or similar benefit at the rate fixed by law when such benefit was conferred.").

94. *State and Locally-Administered Defined Benefit Pension Systems – All Data by State and Level of Government: 2015*, U.S. CENSUS BUREAU, https://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?src=bkmk [https://perma.cc/J4D7-ZYMF] (last visited Feb. 12, 2017).

95. *Horvath*, 697 N.E.2d 644; *Herrick*, 391 N.E.2d 729.

96. OHIO REV. CODE ANN. § 3307 et seq. (Westlaw through 2015–2016 Leg. Sess.) Individuals who become members of STRS are permitted to choose whether to participate in the defined benefit plan or the defined contribution plan. OHIO REV. CODE ANN. § 3307.25 (Westlaw through 2015–2016 Leg. Sess.) This discussion is concerned with the defined benefit plan.

97. OHIO REV. CODE ANN. § 3307.711 (1955). The *Horvath* court concluded that: "By its terms R.C. 3307.711 vests a right to a retirement allowance, annuity, or pension at the time that benefit is granted by the STRB at the rate fixed by law when the benefit is conferred." 697 N.E.2d at 654.

98. *See Horvath*, 697 N.E.2d at 652 ("Grants made from STRS funds, including refunds drawn from the teachers' savings fund pursuant to R.C. 3307.48(B) and 3307.46, constitute statutory benefits.") (citing OHIO REV. CODE ANN. § 3307.03). § 3307.03 provides in relevant part:

When public employees in Ohio have sought constitutional protection from changes in their pension plans, they have relied upon the takings[99] and contracts clauses.[100] The Supreme Court of Ohio's treatment of a public pensions takings claim in the *Horvath* case offers valuable insight concerning the strength of this argument and the analysis that courts are likely to apply. Regarding Ohio's contracts clause, the provision affords scant protection especially in view of the state's statutory scheme. Ohio's decision not to incorporate constitutional language dedicated to carving out and preserving pension rights, translates into substantive differences regarding the status of their pensions for public sector workers.

Michigan, like Illinois and Louisiana, has a special constitutional provision, which defines pension rights. Article IX, § 24 of Michigan's constitution provides:

> 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 thereby. Financial benefits arising on account of service rendered in each fiscal year shall be funded during that year and such funding shall not be used for financing unfunded accrued liabilities.[101]

This provision along with Michigan's Contracts Clause[102] have been invoked most recently in the context of Detroit's monumental municipal bankruptcy filing in 2013. For the reasons discussed below, the structuring of this clause renders pension benefits vulnerable to certain actions of the state or municipality in addressing fiscal matters. Nonetheless, it is better for plan participants to have a special clause devoted to the recognition and

A state teachers' retirement system is hereby established for the teachers of the public schools of the state which includes the several funds created and placed under the management of a state teachers retirement board for the payment of retirement allowances and other benefits under Chapter 3307 of the Revised Code . . . All of its business shall be transacted, and all of its funds invested, all warrants for money drawn and payments made, and all of its cash, securities, and other property shall be held in the name of the board or in the name of its nominee . . . .

Id.

99. OH. CONST. art. I, §19.

100. The Contracts Clause is contained in Article II Section 28 of the Ohio Constitution. The clause provides:

The general assembly shall have no power to pass retroactive laws, or laws impairing the obligation of contract; but may by general laws, authorize courts to carry into effect, upon such terms as shall be just and equitable, the manifest intention of parties, officers by curing omissions, defects, and errors, in instruments and proceedings, arising out of conformity with the laws of this state.

OH. CONST. art. II, §28.

101. Michigan adopted this provision as part of the state's 1963 Constitution. MI. CONST. art. IX, §24.

102. MI. CONST. art. I, §10 ("No bill of attainder, ex post facto law or law impairing the obligation of contract shall be enacted.").

preservation of their rights than not. Bankruptcy, however, presents particular challenges to this provision's efficacy in guarding pension rights from ex post facto modifications.

IV. "FOR THE GOOD OF PEOPLE"—ANALYSIS OF STATUTORY AND CONSTITUTIONALLY-GROUNDED LEGAL ARGUMENTS TO PRESERVE AND CHALLENGE PENSION RIGHTS

This section considers how the formulation of rights, the vehicle through which they are stated, and judicial interpretation translate into significant differences concerning the power of public workers to insulate their retirement benefits from economic and political shifts. It also further explicates how public pension obligations relate to states and cities in crisis. While some jurisdictions may be drastically overstating the proportions of their pension crisis,[103] this paper shares Jack Beermann's assessment that there is ample evidence to support the conclusion that there are serious fiscal issues confronting many regions across the nation.[104] Therefore, pension reform is warranted. However, unlike some scholars and policy officials who are pressing for revisions that will negatively impact current public employees and retirees by contracting their benefits, with one important exception, the recommendations for reform advanced herein, are prospective in nature. The exception concerns the recommendation, that where constitutional pension protections are lacking, legislatures should adopt provisions to shore up the rights of pension-holders in the interests of long-term governmental stability. The coverage that the new amendment provides should pertain to current pensioners and new employees. Examining the pension laws of various states from the vantage point of public workers is useful for identifying approaches that should prove beneficial in the future design of pension plans and for managing the present crisis.

A. The Sovereign's Police Powers and Distinctions Between Pension Protection Clauses and Contracts Clauses in State Constitutions

The primary constitutional source of protection for public pensions in Illinois is the Pension Protection Clause. The court's ruling in *In re Pension Reform* reinforced its effectiveness in guarding pension rights. Its powerful

103. *See* Patrick Yeagle, *The Manufactured Crisis over Illinois Pensions*, ILL. TIMES (Apr. 25, 2013), http://illinoistimes.com/article-11300-the-manufactured-crisis-over-illinois-pensions.html [https://perma.cc/6FYT-DTNK]. *See also* Saqib Bhatti and Carrie Sloan, OUR KIND OF TOWN, *supra* note .

104. Jack Beermann, *The Public Pension Crisis*, 70 WASH. & LEE L. REV. 3, 10–16 (2013).

effect could not even be overcome by the presumption of validity that courts normally extend to legislative statutes.[105] At issue in *In re Pension Reform* was the validity of Public Act 98-599, a new law that modified the Illinois Pension Code[106] by revising the benefits to which certain retirement system members were entitled.[107] The key contentious aspects of the law involved changes:

> which would reduce the retirement annuities of individuals entitled to Tier 1 benefits by raising the age at which members under the age of 46 are eligible to begin receiving their retirement annuities, capping the maximum salary that may be considered when calculating the amount of member's retirement annuity, abolishing the existing fixed 3% annual annuity increases, eliminating at least one and up to five annual annuity increases under the new formula, and altering how the base annuity amount is determined for purposes of the 'money purchase' formula.[108]

There was a lot at stake in this case. Even though there were other strategies to address the state's pension deficits and mounting pension obligations, government officials proposed a solution that solely burdened retirement plan participants.[109]

105. The Illinois Supreme Court reasoned:

> While we presume statutes to be constitutional and must construe enactments by the legislature so as to uphold their validity whenever it is reasonably proper to do so [], there is simply no way that the annuity reduction provisions in Public Act 98-599 can be reconciled with the rights and protections established by the people of Illinois when they ratified the Illinois Constitution of 1970 and its pension protection clause . . . **The General Assembly overstepped the scope of its legislative power. The court is therefore obligated to declare those provisions invalid.**

In re Pension Reform Litigation, 2015 IL 118585, ¶47 (citations omitted) (emphasis added).

106. Illinois Pension Code, 40 ILL. COMP. STAT. ANN. 5/1-101 et seq. (West 2012).

107. *In re* Pension Reform Litigation, 2015 IL 118585, ¶1.

108. *Id.* ¶ 34.

109. The court in *In re* Pension Reform Litigation took note of the exchange between Illinois senators' discussions that made it apparent that downsizing pension obligations was the quick fix to the debt problem. It is worth highlighting part of the exchange, in which Senator Hutchinson and Senator Raoul, respectively stated:

SENATOR HUTCHINGSON:

> Would another alternative be the proposal that the Center for Tax and Budget Accountability outlined before the conference committee, which would have re-amortized the current unfunded liabilities to a new gradual [level] dollar payment schedule to achieve well over eighty percent by 2059?

SENATOR RAOUL:

> Yes. So that - that and many other things could have been possible alternatives.

SENATOR HUTCHINGSON:

The Illinois Supreme Court's holding that Article XIII, § 5 confers protection on a public employee's retirement benefits at the commencement of his employment relationship, rather than when he retires,[110] and that his interest in the retirement benefits attaches immediately,[111] was a coup for Illinois' public-sector workers. The clause explicitly recognizes an enforceable contractual relationship.[112] For labor union members and other government employees, the ruling was particularly gratifying given their view that, "'[p]oliticians caused the pension debt by failing to set aside adequate contributions, in effect borrowing from future retirees to avoid raising revenue or cutting spending instead.'"[113] The decision signals to the legislature and other state government officials that they will not be permitted to manipulate pensions to balance the budget. The broad sweeping language of Illinois' pension clause, which encompasses members "in any pension or retirement System of the State, any unit of local government or school district, or any agency or instrumentality thereof,"[114] confers widespread protection.

Illinois' protection coverage for benefits is also broad in the sense of what is included as a "benefit," as the court's interpretation of that same constitutional pension provision in an earlier case made clear. In *Kanerva v. Weems*,[115] Illinois' high court concluded that it doesn't matter that the type of benefit at issue may be subject to a different calculation from other benefits. Instead, it is the "status" that is decisive. If the benefit "is derived

> [The last sentence of the fourth paragraph of the report contains the phrase] that the legislation is 'minimizing the impact on current and retired State employees'. So by using 'minimizing', does that mean that the legislation is somehow the least restrictive means available to us?

SENATOR RAOUL:

> Yeah, I—you know—I don't know what the least restrictive means are. I—I think what we're doing just reflects what the political climate is. Again, I've—I've—I've said, time and again, that we've been cemented in a stalemate, and I, for my part, don't want to see the State sink as a result of that stalemate. So, it may not be the least restrictive means, but the political climate, I believe, allows for us to—to take the step that we're□we're hopefully now taking.

Id. ¶ 34 (quoting 98th Ill. Gen. Assembly, Senate Proceedings, Dec. 3, 2013, at 41–46 (statements of Senators Hutchinson and Raoul)).

110. *Id.* ¶ 45.

111. *Id.* ¶ 34.

112. The Pension Clause declares, "Membership in any pension or retirement system of the State . . . shall be *an enforceable contractual relationship* . . . ." *Id.* (emphasis added).

113. Dardick, *supra* note 51 (quoting a representative of the American Federation of State, County and Municipal Employees Council 31, the Chicago Teachers Union, the Illinois Nurses Association, and Teamsters Local 700).

114. ILL. CONST. art. 13, §5.

115. 2014 IL 115811.

from membership in one of the State's public pension systems . . . it is protected."[116] This means that not only are calculations based upon salary shielded under the pension clause's umbrella, but so are cost of living adjustments and health insurance. Often, when policymakers target the aforementioned benefits for cuts, they discuss the items as though they are merely supplemental; meaning that, they are not essential to the quality of life and maintenance of retirees. This mischaracterization is far from the truth. The failure to cast a wide, inclusive net when using the term "benefits" could mean that the fixed income savings of retirees are consumed by inflation or astronomical health care costs. If COLAs and health care were part of the original compensation offered at the time of hiring, then government officials should not be allowed to excise these items from the paid benefits retirees receive. The *Illinois Pension Reform* case supports this logic.

As a follow-up to arguments couched in the Pension Protection Clause, members of the plans often resort to the contracts clauses in their state's constitution, to assert that the legislature is forbidden to adopt ex post facto laws that impair contracts. While clauses of this type afford some protection, without more, they often prove inadequate to stave off legislative attacks on pension rights. The reasons are several-fold. First, the contracts clauses do not expressly recognize the relationship between the government and public employees as a contractual arrangement. To bestow the rights, privileges, and mutual obligations that a contract gives rise to, there needs to be a separate constitutional provision or statute recognizing that a contract exists. Preferably, such provision should also specify when the contract is formed. Second, contracts protected solely by the contracts clause are, arguably, more vulnerable[117] to the state's exercise of its police powers.[118]

In re Pension Reform illustrates the difference that having a special provision dedicated to pension protection can make. The case supports the

116. *Id.* ¶ 54.

117. The Illinois supreme court and the bankruptcy court in the *In re* Detroit, Michigan case have expressed different opinions on whether the respective state's pension protection clauses afford more protection than the contracts clauses. Cf. *In re* Pension Reform Litigation, 2015 IL 118585 ¶¶37–38 (recognizing that contracts protected solely under the contracts clause may be overcome by the sovereign police powers in some instances but noting that where the impairment is substantial it is subject to more intense scrutiny and will likely be invalidated).

118. In comparing the Contracts Clause in the United States Constitution to the one in Louisiana's constitution, Louisiana's State Supreme Court concluded that "[a]lthough the language of each clause is facially absolute, its prohibition must be accommodated to the inherent police power of the state to safeguard the vital interests of its people." Segura v. Frank, 630 So.2d 714, 728 (La. 1994) (citations omitted).

proposition that pension contracts protected by special clauses structured like Illinois' are not subject to the state's sovereign police powers[119] whereas contracts clauses are susceptible to such state action.

There, the state asserted its right to exercise its sovereign police powers as a defense to its constitution's pension clause.[120] The state argued that even if the pension clause applies, it doesn't grant any more protection than the contracts clause in times of crisis.[121] Rather than being absolute, the pension clause is subject to the state's police powers just as contracts under the contracts clause were fettered.[122] Consequently, when facing extreme emergencies, the state can exercise its police powers and infringe upon pension rights for the good of the state (and its cities) to protect the safety, health, welfare, and morals of the populace.[123]

The court's holding is remarkable because police powers arguments regarding the prevailing interest in the well-being of populace can be seductive. For the court not to succumb to them and, instead, uphold the pensioners' interests is significant. The decision addressed the power imbalance between public employers and employees in the area of compensation. Not only did it reflect the court's adherence to the objectives of the pension clause—as expressed by the delegates to the Illinois' 1970 constitutional convention to above all else preserve pensioners' benefits[124]—it also is a moment in which the Court discerned the "voice" of the

119. *Id.* at 24. The court reasoned that:

> Given the history of article XIII, section 5, and the language that was ultimately adopted, we therefore have no possible basis for interpreting the provision to mean that its protections can be overridden if the General Assembly deems it appropriate, as it sometimes can be under the contracts clause.

Id.

120. *In re* Pension Reform Litigation, 2015 IL 11858532, ¶¶72–75.

121. Brief for Defendant-Appellants at *21–27, *In re* Pension Reform Litigation, cite for brief 2015 WL 1378612 (2015).

122. Essentially, the government argued that there was nothing in the pension clause to suggest that it would not be subject to the reserved sovereign police powers of the state. Brief for Defendant-Appellants, *supra* note 121, at *16.

123. *In re* Pension Reform Litigation, 2015 IL 11858532, ¶¶33–37, ¶¶47–52, ¶¶60–65. *See* Brief for Defendant-Appellants, *supra* note 121, at *4.

124. The court was clearly influenced by the comments of convention delegates as is evident from its citations to the Record of the Proceedings for the constitutional convention:

> Subsequent comments by other delegates reaffirmed that the provision was designed to confer contractual protection on the benefits of membership in public retirement systems and afford beneficiaries, pensioners or their dependents 'a basic protection against abolishing their rights completely or changing the terms of their rights after they have embarked upon the employment to lessen them.'

people and viewed it as being at odds with the legislature's claims to represent the public interest.[125] The state argued that the fiscal pressures of the Great Recession had devastated the financial condition of the state.[126] Significant decreases in the value of the investments of the pension funds made it challenging, if not impossible, for Illinois to both meet its debt obligations to creditors in a timely manner and to provide services such as public education, police and fire protection, waste collection, and infrastructure maintenance.[127] Reducing the outstanding pension liabilities was one way to manage the debt, allowing for the savings to be redirected to critical services. The state's arguments invited the court to reweigh whether public employees deserved the compensation they were promised against a host of hypothetical disasters such as, closing public "prisons and schools" or not being able to "purchase and distribute vaccines" in the wake of a health crisis.[128]

The state, however, was presenting the court with a false dilemma. Rather than treating pension funds as discretionary assets that may be reallocated towards dire services, they should be viewed as deferred compensation. If the government wasn't comfortable with the level of compensation offered to public employees, it should have made ex-ante changes to the benefits packages. The plausibility of some of the predictions on the state's list of horribles (*e.g.*, further reductions in credit ratings) should not change the fact that the government has pension obligations that it must satisfy. The state's doomsday list does not justify placing the burden more heavily on public employees. Instead, local and state governments should rely upon more equitable burden-sharing mechanisms, such as increasing individual income taxes or imposing taxes on corporations. While these solutions also have potential downsides with respect to their impact on the ability of ju-

In re Pension Reform Litigation, 2015 IL 118585, ¶¶15–18 (citing and quoting Kanerva v. Weems, 2014 IL 115811 at ¶46, quoting 4 Record of Proceedings 2925 statements of Delegate Kinney) (internal quotation marks omitted).

125. The Court reasoned:

> "The people of Illinois give voice to their sovereign authority through the Illinois Constitution . . . Through [the Pension Protection Clause] the people of Illinois yielded none of their sovereign authority. They simply withheld an important part of it from the legislature, because they believed, based on historical experience, that when it came to retirement benefits for public employees, the legislature could not be trusted with more."

In re Pension Reform Litigation, 2015 IL 118585, ¶¶ 75–82.

126. Brief for Defendant-Appellants, *supra* note 121 at *6–8. *See In re* Pension Reform Litigation, 2015 IL 118585, ¶¶ 58–59.

127. Brief for Defendant-Appellants, *supra* note 121, *6–7, *12–13.

128. Brief for Defendant-Appellants, *supra* note 121, at *20.

risdictions to attract and retain companies and human capital,[129] arguably, they are likely to result in less political and economic costs than a municipality or state reneging on the payment of its pension obligations.

If the court had accepted the government's argument, the contested law (i.e. Public Act 98-599) would have been subjected to a rational basis standard of review.[130] In accordance with this standard, if the state could show that the law was "reasonable and necessary to serve an important public purpose" it would survive the court's scrutiny.[131] This deferential standard is a very low threshold to satisfy. Adopting this level of judicial review would render, as the court concluded, the Pension Protection Clause ineffectual and meaningless.[132] The court's allowance of the police power as a defense would be akin to declaring that public employees have pension benefits until the state decides they do not. In other words, it would contravene the main goal of the Pension Protection Clause, which was to change the status of pension benefits from gratuities into enforceable contractual obligations.

The Illinois Supreme Court distinguished between the Pension Protection Clause and the Contracts Clause,[133] noting the differences in the former's import and effect.[134] In so ruling, it rejected the rational basis test.

129. Pozen & Khuruna, *supra* note 27, at 8 (discussing negative consequences of raising taxes to cover pension debt). *See generally* Anderson, *supra* note 15 (identifying some of the consequences associated with governments' fiscal decisions to impose higher taxes to address debt obligations).

130. *In re* Pension Reform Litigation, 2015 IL 118585, ¶62 ("impairment of a contract may survive strict scrutiny under the contracts clause if reasonable and necessary to serve an important public purpose . . . .").

131. *Id.*

132. *Id.* ¶ 75.

133. The court concluded that the state could not "resort to the contracts clause to support its police powers argument" that pension contracts, like other contracts, can be modified in times of emergency to serve the public safety, health, general welfare, and morals. *Id.* ¶ 69.

134. The court reasoned:

> The contracts clause had antecedents in the very first Illinois Constitution and in the Constitution of the United States. When the time came to address the protection for public pensions, the drafters of the 1970 Constitution therefore presumably knew of the substantial body of case law involving that clause, including the case law holding that, when warranted, the protections afforded contracts could be modified through the exercise of the state's police powers. That, however is not the standard they chose with respect to the benefits of membership in public pension systems . . . When it came time to address the rights conferred by membership in public pension systems, however, the drafters included no similar reservation of authority . . . That proposal [] was rejected in favor of the separate, more specific provision of article XIII, section 5.

Id. ¶ 70. One interesting aside is the court's observation that prior to the adoption of the pension clause, when the court assessed the constitutional validity of legislation that impinged on public pension rights under the rational basis scrutiny standard utilized for matters falling under the contracts clause, it struck down such legislation. *Id.* ¶ 61 ("When the legislation has been directed at reducing pension benefits of State employees, this court has expressly held that it is 'not defensible as a reasonable exercise of the

Drawing upon United States Supreme Court precedent, the court proposed an alternative scheme to evaluate the constitutional validity of the pension reform legislation.[135] Under this new framework, the "necessity" element was the focal point. Where the state seeks to modify a contract, concerning its financial interest, to which it is a party and the state argues that the contested legal measure is reasonable and necessary for the good of the public as whole, the court must examine: 1) Whether the "effects" of the constitutional provisions the new law overrides "were unforeseen and unintended by the legislature when initially adopted" and 2) "Whether the state could achieve its purposes through less drastic measures."[136] Based upon this analysis, the court invalidated the state's modification plan.

The test enabled the court to address one of its primary concerns regarding equity in contractual relations. In this instance, the state was seeking to unilaterally modify a contract that it was a party to for its own advantage.[137] The state's actions exemplify the problem with treating pension benefits as gratuities rather than deferred compensation. The bargaining power between parties is unequal if governments are permitted to disregard the terms it presented to job candidates as enticements for them to accept the offer of employment. One way to restore equity in the employer-employee relationship and to discipline governments in terms of their expenditures is to make it more difficult for them to adopt the expedient choice of shortchanging the retirement benefits of public employees. This can be done through the state constitution[138] and, to some extent, through the judiciary. The goal is to motivate government officials and

State's police powers' and declared it invalid under the contracts clause, as well as for other reasons.") (citations omitted). The court's actions suggest that it recognized that pensions should have a special status even before sufficient political forces were galvanized to adopt constitutional protection for them.

135. *Id.* ¶ 65.

136. *Id.*

137. The Illinois court reasoned that:

> Moreover, the United States Supreme Court has held that particular scrutiny of legislative action is warranted when, as here, a state seeks to impair a contract to which it is itself a party and its interests in avoiding the contract or changing its terms is financial . . . In addition, because the state's self-interest is at stake whenever it seeks to modify its own financial obligations, the United States Supreme Court has made clear that it is not appropriate to give the state's legislature the same deference it would otherwise be afforded with regard to whether the impairment is reasonable and necessary to serve an important public purpose.

Id. ¶¶63–64.

138. The Illinois Supreme Court commented on the power of constitutions relative to the legislature: "Where rights have been conferred and limits on governmental action have been defined by the people through the constitution, the legislature cannot enact legislation in contravention of those rights and restrictions." *Id.* ¶ 79.

legislators to find solutions that more fairly "distribute the burdens evenly among Illinoisans."[139]

Richard Briffault comments that one rationale offered for constitutionalizing fiscal restraints is that it removes those matters from the "day-to-day control of the political process" and instead embeds them in the "fundamental structure of the states."[140] He concludes, however, that this strategy did not work regarding the imposition of constitutional spending limits and other budgetary constraints.[141] This paper contends that the foregoing approach holds more promise for pension rights. A strong constitutional provision dedicated to delineating and preserving pension rights will place roadblocks in the way of political representatives who repeatedly choose to sacrifice pensions in lieu of taking more politically controversial actions, such as raising taxes. If courts are willing to subject legislation that threatens pension benefits to a more demanding level of scrutiny, it should alter political behavior in that it forecloses the option of welching on pension promises to reduce pension debt. By signaling that they are unwilling to be deferential towards eleventh-hour legislation and police powers justifications, courts can place the burden on municipalities and states to find better solutions that do not immediately penalize pensioners.

In the Louisiana and Ohio cases examined herein, the arguments sounding in contract law clause were structured in a different way. The cases showcase the unsuccessful strategies of plan members who relied upon the contracts clause in their state's constitution as a foil to thwart legislative adjustments to their pension benefits. The *Smith v. Board of Trustees of Louisiana Employees' Retirement System* case dealt with Louisiana's State Employees Retirement System ("LASERS"). State employees brought suit relying upon arguments grounded in constitutional contracts-based provisions[142] and a civil code provision proscribing retroactive laws.[143] They asserted that, because the impact of the contested law was to revoke retirement benefits that were available to them at the time they were

139. *Id.* ¶ 69.

140. Briffault, *supra* note 10, at 944.

141. Briffault concludes that "There is an enormous gap between the written provisions of state constitutions and actual practice. State legislatures and local governments have repeatedly sought to expand the 'public purpose' and to slip the restraints of the tax and debt limits." Briffault, *supra* note 10, at 909 (footnotes omitted).

142. The Contracts Clause is contained in Article I § 23 of the Louisiana constitution. The other contracts provision pertains to pensions and is contained in Article X § 29. The plaintiffs also relied upon the federal contracts clause. For purposes of this analysis, however, the focus is on the state constitution. *See* LA CONST. art. I, § 23; *id.* art. X, § 29

143. LA. C.C. art 6 ("In the absence of contrary legislative expression, substantive laws apply prospectively only.").

rehired, and replace those benefits with lesser options, the law impermissibly impaired their contracts with the state[144] and was retroactive. The court viewed the contracts clause argument as secondary to the vesting issue. From the court's perspective, there could be no impairment operating retroactively unless the challenged legal measure "modifie[d] or suppresse[d] the effects of a right *already acquired*."[145] Thus, the key issue was whether public employees who had not yet retired could claim to have legally enforceable rights in their pension benefits.[146]

The essential contract provision that the *Smith* plaintiffs drew upon was in the article governing pension benefits. Article X, Section 29(B) of the Louisiana constitution establishes that the relationship between public employers and employees is a contractual one.[147] With respect to this relationship, however, Louisiana's Supreme Court took a strikingly different approach from that of Illinois. The *Smith* court concluded that the contract is formed only when the employee has fulfilled the requisites of the employment relationship by qualifying for retirement.[148] In contrast, Illinois recognizes that the contract is formed and, therefore, rights attach, at the start of the employment relationship. Because the *Smith* court determined that the pension contract provision of Section 29(B) only pertains to retirement benefits that are vested,[149] and the plaintiffs in *Smith* were concerned about benefits for which they had not yet met the age and service requirements, the new law that revised the benefits available did not violate the contracts clause.[150]

144. Smith v. Bd. of Tr. of Louisiana State Emp.s' Ret. Sys., 851 So. 2d 1100, 1105–06 (La. 2003).

145. *Id.* at 1106 (emphasis added).

146. *Id.* at 1109.

147. LA. CONST. art. X, § 29.

148. *Smith*, 851 So. 2d at 1108–09. The Smith court concludes: "Upon their retirement, plaintiffs had a contract with the state for those retirement benefits that were vested." *Id.* at 1109.

149. The *Smith* court reasoned that "although La. Const. Art. X, §29(B) expressly states that membership in LASERS creates a 'contractual relationship,' this constitutional provision serves to expressly recognize the existence of a contract between the state and employee as to those retirement benefits that are vested." *Id.* at 1109.

150. *Id.* at 1110 ("As we have found that the plaintiffs have not met their burden under part one of the Contracts Clause analysis that the statute impaired a contractual obligation, our Contract Clause analysis is at an end."). The *Smith* court identifies the four-part test that should be applied for evaluating whether there is a violation of the contracts clause:

> (i) whether the law impairs a contractual relationship, (ii) whether the constitution is implicated by the impairment, (iii) 'whether a significant and legitimate public purpose justifies the regulation,' and (iv) where there is a significant and legitimate purpose 'whether the adjustment of the rights and responsibilities of the contracting parties is based upon reasonable conditions and is of a character appropriate to the public purpose justifying the legislation's adoption.'

The negative impact of the court's decision on public workers is substantial. It leaves them vulnerable to the whims of the legislature and to fiscally irresponsible state and local governing officials. The *Smith* holding means that public employees could work up until several days before they retire, counting on the benefits that their government-employer originally presented to them and that were in effect during the tenure of their employment, and right before their retirement, the legislature could modify or eliminate those benefits entirely.[151] What facilitated the court's ruling were three items. One item concerns the drafters' inclusion of the phrase "accrued benefits" in the pension protection provision of 29(E)(5). Another item deals with the drafters' separation of the ideas that the contract cannot be impaired or diminished from the language recognizing the existence of a contract between public employers and employees.[152] Yet another item concerns the reference in 29(F) to future changes to the retirement systems.[153] This language formally contemplates that the legislature can make changes to the pension system; however, notice of proposed changes is required.[154]

Rather than the language in Sections 29 (A) and 29(B) operating to grant substantial protection to public employees, it is undercut by section 29(E)(5)—a section which refers to accrual and, thus, opens the door to the court interpreting vesting to occur other than at the moment one begins one's employment. Even though some may view the constitutional provisions and the court's interpretation of them as allowing the appropriate amount of flexibility for legislatures to maneuver in times of severe financial crisis, Louisiana's view is destabilizing to local and state economies.

Id. at 1109. The test appears to allow for somewhat rigorous scrutiny of a pension modifying law but, because only retirees can claim an impairment, it is of limited effectiveness with respect to preserving pension benefits.

151. *Id.* at 1108 ("Likewise, we hold that reemployment benefits for retirees can be modified prior to the point when the retirees become eligible for those benefits.").

152. The language is in the same article. But the separation of the concepts into different sections of that article allows for conflicting interpretations regarding pension rights. Sections 29 (A) and 29 (B) recognize that an employer–employee contractual relationship exists between public employees who are members of the public retirement system and the state. Section 29(E) precludes changes that diminish or impair "accrued benefits." LA. CONST. art. X, § 29. Despite the language acknowledging the formation of a contract between the government and public employees by virtue of being members of the retirement system in 29(B), the *Smith* court relied upon the "accrual" language in section 29 (E) to reason that impairment of benefits that have not yet been accrued is permissible under the state constitution. Smith v. Bd. of Tr. of Louisiana State Emp.s' Ret. Sys., 851 So. 2d 1100, 1109–10 (La. 2003).

153. Section 29(F) provides in relevant part that "[b]enefit provisions for members of any public retirement system, plan, or fund that is subject to legislative authority shall be altered only by legislative enactment . . . ." LA. CONST. art. X, § 29(F).

154. LA. CONST. art. X, § 29.

Furthermore, it assigns the primary risks of pension fund insolvency to public workers.

Ohio's approach towards pensions differs markedly from that of the other states already examined, in that Ohio does not have a pension protection clause in its constitution. Instead, the definition of plan rights for Ohio's public employees is contained in numerous statutes that govern various pension funds. This limited segmented approach, judging from the STRS statutes, offers substantially less protection for plan participants when compared to Illinois' framework. Ohio's treatment of public pensions demonstrates that, where states fail to specifically carve out contractual status for pensions, courts will be reluctant to afford them substantial protection. The Supreme Court of Ohio's response to the plaintiff's attempts in *State ex rel. Horvath v. State Teachers Retirement Board* to draw upon the language of contract[155] to stave off the application of changes to his wife's pension benefits supports this conclusion. Grounding its ruling in the unmistakability doctrine,[156] Ohio's Supreme Court held that the relationship between public employees and their employer is not one of contract.[157] Absent an express intention of the government to establish a contract, the court declined to find one.[158] The *Horvath* court concluded that, "there is nothing in any version of the Act evincing an intent on the part of the General Assembly to bind itself contractually to STRS participants."[159] Except for the language referencing the unmistakability doctrine, Ohio's approach is like Louisiana's. Ohio does not recognize "a vested or contractual right to defined STRS benefit levels upon commencement of public employment."[160] In *Horvath*, this meant that "public school teachers do not possess contract rights in any STRS benefits unless and until the benefit vests by operation" of the relevant statute, which is pegged to when one retires.[161] Prior to vesting, the legislature can alter benefits for public employees.[162]

155. 697 N.E.2d 644, 653–55 (Ohio 2007). The *Horvath* plaintiff's arguments were based, in part, on the contracts clause. *Id.* (plaintiff argued, *inter alia*, that the state was precluded by the state constitutional Contracts Clause from altering his wife's pension plan).

156. The unmistakability doctrine requires that the legislature expressly declare its intentions to "bind future legislatures" to overcome the court's "presumption" that contractual rights are not prevailing in relationships between the government and others. *Id.* at 653.

157. *Id.* at 654.

158. *Id.*

159. *Id.*

160. *Id.*

161. *Id.* at 655.

162. *Id.* at 654.

Another interesting aspect of Ohio's public pension jurisprudence concerns its treatment of constitutional property-based arguments and takings claims. This matter is explored below.

B. State Constitution Property-Based Rights: Pensions as Property and the Takings Clause

Jack Beermann has observed that, "under current understandings government contractual promises may be considered property for constitutional purposes."[163] Instinctually, one may assume that property rights furnish substantial protection to prospective pensioners. Certainly, from the perspective of the public employee, pension benefits feel like property they will claim in the future regardless of the applicable vesting rules. However, this assumption regarding property law's potential to defend the interests of pension holders is not borne out by Ohio's case law. Property-based arguments afford less protection to public workers than ones that are contract-based.[164] This is the case for several reasons, beginning with the connection between contract and property law claims. A preliminary step to recognizing a property right in pensions is the establishment of a contract between public employees and the relevant government entity.[165] If one follows the logic of the *Horvath* court, it is easy to understand how this initial hurdle can immediately frustrate property-based arguments. If the contract between public employees and employers is not realized as being fully formed until the end of one's employment (i.e. until one attains retirement age) then the property argument—from this narrow perspective—neither enriches the analysis nor reinforces the employee's claim. Property in one's pension is constituted when the contract is legally acknowledged.

According to Ohio's Supreme Court, the statutes pertaining to pensions have the capacity to strip one's property (*e.g.*, one's monetary contributions to the pension system) of its character as personal property and transform it into public "statutory benefits."[166] This interpretation disarms

163. Beermann, *supra* note 104, at 63.

164. *See* Beermann, *supra* note 104 at 63–64 ("the Takings Clause is unlikely to add much to claims under the Contracts Clause because a participant's interest in pension promises is unlikely to be property unless it is found to be a contractual promise protected under the Contract Clause or state law pension doctrine."). *See also* T. Leigh Anenson et al., *supra* note 41, at 17, 20 ("the takings clause is not much of a barrier to pension reform.").

165. Maine Ass'n. of Retirees v. Bd. of Trustees of Maine Public Employment Retirement System, 758 F.3d 23, 29 (1st Cir. 2014). Beermann, *supra* note 104, at 63–64.

166. The *Horvath* court held that "mandatory teacher contributions to the STRS result from economic legislation designed to benefit retired and disabled public school teachers and their survivors and beneficiaries[] and, when placed in the fund, lose their character as private property." 697 N.E.2d at 652 (citing OHIO REV. CODE ANN. § 3307.03) (footnote omitted).

property-law-based arguments of their power. Legislative decisions will then determine "the nature and extent of a contributor's protected property rights in the STRS."[167] When viewed from a property law perspective, any attempts to modify public pensions would be considered takings requiring just compensation under the Fifth and Fourteenth Amendments of the United States Constitution. Framing pension rights in this way does not guarantee that they will be immune from attack. The federal constitution does not preclude takings. It merely recognizes them and imposes due process and compensatory requirements when they occur. In certain respects, given the privileged construct of property owners and non-owners within the American legal system, it makes sense to view pensions as property. This orientation accords owners certain rights and privileges when appropriation is threatened. When one considers, however, the state of federal takings jurisprudence, adopting this approach gets courts entangled in the messy work of balancing the interests of pension holders with those of the larger society.

An argument that a new law takes one's property by eliminating or decreasing the value of benefits that were once promised places such claims within the universe of regulatory takings.[168] If, however, the governmental entity sought to appropriate pension benefits that had already been paid, in some jurisdictions, the pensioner could assert a physical takings claim.[169] *Horvath* offers insight into the outcome of a claim from a regulatory takings perspective. In *Horvath*, the husband of a public employee brought an action to recover interest on his wife's contributions to the STRS following her death. Mr. Horvath alleged that the statute the state adopted after his wife's employment with STRS but prior to her death,[170] was a taking as to a portion of her retirement benefits in violation of the takings provisions in the federal and Ohio constitutions.[171] The court ap-

167. *Id.*

168. *See* Beermann, *supra* note 104, at 64–65, n.234 (commenting on the difficulties of valuing pension benefits within the framework of a regulatory takings claim).

169. *See* Beermann, *supra* note 104, at 64. The pensioner could also seek to recover the contributions he paid into the retirement system fund but not, necessarily, the interest that had accrued on those contributions over time, as the *Horvath* case demonstrates. *Id.*

170. The wife died before she reached retirement age.

171. The Fifth Amendment of the U.S. Constitution contains the Takings Clause, which provides that private property shall not "be taken for public use, without just compensation." U.S. CONST. amend. V. Similarly, Article I § 19 of Ohio's Constitution covers takings and provides:

> Private property shall ever be held inviolate, but subservient to the public welfare. When taken in time of war or other public exigency, imperatively requiring its immediate seizure or for the purpose of making or repairing roads, which shall be open to the public, without charge, a compensation shall be made to the owner, in money, and in all other cases, where private property shall be taken for public use,

plied the three-prong balancing test that the United States Supreme Court articulated in *Penn Central Transportation Co. v. New York*.[172] When evaluating regulatory takings claims, the court must weigh three factors: (1) "the economic impact of the regulation on the claimant"; (2) "the extent to which the regulation has interfered with distinct investment-backed expectations"; and (3) "the character of the governmental action."[173] This framework for takings determinations is fraught with numerous problems, not the least of which is the second prong regarding what constitutes "distinct investment-backed expectations." Many property law scholars have offered noteworthy critiques of judicial approaches to regulatory takings.[174]

The first prong of the *Penn Central* test is likely to bring the court back to the question of whether the claimant has property in the pension benefit he is claiming. That query will lead the court to assess whether the individual's right has vested or has not yet accrued. If the court determines that the benefit has not accrued, as the *Horvath* court concluded,[175] this sets up the plaintiff's likely failure on the second prong. That is, if the plaintiff does not have a property right in the benefit he seeks to preserve for his retirement, then he could not have reasonable distinct investment-backed expectations with respect to that benefit.[176] This is essentially the logic that the *Horvath* court followed to hold that the *Penn Central* analysis weighed "against finding a taking."[177] Just as the *Penn Central* test proved unfavorable to Penn Central's arguments—that relying upon its airspace to develop its property in order to take advantage of the terminal's prime location and benefit from a lucrative lease with a tenant was within its reasonable distinct-investment backed expectation[178]—pre-retiree participants in certain

> a compensation therefor shall first be made in money, or first secured by a deposit of money; and such compensation shall be assessed by a jury, without deduction for benefits to any property of the owner.

172. 438 U.S. 104 (1978).

173. *Id.* at 124. *See* State ex rel. Horvath v. State Teachers Ret. Bd., 697 N.E.2d 644, 650 (Ohio 2007).

174. , *See e.g.*, THOMAS W. MERRILL & HENRY SMITH, PROPERTY: PRINCIPLES AND POLICIES 1219–1336 (3d ed. 2016); Carol Rose, *Mahon Reconstructed: Why the Takings Issue Is Still a Muddle?*, 57 S. CA. L. REV. 561 (1984); Carol Rose, *Takings, Federalism, Norms*, 105 YALE L.J. 1121 (1996); WILLIAM A. FISCHEL, REGULATORY TAKINGS: LAW, ECONOMICS, AND POLITICS (Harv. U. Press 1995).

175. *Horvath*, 697 N.E.2d at 651 ("In Mrs. Horvath's case, failure to reach retirement age cause her potential STRS benefits to remain unrealized.").

176. *Id.*

177. *Id.*

178. Despite having secured a multi-million-dollar lease with a commercial tenant, the court held that New York's Landmarks Preservation law, which precluded Penn Central's tenant from constructing a fifty-story office tower on top of its property without the Landmarks Preservation Commission's approval, did not constitute a taking. Penn Central Transportation Co. v. New York, 438 U.S. 104, 116 (1978).

pension systems are likely to find arguments, regarding what is reasonable, unhelpful. It is easy to manipulate the outcome of the test where there is no anchoring pension clause that carves out a vested right upon entry into public employment. While asserting that one has a property right in one's pensions is a component of the argument pension expectants will make, the takings argument only gets one so far. Retirees will have the strongest takings arguments because at least with respect to the base pay (i.e. excluding COLAs), courts would most likely deem their rights to those benefits to be vested. If a takings claim is successful, the remedy could be an injunction prohibiting the application of the law or just compensation. The former would be better. The latter opens the potential for revaluation of the pension benefit in terms of the "just compensation" measure. In recessionary times, depending upon whether the municipality or state is experiencing economic duress, just compensation may not equate to a dollar for dollar replacement of the benefit that is being removed from one's benefit package.[179]

Because the property-based approach entails a balancing test, it injects a level of uncertainty in case outcomes, which seems counter to the objectives of public pensions. To the extent that governments utilize pension benefits to attract employees and to spread compensation over a period that is more manageable than paying higher salaries upfront, they should be reliable in the payment of retirement benefits. The United States Supreme Court has not always been consistent or clear in its articulation of the standards for takings or their application.[180] While asserting that one's property has been taken may at first seem like a position of strength, in practice—for those jurisdictions that adopt a property-based perspective—it may render public workers more vulnerable to governmental restructuring of their plans. Notably, pensioners' arguments grounded in property law give rise to the counter-position of governments that modifications to pensions are permissible under the state's police powers and are necessary when the health, safety, and welfare of a jurisdiction is threatened.[181]

179. S Beermann, *supra* note 104, at, at 65–66 (highlighting the difficulty of calculating just compensation for the government's taking of pension benefits).

180. *See e.g.*, Rose, *Mahon Reconstructed*, *supra* note 174, at 562–63, 597–99 (focusing on the *Mahon v. Pennsylvania Coal* case to discuss issues with takings jurisprudence and to offer clarifying solutions); FISCHEL, *supra* note 174, at 14.

181. For example, Although Louisiana's constitution recognizes a right to property, this section apparently would not provide more shelter for pension holders than the protections under Article X, primarily because it also includes language stating that it is "subject to reasonable statutory restrictions and the reasonable exercise of police power." LA. CONST. art I, § 4(A).

C. Bankruptcy and the Federal Government's Role in Resolving the Public Pension Crisis

If one must identify the limit of pension rights, it appears to be when a municipality declares bankruptcy.[182] Given that states cannot declare bankruptcy, for state pensions the limit is determined by the vesting rules, which may dictate that benefits are owed when the retiree reaches the designated retirement age and retires. Michigan's Pension Protection Clause[183] offered little to no protection against government administrators who sought to restructure Detroit's debt under the cloak of federal bankruptcy.[184] There is a question of whether any provision, even one as tightly crafted to confer protection as Illinois', would be impenetrable in bankruptcy proceedings. Certainly, if all bankruptcy courts follow the logic of the judges in the Michigan and Stockton, California cases,[185] even pension provisions like Illinois'— provisions that have been interpreted as providing contractual and property rights in retirement benefits at the inception of employment—

182. Michigan, Illinois, and Ohio "have formal intervention programs for municipal bankruptcy." Anderson, *supra* note 15, at 1156 (citing to THE PEW CHARITABLE TRUSTS, THE STATE ROLE IN LOCAL GOVERNMENT FISCAL DISTRESS (July 2013), http://www.pewtrusts.org/~/media/assets/2013/07/23/pew_state_role_in_local_government_financial_distress.pdf [https://perma.cc/7NML-PPNR].).

183. MI. CONST. art. IX, § 19.

184. *See* In re City of Detroit, 504 B.R. 97, 150 (E.D. Mich. 2013).

185. Prior to Detroit's filing, Stockton, California ranked as the largest municipality to file for bankruptcy. *See* Jim Christie, *Stockton, California files for bankruptcy*, REUTERS (June 28, 2012), In the Stockton case, the court held:

> It follows then, that contracts may be impaired in this Chapter 9 case without offending the Constitution. The Bankruptcy clause gives Congress express power to legislate uniform laws of bankruptcy that result in impairment of contract; and Congress is not subject to the restriction that the Contracts Clause places on states . . . .
>
> . . . .
>
> The federal bankruptcy power also, by operation of the Supremacy Clause, trumps the similar contracts clause in the California state constitution.
>
> . . . .
>
> In sum, even if the plaintiffs' benefits are vested property interests, the shield of the Contracts Clause crumbles in the bankruptcy arena.

In re Stockton, 478 B.R. 8 (E.D. Cal. 2012), 16. An interesting subsequent development in the Stockton case is that because of California's Public Employee's Retirement System strenuous opposition to the court's ruling that pensions can be modified in bankruptcy, it has led the city to rethink some of the initial pension cuts proposed. *See* Robin [Respaut, Stockton bankruptcy judge calls California pension fund a "bully,] " REUTERS (Feb. 5, 2015). This turn of events suggests that even when circumstances are dire political will is often averse to reneging on pension obligations.

would be incapacitated by the jurisdiction of the bankruptcy court. Michigan bankruptcy judge Steven Rhodes reasoned:

> [t]he state of Michigan cannot legally provide for the adjustment of pension debts of the City of Detroit. This is a direct result of the prohibition against the State of Michigan impairing contracts in both the United States Constitution and Michigan Constitution, as well as the prohibition against impairing the contractual obligation relating to accrued pension benefits in the Michigan Constitution. The bankruptcy court, however, is not so constrained.
>
> . . .
>
> The state constitutional provisions prohibiting the impairment of contracts and pensions impose no constraints on the bankruptcy process. The Bankruptcy Clause of the United States Constitution, and the bankruptcy code enacted pursuant thereto, explicitly empower the bankruptcy court to impair contracts and to impair contractual rights related to accrued vested pension benefits. Impairing contracts is what the bankruptcy process does. [186]

The inviolability of Illinois' pension clause in the context of bankruptcy is thrown further into doubt by the Supremacy Clause of the United States Constitution.[187] While the intervention of the federal government in matters of state and local government may raise federalism concerns, those concerns are tamed where the states consent to a municipal bankruptcy.[188] The Michigan and California precedents suggest that state constitutional pension protection stops where federal powers begin, as long as the state has consented to the bankruptcy.[189] Nonetheless, making the decision to restructure pension benefits in bankruptcy will likely have a significant impact on the behavior of creditors and employees in the public sector that will be detrimental for municipalities and states. Notably, as Michele Anderson cautions, in the fallout from a bankruptcy in which pension obliga-

186. [*In re] City of Detroit*, 504 B.R. at 150 (citations omitted).

187. The Supremacy Clause, Article VI provides:

> This Constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, anything in the Constitution or laws of any State to the contrary notwithstanding.

U.S. CONST art. VI, cl. 2.

188. [*In re City of Detroit*,] 504 B.R. at 141–49.

189. The *In re City of Detroit* court concluded that, "with state consent, the adjustment of municipal debts does not impermissibly intrude on state sovereignty" and, further, "[f]or Tenth Amendment and state sovereignty purposes, nothing distinguishes pension debt in a municipal bankruptcy case from any other debt." *Id.* at 150 (citing United States v. Bekins, 304 U.S. 27, 52 (1938)).

tions are modified, "unions and public employees [will] have to learn how much to trust deferred forms of compensation like pensions and retirement health care."[190] Creditors are likely to demand more upfront in terms of loan fees and rates and workers will seek more in compensation to mitigate the risk of doing business with government entities.

Notwithstanding the federal supremacy clause, the shortcomings of Michigan's provision, like Louisiana's, are attributable to the use of the word "accrued" in connection with benefits.[191] Even outside of the context of bankruptcy the "accrual" language makes pension benefits that have not vested susceptible to modification. The qualifying language inserts too much uncertainty; it permits courts and legislators to repeatedly redefine what constitutes "accrual" well after public workers have entered into employment on the assumption that, if they performed their duties in accordance with the rules that were in place at the time, they would be entitled to claim their retirement benefits that were in effect at the time. From the standpoint of protecting public employees, it is better to deal with the matter of accrual when calculating the benefits that are due.

Bankruptcy connotes fiscal crisis. Some municipalities may seriously contemplate filing for bankruptcy as a solution to their financial dilemmas, particularly with respect to pensions, because pension debt is indistinguishable from other kinds of debt.[192] This means that where municipalities can justify renegotiating the debt, they can do so without running afoul of state or federal constitutional constraints. Municipal bankruptcy, however, is a solution with enormous costs. Therefore, despite some predictions that Detroit's ability to modify pensions relying upon this procedure sets a disturbing precedent for public employees with municipal pensions,[193] there are substantial disincentives that should dissuade financially troubled cities from rushing en masse to seek state approval to pursue this option. Stigma, additional negative credit ratings, and incurring the distrust of future creditors and workers are some of the more potent reasons weighing against selecting municipal bankruptcy. Municipal bankruptcy also presents a problem for pensioners who would have the status of unsecured creditors.

190. Anderson, *supra* note 15, at 1153.

191. It provides in relevant part, "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 thereby." MI. CONST. art. IX, § 24.

192. Judge Steven Rhodes presided over the Michigan bankruptcy proceeding. *In re city of Detroit*, 504 B.R. at 150.

193. The New York Times reported one bankruptcy lawyer as commenting that, "'If you end up with precedent that allows the restructuring of retirement benefits in bankruptcy court, that will make it an attractive option for cities." Davey & Walsh, *Billions in Debt*, *supra* note 57 at 4.

This means they would have low status priority in terms of receiving their pension payments.

Another type of federal intervention is the bailout. Exploring this option fully is beyond this paper's scope. Nonetheless, a few words on this topic are warranted, given the consideration of the legal nature and limits of pension rights herein. While it is premature to promote the possibility of a federal bailout because it creates the wrong incentives for local and state governments, and rewards their reckless behavior in failing to adequately fund their pensions and invest pension money responsibly, the costs and benefits of such a proposal should nonetheless be considered. Before approving this approach, state and local governments should consider whether there are a sufficient number of people or corporate entities residing in the relevant jurisdiction with enough assets and income to generate the required amount of revenue to cover the pension liability. Interim courses of action should be taken, such as adjusting pension benefits for future employees, valuing current pension liabilities properly, annually appropriating contributions for the pension funds, and raising taxes to spread the burden of the debt obligations. If these adjustments are inadequate, federal intervention may be appropriate. Another factor that should be included in weighing the costs is whether the pensioners in a failed pension fund would need to collect some other type of federal aid to survive. Assuming that everyone who needed aid qualified for it in some form, would those costs outweigh the costs of a bailout by the federal government? If deemed appropriate, the bailout would be a last resort option. The federal government would need to clearly outline the criteria for selecting this course of action.

V. CONCLUSION

The importance of state constitutions in moments in which city and state governments are enthralled in severe fiscal and political crisis should not be disregarded. The current challenges, however, are not merely crises of solvency. Municipalities and states are facing tough ethical and economic challenges that relate to labor, matters of fairness, and the public interest. In weighing the public interest, as defined by government officials and legislators, against the interests of pensioners to their retirement benefits, the latter should prevail.

With respect to public pensions, constitutional clauses that are appropriately formulated—clearly delineating the rights of public employees and the limitations on the powers of government to impinge upon those rights—are valuable for several reasons. Such clauses inject a measure of predictability and certainty in the relationship between public employers

and employees. Employees can be confident that their employer will provide the retirement benefits they were offered as part of their employment package at the time they were hired. Employers will know that they are not permitted to renege on retirement benefits that individuals have relied upon and accepted in connection with their employment. Thus, a constitutional provision that is protective of pensioners' rights should produce fiscally responsible behavior, provided that courts also view the language as being protective. Governments will be placed on notice that they don't have the option of covering budget shortfalls with pension funds and, therefore, they will be incentivized to find alternative solutions. The burden is appropriately imposed on Government Public Pension Decision-makers because of their superior positioning in making choices about the funding, management, and disbursement of pension benefits. Public decision-makers select the contents of the retirement benefits package, determine the appropriate contribution levels, decide whether to make contributions annually, select the investment specialists who choose which funds the pension investments should be placed in, and determine how the pension funds should be valued. Because they are the critical decision-makers, and because the actions they take with respect to scaling down pension obligations are self-interested, decisions to fix the pension funding deficits by eviscerating pension obligations should be restrained by constitutional provisions and met with extreme judicial skepticism.[194]

A blanket constitutional provision that prohibits governments from making harmful changes to pensions addresses the problem that plan participants in some states may face regarding coordinating quickly and efficiently to prevent the implementation of new laws that imperil their benefits. It ensures the uniform protection of pensions within the state. Because of the importance of such clauses, collective bargaining units, pension-overseeing entities (*e.g.*, boards of trustees) or pension fund representatives, and public employees should lobby for the inclusion of a pension protection clause in their state constitutions if they don't currently have one.

This comparison of state constitutional clauses and statutes pertaining to public pensions in Illinois, Ohio, Louisiana, and Michigan, reveals that placing constitutional limits on government power can achieve the goal of protecting retirement benefits from the incursions of politicians, though it depends upon how the protections clauses are drafted. The vulnerability of

194. Although where they are involved, the power of unions to negotiate for pension benefits should not be discounted, the decisions concerning the funding of pensions rests with government representatives.

Louisiana's and Michigan's pension clauses to political maneuvering relates to their insufficient textual formulation. The Detroit and Stockton examples suggest that, while these provisions may ultimately be penetrable in the federal bankruptcy context, if the provisions are cast in language that expressly prohibits altering retirement benefits for those that have joined a retirement system, it provides a stronger legal foundation for those arguing against such modifications.

One truism should be acknowledged: regardless of how infallible the constitution drafters think a provision offering pension protection is, its strength is ultimately defined by courts in the context of litigation.[195] In their interpretation of constitutional pension protection clauses, courts are uniquely positioned to give the protections their fullest expression. Rather than adopting a deferential approach to legislative attempts to restructure pension obligations, courts should more carefully scrutinize the changes being proposed and the reasons prompting them. While this recommendation immerses courts in the thicket of reviewing difficult financial decisions and political jockeying, this is necessary when an interest as fundamental as the financial support of retirees is at stake. The work of the courts in safeguarding public pensions is facilitated where there are strong constitutional provisions dedicated to this purpose. In the absence of such provisions, there are limits to what courts may properly do. Where the state constitutional text is supportive—and provided that the judiciary is cooperative in reading the provisions as being protective of workers' rights—the positives identified above regarding predictability, uniformity, and properly incentivizing the behavior of governments should be realized. At the very least, subjecting restructuring proposals to a higher level of scrutiny prompts governments to work harder to avoid a crisis and transmits the message that more will be required to persuade the court that this is the best option available to address the problem. Further, communicating to future public-sector employees that a significant portion of their compensation will not repeatedly be subjected to unilateral modification is likely to have a positive effect on the ability of states and municipalities to attract and retain workers. This outcome, in turn, should have a positive impact on generating the essential revenue that municipalities need for sustenance and growth.

195. With respect to fiscal limits, Briffault comments that, "[j]udicial interpretations have effectively nullified the public purpose requirements that ostensibly prevent state and local spending, lending, and borrowing in aid of private endeavors." Briffault, *supra* note 10, at 909.