No. 436PA13-4 TWENTY-SEVEN-A DISTRICT

SUPREME COURT OF NORTH CAROLINA

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I. BEVERLY LAKE, JOHN B. LEWIS, JR., EVERETTE M. LATTA, PORTER L. McATEER, ELIZABETH S. McATEER, ROBERT C. HANES, BLAIR J. CARPENTER, MARILYN L. FUTRELLE, FRANKLIN E. DAVIS, THE ESTATE OF JAMES D. WILSON, THE ESTATE OF BENJAMIN E. FOUNTAIN, JR., FAYE IRIS Y. FISHER, STEVE FRED BLANTON, HERBERT W. COOPER, ROBERT C. HAYES, JR., STEPHEN B. JONES, MARCELLUS BUCHANAN, DAVID B. BARNES, BARBARA J. CURRIE, CONNIE SAVELL, ROBERT B. KAISER, JOAN ATWELL, ALICE P. NOBLES, BRUCE B. JARVIS, ROXANNA J. EVANS, and JEAN C. NARRON, and all others similarly situated,	)	
Plaintiffs-Appellants,	)	From
v.	)	Gaston
	)	County
STATE HEALTH PLAN FOR TEACHERS AND STATE EMPLOYEES, TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM OF NORTH CAROLINA, BOARD OF TRUSTEES OF THE TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM OF NORTH CAROLINA, DALE L. FOLWELL, in his official capacity as Treasurer of the State of North Carolina, and the STATE OF NORTH CAROLINA,	)	
Defendants-Appellees.	)	

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DEFENDANTS-APPELLEES' BRIEF

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DEFENDANTS-APPELLEES' BRIEF

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ISSUES PRESENTED

1. Did the Court of Appeals correctly hold that the General Assembly did not intend to create a contract to give all state retirees a fixed level of premium-free health benefits for life?

2. If there was such a contract, were the General Assembly's actions nevertheless lawful because they did not substantially impair the contract in a way that failed to serve an important public purpose?

INTRODUCTION

In this case, plaintiffs claim that when the General Assembly enacted a statute to offer health benefits to state retirees, it made a contract to guarantee them a fixed level of premium-free health benefits for life. The Court of Appeals correctly held that this theory is unsupported by this Court's precedents.

Plaintiffs' contract theory overlooks the strong presumption that statutes do not create contracts. As this Court has explained, because statutory contracts erode core legislative powers, courts are "deeply reluctant to . . . find[ ] a contract created by statute without compelling supporting evidence" that the legislature specifically intended that result. *N.C. Ass'n of Educators v. State*, 368 N.C. 777, 787, 786 S.E.2d 255, 263 (2016).

Here, there was no compelling evidence of that kind. To the contrary, the record shows that the General Assembly specifically decided *not* to make

statutory health benefits contractual. To start, the statute never says that health benefits are vested or contractually guaranteed. Nor does the statute authorize any state agency or official to offer contracts for health benefits. These omissions are even more telling when considered alongside the statute's numerous references to *other* contracts.

Moreover, in the very statute that plaintiffs say creates a contract, the General Assembly explicitly reserved the unqualified right to amend health benefits at any time. It is established law that when a legislature reserves the right to amend a statute, the statute is not a contract. After all, legislatures inherently have the right to amend their statutes, so the *only point* of a right-to-amend provision is to foreclose creation of a statutory contract.

The benefit statute's history confirms, moreover, that this reservation of rights was precisely intended to prevent formation of a contract. When the statute was enacted in 1982, it was specifically designed to ensure that the General Assembly retained plenary control over health benefits.

In the decades that followed, the General Assembly repeatedly confirmed its understanding that health benefits are noncontractual and subject to legislative control. It did so by making hundreds of changes to the terms of those benefits, through statutes that it passed almost annually. As

this Court has held, frequent statutory amendments like these are powerful "evidence that the State did not intend to create a contract." *Id.* at 788, 786 S.E.2d at 264. Indeed, the legislature's prior changes here include two previous laws that made the *exact same change* that is the core of plaintiffs' claim: increasing the members' coinsurance rate for premium-free benefits.

For these reasons, the Court of Appeals was right to reject plaintiffs' claim to a statutory contract.

To resurrect their claims, plaintiffs also argue that they have a *nonstatutory* contract for health benefits. They do so by stitching together snippets of the nearly 20,000-page record that purport to show that plaintiffs were guaranteed a fixed level of health benefits for life. These snippets do not come close to showing a contract at all, let alone a contract with those terms. For example, nearly all of the cited statements were issued by agencies that have no role in providing health benefits. Indeed, most of plaintiffs' nonstatutory arguments are based on a false premise: that health benefits are part of the Retirement System. But that assertion is provably wrong. By law, the Retirement System administers pensions, not health benefits. Thus, as former Treasurer Janet Cowell confirmed in her

deposition, when Retirement System documents refer to the "retirement benefit," they are referring to pensions.

Instead, health benefits are provided by the State Health Plan.[1] And the relevant documents issued by the Plan confirm that health benefits were never contractually guaranteed. In particular, over the past forty years, the State Health Plan has regularly distributed booklets to plan members. If *any* document could give rise to contract rights, it would be these booklets, which comprehensively described the Plan's benefits directly to plaintiffs. But these booklets affirmatively refute plaintiffs' contract theory. They described when the General Assembly had reduced benefits, and they explicitly and repeatedly warned that the General Assembly could reduce benefits further in the future. Thus, the record disproves plaintiffs' assertion that a fixed level of health benefits was contractually guaranteed.[2]

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[1] This brief uses the term "the State Health Plan" to describe both the State's package of health benefits and the agency that manages those benefits. *See, e.g.*, N.C. Gen. Stat. § 135-48.1(14) (2017) (same).

[2] For the Court's convenience, defendants have included a chart listing all of the documents cited in plaintiffs' brief, where the documents may be found in the record, and the reasons the documents do not support the existence of a contract. *See* App. 1-17.

Finally, even assuming plaintiffs could prove a contract, they have failed to produce a working theory for how that contract has been substantially impaired. In their complaint, plaintiffs demanded an "80/20" plan. After proposing—and then abandoning—several theories for the meaning of that term, plaintiffs now demand a plan with an actuarial value that is equivalent to the "regular state health plan." This vague term cannot be part of any contract for the simple reason that the term has never been used by the General Assembly or the State Health Plan to describe any health plan provided by the State.

Although the Retirement System sometimes used the term, it did so only to refer to the Major Medical Plan, the statutory plan that the General Assembly discontinued in 2008. And the record shows that the State has always offered premium-free plans to retirees with actuarial values that are equivalent to that plan. Thus, even accepting plaintiffs' latest theory of the alleged contract's terms, they have failed to show a material breach.

For these and other reasons, the Court of Appeals correctly held that plaintiffs do not have a contract that locks in a fixed level of health benefits, premium-free, for the rest of their lives. This Court should affirm the Court of Appeals' unanimous decision.

STATEMENT OF THE CASE

In 2011, the General Assembly authorized the state agency that administers the State Health Plan for Teachers and State Employees to charge a monthly premium for one of its health plans.

A few months later, a group of retired state employees and teachers filed this lawsuit. They claimed that the premium impaired a contract between them and the State, violating the Contract Clause of the U.S. Constitution and article I, section 19, of the North Carolina Constitution. (R pp 21-22) The Chief Justice designated the case as exceptional and assigned it to Superior Court Judge Edwin G. Wilson, Jr. (R pp 33-34)

The State moved to dismiss based on sovereign immunity. (R pp 27-32) The trial court denied the motion and the Court of Appeals affirmed. *Lake v. State Health Plan for Teachers & State Emps.*, 234 N.C. App. 368, 375, 760 S.E.2d 268, 273-74 (2014).

On remand, the trial court granted plaintiffs' motion to certify the case as a class action. The class includes almost all retired state employees who were eligible to enroll in the State Health Plan as of 1 September 2016. The class includes more than 220,000 retirees or their estates. (R p 377)

Both sides moved for summary judgment. The trial court granted plaintiffs' motion and denied the State's motion. (R pp 612-20) It also entered a permanent injunction against the State. (R p 618-19)

The State appealed. (R pp 621-23) The Court of Appeals reversed and remanded for entry of an order dismissing the case. *Lake v. State Health Plan for Teachers & Emps.*, 825 S.E.2d 645, 656 (N.C. App. Mar. 5, 2019).

STATEMENT OF JURISDICTION

This Court has appellate jurisdiction under the substantial-right doctrine. *See* N.C. Gen. Stat. §§ 1-277(a), 7A-27(b)(3)(a). Although the trial court did not address all the remedies plaintiffs have sought, the parties have agreed that this Court has jurisdiction to review the trial court's order.[3] This is so for two reasons.

First, the trial court's decision prevented the State from enforcing state statutes. Under this Court's precedent, an injunction that prevents a "defendant from executing its statutory duties" affects a substantial right and thus may be immediately appealed. *Gilbert v. N.C. State Bar*, 363 N.C. 70, 77,

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[3] *See* Joint Pet. for Disc. Rev. at 20 (Dec. 5, 2017) ("The parties agree that the trial court's order here is immediately appealable under the 'substantial right' doctrine.")

678 S.E.2d 602, 606 (2009); *see also Sandhill Amusements, Inc. v. Sheriff of Onslow County*, 236 N.C. App. 340, 360, 762 S.E.2d 666, 680 (2014) (Ervin J., dissenting) (an injunction that precludes a state official from "enforcing the law" affects a substantial right), *rev'd for reasons stated in dissent*, 368 N.C. 91, 773 S.E.2d 55 (2015). Section 7A-27 of the North Carolina General Statutes likewise provides that the State may appeal any order that grants "injunctive relief restraining the State . . . from enforcing the operation or execution of an act of the General Assembly." N.C. Gen. Stat. § 7A-27(b)(3)(f).

Here, as the Court of Appeals recognized, the trial court's order directly restrained the enforcement of multiple state statutes. *Lake*, 825 S.E.2d at 649. For example, the General Assembly has enacted a law that allows the General Assembly "to alter, amend, or repeal" the State Health Plan. N.C. Gen. Stat. § 135-48.3. The trial court's order prevents the General Assembly from exercising its statutory authority to reform the Plan.

The trial court's order also prevents other elements of the state government from exercising their powers. The General Assembly has authorized the State Treasurer and the State Health Plan's Board of Trustees to take various steps to reform the plan. *See* N.C. Gen. Stat. § 135-48.30. For example, the Treasurer may, subject to the Board's approval, "[s]et benefits,

premium rates, co-pays, deductibles, and coinsurance percentages and maximums." *Id.* § 135-48.30(a)(2). The trial court's order limits the ability of the Treasurer and the Board to exercise these powers. Finally, in 2011, the General Assembly authorized the State Health Plan to charge a premium for certain health plans. Act of May 11, 2011, ch. 85, § 1.2(a), 2011 N.C. Sess. Laws 120. The trial court's order countermanded this statutory authorization.

Appellate review is also appropriate here for a second reason: The court's order significantly affects the state budget. *See Lake*, 825 S.E.2d at 649. The order requires the State to directly pay damages that could exceed one hundred million dollars. Moreover, complying with the trial court's injunction would have broad-ranging financial repercussions for the State's overall budget. *See Dunn v. State*, 179 N.C. App. 753, 757, 635 S.E.2d 604, 606 (2006) (reviewing an order that affected the fiscal stability of the State).[4]

Given these two unique circumstances, this Court has jurisdiction to decide this appeal under the substantial-right doctrine.

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[4] For this reason, the State has been required to report the trial court's order to the State's creditors as one of the few potential liabilities that could affect the State's overall bond rating. Office of the State Controller, *North Carolina Comprehensive Annual Financial Report, Fiscal Year Ended June 30, 2019* at 180 (Dec. 5, 2019).

STATEMENT OF THE FACTS

A. The Development of the State Health Plan

Since 1972, the State has offered health benefits to current employees on a statewide basis. Act of July 20, 1971, ch. 1009, 1971 N.C. Sess. Laws 1588-89. Much like a private corporation, the State provided these benefits via group insurance contracts that the State purchased on behalf of its employees. *Id.* § 1 at 1588. These group insurance contracts stated in detail the health benefits that were provided for each plan year. In 1974, the State extended these benefits to retired state employees. Act of Apr. 11, 1974, ch. 1278, 1974 N.C. Sess. Laws 454-55. The General Assembly later clarified that retirees would be eligible for health benefits only if they had worked for the State for five years. Act of Aug. 14, 1987, ch. 857, § 9, 1987 N.C. Sess. Laws 2101; *see also infra* pp 87-94.

In 1981, the General Assembly established a legislative committee to oversee the State Health Plan. Act of July 8, 1981, ch. 859, § 13.12-13.19, 1981 N.C. Sess. Laws 1248, 1264-66. The following year, however, to comply with this Court's ruling in *State ex. rel. Wallace v. Bone*, the General Assembly disbanded the committee. *See* 304 N.C. 591, 286 S.E.2d 79 (1982) (holding that delegating authority to a legislative committee to implement a law

violates the separation of powers). To retain plenary control over the plan's terms, the General Assembly chose to codify the plan's terms in the benefit statute, rather than delegate authority over the plan to an executive agency.[5] Act of June 23, 1982, ch. 1398, § 6, 1981 N.C. Sess. Laws 292-311. It called this statutory plan the Comprehensive Major Medical Plan.[6] *Id.* at 292. The statute set out the services and products that the plan covered, similar to how a private group contract would. *Id.*

The 1982 law also codified the plan's key financial terms. For example, the plan had:

- A $100 deductible. That is, every year, members were required to pay the first $100 of their health costs.
- An out-of-pocket maximum of $100. After a member paid the $100 deductible and another $100 in health costs in a given year, the plan would pay the rest of the member's health costs that year.

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[5] This brief uses "the benefit statute" to refer to the statutory sections that govern the State Health Plan. The benefit statute currently appears in article 3B of chapter 135.

[6] The statutory plan has also been called the "regular state insured plan" and the "Indemnity Plan," among other monikers.

- Coinsurance of 5%. After the deductible was met, members would pay 5% of their covered health costs until they reached the out-of-pocket maximum. Coinsurance is often described as a split of 100% of health costs. For example, a plan with 5% coinsurance is referred to as a 95/5 plan.
- No premium. Members did not have to pay any monthly fee to participate in the plan.
- No copayment. Members did not have to pay a flat fee to receive specific services.[7]

N.C. Gen. Stat. § 135-40.6 (1982); Doc. Ex. 1240, 1244-45. However, there is no indication that the General Assembly attempted to create a plan with a particular actuarial value—that is, a plan that would be projected to cover a given percentage of members' total expected health costs.[8] Indeed, there is

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[7] Some early plan materials refer to coinsurance as an annual "copayment." (Doc. Ex. 1167-68) This brief uses the term "copayment" to refer to a flat fee that policy holders must pay to access a specific health service.

[8] An actuarial value estimates the percentage of "total average costs for covered benefits that the plan will cover." Ctrs. for Medicare & Medicaid Servs., *Actuarial Value*, HealthCare.gov, https://www.healthcare.gov/

no evidence that the General Assembly, or any state agency or official, ever considered the 1982 plan's actuarial value.

In the 1982 law, the legislature also included a clause to prevent the statute from being construed as a contract. Specifically, the General Assembly explicitly "reserve[d] the right to alter, amend, or repeal" the plan in the future. Act of June 23, 1982, ch. 1398, § 2, 1981 N.C. Sess. Laws 288. The right-to-amend provision has remained in place since that time. *See* N.C. Gen. Stat. § 135-48.3.

Consistent with this right, the General Assembly has amended the benefit statute almost annually. Over the twenty-nine years between 1982 and the filing of this lawsuit in 2011, the General Assembly amended the plan at least twenty-seven times, making hundreds of changes to the plan's terms. (Doc. Ex. 17-25) Many of these amendments significantly changed the benefits available under the plan. For example, the General Assembly has regularly amended the plan's core financial terms. These changes include:

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glossary/actuarial-value/ (last visited July 17, 2020). It is calculated by considering all aspects of a plan's benefit structure and estimating the amount of health care the average person will need. Because it is a statistical projection, the actuarial value does not reflect the amount any individual actually pays for health care. *Id.*

- In 1985, coinsurance rose from 5% to 10%. In 1991, it rose again to 20%.
- In 1986, the deductible rose from $100 to $150, then to $250 in 1991, then to $350 in 2001, then to $450 in 2007.
- In 1985, the out-of-pocket maximum rose from $100 to $300, then to $1000 in 1991, to $1500 in 2001, and to $2000 in 2005.
- Copayments were introduced and then repeatedly increased for different kinds of services and prescription drugs.

(Doc. Ex. 14, 17-25) Throughout all these changes, there is no evidence that the General Assembly ever considered the plan's actuarial value.

Over the years, the State Health Plan has also offered a number of different plans alongside Major Medical Plan. (Doc. Ex. 1168, 3036-52) For example, in 2005, the General Assembly amended the benefit statute to authorize the State Health Plan to introduce a new kind of health plan, in addition to the Major Medical Plan. Act of Aug. 13, 2005, ch. 276, § 29.33(a), 2005 N.C. Sess. Laws 1003. These "preferred provider organization" (PPO) plans differed markedly from the Major Medical Plan. Most notably, benefits under a PPO plan vary based on the service provider. That is, under a PPO plan, certain medical providers agree to charge the State Health Plan lower

rates. To encourage members to use these "preferred providers," the plan charges a lower deductible and lower coinsurance when members use an "in-network" provider. (Doc. Ex. 59, 64)

Between 2006 and 2008, the State Health Plan offered members a choice of three different PPO plans, in addition to the Major Medical Plan. Each plan differed in its financial terms, as well as in the health services covered. (*E.g.*, Doc. Ex. 1060) The PPO plans are commonly referred to by their in-network coinsurance rates: the 70/30 PPO plan, the 80/20 PPO plan, and the 90/10 PPO plan. (Doc. Ex. 63)

Effective in 2008, the General Assembly discontinued the Major Medical Plan, the statutory plan that the State had offered, with numerous amendments, since 1982. Act effective July 1, 2008, ch. 323, § 28.22A(a)-(b), 2007 N.C. Sess. Laws 892.

Since the introduction of the PPO plans in 2006, the State has continued to offer a variety of health plans. At least one of these plans has always been premium-free for individual retirees.[9] For example, the State has never charged a premium for retirees to enroll in the 70/30 PPO plan.

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[9] On the other hand, since 1982, the State Health Plan has always charged premiums for coverage of spouses and family members.

Before 2011, the 80/20 PPO plan also did not charge a premium. (Doc. Ex. 3056-60) In 2011, however, the General Assembly authorized the State Health Plan to charge state employees and retirees a monthly premium for individual coverage under the 80/20 PPO plan. Act effective July 1, 2011, ch. 85, § 1.2(a), 2011 N.C. Sess. Laws 120. In effect, this change increased the coinsurance from 20% to 30% for individual retirees who preferred a premium-free plan. Some class members chose the 80/20 PPO plan and paid the premium; others enrolled in the premium-free 70/30 PPO plan.

In 2014, the State introduced two new types of health plans that were also premium-free. First, the State began to offer Medicare Advantage plans. (Doc. Ex. 53-54, 60, 66) Medicare Advantage plans are private health plans that substitute for Medicare, the federal health plan available to Americans 65 and older. Benefits under Medicare Advantage plans must be at least as generous as those offered by Medicare, and they are usually more generous. (Doc. Ex. 127, 132, 3367) Over 75% of state retirees are eligible to enroll in a Medicare Advantage plan. (Doc. Ex. 108) Since these plans were introduced, the State has always offered one that is premium-free.

Second, the State began to offer a Consumer-Directed Health Plan. This plan had a higher deductible than the 80/20 PPO plan, but only 15%

coinsurance. (Doc. Ex. 15) It generally carried no premium for individual coverage. (Doc. Ex. 104, 105) This plan was discontinued in 2017.

Overall, the State Health Plan covers over 700,000 state employees, retirees, and dependents—about 7% of the State's population.

B. Administration of the State Health Plan

After the 1982 codification of the plan's terms, the legislature still needed an executive entity to administer the plan on a day-to-day basis. The General Assembly established a board of trustees within the Office of State Budget and Management and directed the board to contract with a third party to serve as the plan administrator. N.C. Gen. Stat. §§ 135-48.22, 48.32. The board regularly awarded the contract to private companies like Blue Cross Blue Shield of North Carolina. (*E.g.*, Doc. Ex. 1317, 1550) Under this contract, the company does not serve as an insurer. Instead, it merely administers the health benefit established by the State Health Plan (through applicable statutes, rules, booklets, policies, and procedures), which is self-funded by the State through appropriations and other means. N.C. Gen. Stat. § 135-48.5.

Retired state employees may also be entitled to a pension. Pensions are described by statute as the "retirement benefit," *id.* § 135-5, and are

administered by the Retirement System.[10] The Retirement System was established in 1941, many decades before state employees first received health benefits or the State Health Plan was established. *See id.* § 135-2. For the period relevant to plaintiffs' claims—1982 to 2011—the State Health Plan and the Retirement System were run by different state agencies.[11] *See* 1981 N.C. Sess. Laws 289.

Both the Retirement System and the State Health Plan produce and distribute program summaries to educate members on the benefits available under their respective systems. Over the years, these materials were regularly updated to reflect changes in the programs. The Retirement System handbooks consistently confirm that "the benefits provided by the Retirement System" include only pensions, and not health benefits. (Doc.

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[10] The General Statutes explicitly name the "Retirement System" as a shorthand for the state pension agency. N.C. Gen. Stat. § 135-1(22) ("'Retirement System' shall mean the Teachers' and State Employees' Retirement System of North Carolina"); *id.* § 135-2 (same). The pension agency's internal materials likewise refer to the agency as the "Retirement System." *(E.g.*, Doc. Ex. 3849-50).

[11] In 2012, after the relevant events in this lawsuit, the General Assembly placed both the State Health Plan and the Retirement System under the supervision of the Department of State Treasurer. N.C. Gen. Stat. §§ 135-6(q)-(r), -48.16. The agencies remain in separate divisions within the Treasurer's office, with separate boards of trustees. *Id.* §§ 135-6, -48.20.

Ex. 3849) For example, the 1988 Retirement System handbook mentioned health benefits only in a single paragraph, after twenty-six pages devoted exclusively to pensions. (Doc. Ex. 3849-62) There, the handbook also listed several other benefits that the Retirement System does not administer, including federal Social Security and Medicare benefits. (Doc. Ex. 3862) By treating health benefits in this way, the handbook confirmed that health benefits are not part of the pension system.

The booklets published by the State Health Plan, by contrast, contain extensive discussion of the health benefits that the plan is responsible for administering. (Doc. Ex. 1321-3028) Notably, these booklets never describe health benefits as a contract right. Instead, they contain repeated and explicit statements that the booklets do *not* create independent legal rights, contractual or otherwise. (*E.g.*, Doc. Ex. 1281, 1300, 1324, 1349, 1377, 1407, 1440) For example:

- The 1983 booklet stated that it provided merely "a summary of the Plan's provisions" and that if the booklet "conflicts with the laws of the State of North Carolina" then "said laws . . . will govern." (Doc. Ex. 1278) It further stated that "[s]ince the Plan was established by

law, benefits and policies can be changed only through new legislation." (Doc. Ex. 1254)

- The 2004 booklet stated that it was not a source of legal rights, because the "Major Medical Plan [is] based upon legislation enacted by the North Carolina General Assembly." (Doc. Ex. 1656)

Nor did the booklets ever promise that benefits would stay at a fixed level. In fact, they said the opposite. The booklets consistently informed retirees that "[t]he North Carolina General Assembly determines benefits for the Plan and has the authority to change benefits." (*E.g.*, Doc. Ex. 1486, 1535, 1652, 1867 2316, 2765) And they repeatedly warned retirees that benefits could be reduced because of rising health care costs. For example:

- The 1982 booklet said that because "the cost of health care is increasing each year at an alarming rate," the value of health benefits could fall. (Doc. Ex. 1240)
- The 1986 booklet noted that the Plan's value had already fallen, and cautioned that "given the continued rise in health care costs and utilization (some 12% to 14% a year in this plan alone!) further benefit changes may be necessary." (Doc. Ex. 1280)

The booklets also reflected the ongoing reductions in plan benefits that were enacted into law by the General Assembly. They showed, for example, that over the years the General Assembly increased members' coinsurance, increased the deductible, added and then increased copays, and made several other changes that reduced the value of the plan for employees and retirees. *Compare* Doc. Ex. 1331 (showing $150 deductible and 10% coinsurance and in 1989) *with* Doc. Ex. 1357-58 (showing $250 deductible and 20% coinsurance in 1992).

The booklets also made clear that the State Health Plan provided uniform health benefits for both current and retired state employees. For example, from 1982 to 2008, the booklets described a single Major Medical Plan in which employees and retirees could enroll. (*See* Doc. Ex. 1239, 1376-1405) All Plan members—both employees and retirees—received the same booklets. (Doc. Ex. 1176) Thus, while the plaintiffs were still employees, the booklets showed them the constant changes that the State was making to benefits for retirees.

C. The Current Lawsuit

In 2012, a group of retired state employees and teachers filed this lawsuit against the State and other government defendants. They alleged

that the benefit statute constitutes a binding contract. Plaintiffs claim that, under the contract, they are entitled to receive a specific premium-free health plan at a fixed level for the rest of their lives. (R pp 4-5)

Plaintiffs alleged that by enacting the benefit statute in 1982, the General Assembly made a contract offer to them. (R p 16) They argued that they accepted this offer by working for the State for five years. (R p 17) Plaintiffs claimed that the alleged contract requires the State to give them an "80/20 health insurance plan" that involves no premium. (R pp 4-5)

The specifics of plaintiffs' demand for an "80/20" plan have changed repeatedly during this lawsuit. At first, plaintiffs appeared to use this figure to refer to a plan's coinsurance rate—which is the only way the term "80/20" has ever been used either in state law or by the State Health Plan.

Later, however, plaintiffs asserted that "80/20" refers to a plan's actuarial value. Based on this assertion, they asked the trial court to "order that the Defendants provide a non-contributory comprehensive retirement health benefit to all Plaintiff Class members at a minimum actuarial value of at least eighty percent." (R p 357)

Plaintiffs later shifted their theory once again. In their brief responding to the State's motion for summary judgment, plaintiffs claimed

that 80/20 referred to the "regular state health plan." (R p 514) That term has never been used by the General Assembly or the State Health Plan. It was used by the Retirement System, but only to refer to the Major Medical Plan. (*E.g.*, Doc. Ex. 5670-74) Despite this usage, plaintiffs did not assert that the State impaired the alleged contract when it discontinued the Major Medical Plan in 2008. Instead, they claimed that the State impaired the contract more than three years later, in 2011, by attaching a premium to the 80/20 PPO plan. They stake this claim on the assertion that the 80/20 PPO plan is the "heir and progeny" of the repealed Major Medical Plan. (R p 517)

The alleged contract impairment, in plaintiffs' view, violates the Contract Clause of the United States Constitution. (R p 22) Plaintiffs also claimed that requiring payment of a premium took plaintiffs' property without just compensation, violating article I, section 19 of the North Carolina Constitution. (R pp 22-23)

After discovery, the trial court entered summary judgment for plaintiffs. The court concluded that health benefits are deferred compensation for plaintiffs' earlier work. On this theory, the court held that the State has made a contractual promise to give a fixed level of health benefits to state retirees for the rest of their lives. (R pp 614-15) Specifically,

the court held that the alleged contract requires a premium-free health plan with the same actuarial value as the September 2011 version of the 80/20 PPO plan. (R p 616) It said that such a plan would continue the "regular state health plan" that the State had offered retirees since 1982. (R p 615) The court went on to hold that when the State began charging a premium for the 80/20 PPO plan, it violated the Contract Clause in the U.S. Constitution and took plaintiffs' property without just compensation. (R pp 616, 618)

The court issued a permanent injunction that requires the State to give the class members lifetime access to a premium-free health plan that has an actuarial value equivalent to that of the September 2011 80/20 PPO plan. (R pp 618-19) As for damages, the court ordered the State to repay any premiums that class members had paid for the 80/20 PPO plan. (R p 619) The court held that the State also owed damages to class members who enrolled in the premium-free 70/30 PPO plan, but it did not explain how to calculate those damages. (R p 620)

On appeal, the Court of Appeals unanimously reversed and remanded for entry of judgment in the State's favor. The Court initially observed that the trial court's order was subject to immediate appeal because it "enjoined [the State] from enforcing duly-enacted statutory provisions requiring state

retirees to pay premiums" for health benefits, and because the costs of complying with the order "could severely impact the state's budget." *Lake*, 825 S.E.2d at 649.

The Court then held that plaintiffs' claims failed at the threshold, because plaintiffs could not show that the State had ever offered them a lifetime contract for health benefits. *Id.* at 656. In reaching this conclusion, the Court of Appeals cited this Court's guidance that statutes do not "create contractual rights in the absence of an expression of unequivocal intent" on the part of the legislature that a statute should constitute a contract. *Id.* at 651 (quoting *NCAE*, 368 N.C. at 786, 786 S.E.2d at 262-63).

The Court of Appeals explained that the benefit statute could not overcome the strong presumption against statutory contracts. It held that this conclusion flows from the statute's text: the statute never describes health benefits as a "'contract' between the employees and the State," but "[t]he term 'contract' *is* used in the statute to describe the relationship between the State Health Plan and its service providers." *Id.* at 654. This pattern, the Court explained, shows that the legislature did not intend for health benefits to be contractually guaranteed. *Id.*

The Court also observed that "the statute contains and reserves an express right to amend provision," and that "[t]he General Assembly has exercised this reserved power to revise and amend [the benefit statute] approximately 200 times without challenge since 1983." *Id.* at 654-55. These amendments further confirmed that the legislature never intended health benefits to be contractual. *Id.* at 655 (citing *NCAE*, 368 N.C. at 788, 786 S.E.2d at 264).

In addition, the Court explained that the health-benefit statute lacks the features that have caused this Court to rule that the state's pension statutes are contractual. In particular, the pension statutes create a mandatory scheme of deferred compensation, whereas the health-benefit statute creates a voluntary program—a program that employees can forgo, and that the legislature can change at any time. *Id.* at 652-53.

For these reasons, the Court of Appeals held that plaintiffs could not show the existence of a valid contract—a necessary precondition for all of their claims. *Id.* at 650-51. The Court therefore reversed the trial court's grant of summary judgment for plaintiffs and remanded for entry of judgment dismissing the complaint.

Finally, the Court of Appeals observed that, at most, the health-benefit statute provides for retirees to have "equal access to health care benefits" as active state employees. *Id.* at 656. The Court noted that the State has always maintained at least one health plan for retirees that is premium-free. *Id.*

This Court granted discretionary review.

SUMMARY OF THE ARGUMENT

To prevail on their Contract Clause claim, plaintiffs must show that they had a contract with the State, that the State substantially impaired that contract, and that the State's actions were not justified by a legitimate public purpose. *NCAE*, 368 N.C. at 784, 791, 786 S.E.2d at 261, 265. Plaintiffs cannot carry any part of this heavy burden.

First, plaintiffs have not shown, as they must, that the General Assembly expressed an unmistakable intent to create a statutory contract. Nothing in the text of the benefit statute marks it as a contract. To the contrary, the statute explicitly states that it is not a contract: The General Assembly reserved the unilateral right to amend the statute at any time. As the U.S. Supreme Court has repeatedly held, right-to-amend provisions of this kind prevent the creation of statutory contracts. Indeed, as Justice Story first explained more than two centuries ago in the landmark *Dartmouth*

College case, the very purpose of a right-to-amend provision is to ensure that courts do not construe statutes to create private contract rights. *Tr. of Dartmouth Coll. v. Woodward*, 17 U.S. 518, 712 (1819) (Story, J., concurring).

Here, the General Assembly has amended the statute almost annually. These constant amendments confirm that the General Assembly intended the benefit statute not as a contract, but as an ordinary statute—one subject to amendment and repeal.

The noncontractual nature of the benefit statute is consistent with this Court's earlier decisions. This Court has recognized statutory retirement contracts in only one context: pensions. Pensions are contractual, because they represent deferred compensation for an employee's work. Health benefits, by contrast, are not deferred compensation. They are optional benefits that, unlike salary, are available to all employees on equal terms.

Plaintiffs next argue that their contract is confirmed by nonstatutory record materials. But upon examination, this argument falls apart. Most of the cited documents do not even discuss health benefits. Many others were created by government contractors, not by the State. Still others were for internal government use, and thus never communicated to plaintiffs until this lawsuit. These kinds of materials cannot possibly be evidence of a

contract. And plaintiffs cite no record documents that even suggest that anyone ever believed that health benefits were guaranteed to be premium-free and *at a fixed level* for the rest of plaintiffs' lives.

Moreover, plaintiffs largely ignore the record materials that are the most authoritative: the State Health Plan's benefit booklets. And with good reason. These materials, which were regularly distributed to all class members, affirmatively disprove plaintiffs' record-based assertions. As part of their comprehensive summaries of the plan's benefits over a given period, the booklets repeatedly warned plaintiffs that benefits could be reduced by the General Assembly. They even informed plaintiffs of reductions in value that mirror the precise changes that plaintiffs challenge here: increases in the coinsurance rate for premium-free benefits.

For these and other reasons, the Court of Appeals was right to hold that the benefit statute is not a contract.[12]

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[12] Plaintiffs have sometimes claimed that "[t]he statutes themselves are not the contract, but merely the enabling legislation for the contracts." (Doc. Ex. 5782) Other times plaintiffs have said that the statute itself "created a contract." (R p 66; *see also* R p 68) Regardless of the theory that plaintiffs now advance, the law and the facts show that the statutes are neither a contract nor a contract offer, and that no state official or agency has ever offered a contract of the kind they claim.

Second, even if the benefit statute were a contract, plaintiffs have not shown that the State impaired that contract substantially. Under the Contract Clause, a statute substantially impairs contract rights only if it disrupts a plaintiff's objectively reasonable reliance interests. *Energy Reserves Grp. v. Kan. Power & Light Co.*, 459 U.S. 400, 416 (1983).

Plaintiffs here fail this standard, because the right-to-amend provision, and the regular reminder of it in the benefit booklets, put them on notice that the benefit statute was subject to legislative alteration. Given these explicit warnings (made after prior unchallenged changes), plaintiffs could not have had any reasonable expectation that benefits would remain fixed.

In fact, the record does not show that the State impaired any contract rights at all. Plaintiffs claim a contract right to a premium-free health plan with an actuarial value that mirrors the Major Medical Plan, which was discontinued in 2008. But the evidence shows that the State has always offered plaintiffs a health plan with an actuarial value at that level. In addition, to the extent plaintiffs claim a contract right to enroll in the same plan as active state employees, the State has always allowed them to do so.

Finally, plaintiffs cannot satisfy the final part of the Contract Clause test, because any impairment of plaintiffs' contract rights was justified. The

benefit changes that plaintiffs challenge here were designed to address a serious fiscal problem: thirty-five billion dollars or more in unfunded future benefits. In fact, this lawsuit risks destabilizing the State's fiscal planning to such an extent that the State was required to report the case to its creditors, which could affect the State's bond rating. A jury could conclude that the Contract Clause does not bar the State from taking modest measures, like adding a small monthly premium, to address this looming fiscal threat.

For these reasons, defendants respectfully request that the decision of the Court of Appeals be affirmed.

ARGUMENT

Standard of Review

The trial court granted plaintiffs' motion for summary judgment and denied the State's motion for summary judgment. Such an order receives de novo review. *Charlotte-Mecklenburg Hosp. Auth. v. Talford*, 366 N.C. 43, 47, 727 S.E.2d 866, 869 (2012).

To earn summary judgment, a movant must show that it prevails under the governing law. N.C. Gen. Stat. § 1A-1, Rule 56(c). It must also show that there are no genuine issues of fact for trial. *Id.* When a court decides whether a case presents genuine factual issues, all factual inferences

are resolved against the moving party. *Forbis v. Neal*, 361 N.C. 519, 524, 649 S.E.2d 382, 385 (2007).

Discussion of Law

In their key claim in this case, plaintiffs argue that the State violated the Contract Clause of the U.S. Constitution when it made changes to the State Health Plan. As shown below, the law and the record defeat this claim.

To succeed on their Contract Clause theory, plaintiffs must show that (1) the benefit statute created a binding contract between plaintiffs and the State, (2) the State's actions substantially impaired plaintiffs' contract rights, and (3) the impairment was not reasonable and necessary to serve a legitimate public purpose. *NCAE*, 368 N.C. at 784, 786 S.E.2d at 261. As shown below, plaintiffs did not meet their burden on any part of the Contract Clause test.[13]

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[13] Federal law governs each part of this test, including the key question here: whether plaintiffs had an enforceable contract. *Gen. Motors Corp. v. Romein*, 503 U.S. 181, 187 (1992) ("The question whether a contract was made is a federal question for purposes of Contract Clause analysis"). Thus, this Court's previous Contract Clause decisions rely extensively on U.S. Supreme Court decisions—and explicitly incorporate the federal standard. *E.g.*, *NCAE*, 368 N.C. at 784, 786 S.E.2d at 261. Plaintiffs claim that this Court has instead applied three separate Contract Clause tests, only one of which is

I. The Court of Appeals Correctly Held That the Benefit Statute Does Not Constitute a Contract for Lifetime Health Coverage.

Both on the law and on the record, plaintiffs fail to show that the benefit statute is a contract. Plaintiffs have not carried their burden to show that the General Assembly clearly intended the benefit statute as a contract. *See infra* pp 38-59.

Furthermore, health benefits, unlike pensions, are not deferred compensation. *See infra* pp 59-69.

Finally, even assuming that the benefit statute created a contract, it would allow plaintiffs only to enroll in the evolving form of the State Health Plan, not require any fixed level of benefits. *See infra* pp 79-87.

For all these reasons, plaintiffs have not shown that they have a contract for lifelong, premium-free health benefits at a fixed level.

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governed by federal law. Br. 22. But this Court has repeatedly applied federal law to decide the issues raised here. *E.g.*, *Bailey v. State*, 348 N.C. 130, 140-41, 500 S.E.2d 54, 60 (1998) ("In determining whether a contractual right has been unconstitutionally impaired, we are guided by the three-part test set forth in *U.S. Tr. Co. v. New Jersey*, 431 U.S. 1 (1977)"). It is true, of course, that state agencies and officials can enter private contracts that incorporate statutes. But under state law, those contracts must be authorized by statute. *McCaskill v. Dep't of State Treasurer, Ret. Sys. Div.*, 204 N.C. App. 373, 396, 695 S.E.2d 108, 125 (2010) (Ervin, J.), *aff'd per curiam*, 365 N.C. 69, 706 S.E.2d 226 (2011). Thus, an unauthorized document that purports to create a contract for retirement benefits is invalid. *Id.*; *see infra* pp 70-74.

A. The law presumes that statutes do not create contracts.

This Court has followed the U.S. Supreme Court in adopting a "strong presumption" that a statute does not create contractual rights, but instead "'merely declares a policy to be pursued until the legislature shall ordain otherwise.'" *NCAE*, 368 N.C. at 786, 786 S.E.2d at 263 (quoting *Dodge v. Bd. of Educ.*, 302 U.S. 74, 79 (1937)). The "party asserting that a legislature created a statutory contract bears the burden of overcoming [the] presumption" against statutory contracts "by demonstrating that the legislature manifested a clear intention to be contractually bound." *Id.* at 786, 786 S.E.2d at 262 (citing *Nat'l R.R. Passenger Corp. v. Atchison, Topeka & Santa Fe Ry. Co.*, 470 U.S. 451, 466 (1985)). This requires the legislature to make "an expression of unequivocal intent" for a statute to be a contract. *Id.*

This presumption against treating statutes as contracts stems from separation-of-powers concerns. *NCAE*, 368 N.C. at 787, 786 S.E.2d at 263. Under our constitutional system, "the primary function of a legislature is to make policy," not contracts. *Id.* at 786. "Policies, unlike contracts, are inherently subject to revision and repeal" by later legislation. *National Railroad,* 470 U.S. at 466. This flexibility allows legislatures to enact policies that reflect the popular will through legislation.

By "prevent[ing] subsequent revisions and repeals" of legislative enactments, statutory contracts "bind[ ] the hands of future sessions of the legislature" and prevent them from making policies to advance the public welfare. *NCAE*, 368 N.C. at 786, 786 S.E.2d at 262. Because statutory contracts pose "a threat to the sovereign responsibilities of state governments," the presumption against legislative contracting is necessary to "limit[ ] contractual incursions on a State's sovereign powers." *United States v. Winstar Corp.*, 518 U.S. 839, 874-75 (1996). Without the presumption, statutory contracts would "hamper[ ] the legislative power of the State" and "leave it without the means of performing its essential functions." *Mial v. Ellington,* 134 N.C. 131, 153, 46 S.E. 961, 968 (1903).

Because of these concerns, this Court is "deeply reluctant" to find a statutory contract "without compelling supporting evidence." *NCAE*, 368 N.C. at 787, 786 S.E.2d at 263. This reluctance calls for courts to "proceed cautiously both in identifying a contract within the language of a regulatory statute and in defining the contours of any contractual obligation." *National Railroad,* 470 U.S. at 466.

The concern that statutory-contract claims intrude on legislative powers "take[s] on added force" when a claim involves a "comprehensive

social welfare program" that affects large numbers of people. *Bowen v. Pub. Agencies Opposed to Soc. Sec. Entrapment*, 477 U.S. 41, 53 (1986) (stating that courts are "extremely reluctant" to recognize statutory contracts in this situation). This is because the State's need for flexibility is greatest when it enacts a broad regulatory program to advance the public welfare. *Id.* The Court should therefore proceed cautiously here, where plaintiffs seek to contractually guarantee health benefits to hundreds of thousands of North Carolinians, with broad repercussions for the State's overall budget.

That reluctance should be at its zenith in this case, moreover, because plaintiffs are alleging a contract for *lifelong* benefits. Such an allegation violates the traditional principle that "contracts that are silent as to their duration" are presumed not to create "lifetime promises." *M&G Polymers USA, LLC v. Tackett*, 574 U.S. 427, 441 (2015); *see id.* at 442 ("[W]hen a contract is silent as to the duration of retiree benefits, a court may not infer that the parties intended those benefits to vest for life."). The U.S. Supreme Court has applied that principle twice in recent years. In both cases, it rejected retirees' claims that they had a contract that entitled them to "lifetime contribution-free health care benefits." *Id.* at 931, 937 (applying the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001-1461);

accord CNH Indus. N.V. v. Reese, 138 S. Ct. 761, 763-64 (2018) (rejecting claim to lifetime benefits, because "if the parties meant to vest health care benefits for life, they easily could have said so in the text").

In sum, plaintiffs must overcome a high burden to establish the massive statutory contract that they allege here—a contract that would intrude on the legislature's core policymaking function.

B. Plaintiffs cannot show that the benefit statute is a contract.

The Court of Appeals correctly applied the above principles to hold that the health-benefit statute is not a contract. Plaintiffs cannot show that the General Assembly has expressed an unmistakable intent for health benefits to be contractually guaranteed. To the contrary, the text and history of the benefit statute show that the General Assembly never intended the statute to create contract rights.

The legislature's lack of contracting intent is shown by four points:

- First, the benefit statute never says that it is a contract, even as it specifically refers to other contracts. *See infra* pp 39-43.
- Second, the General Assembly expressly reserved the right to change the terms of the State Health Plan. *See infra* pp 44-51.

- Third, the General Assembly has repeatedly amended the statute in ways that contradict any supposed intent to create a statutory contract. *See infra* pp 52-55.
- Fourth, the statute's enactment history shows that the General Assembly structured the statute to maintain full control over the Plan's terms, not to cede that very control by creating a statutory contract. *See infra* pp 55-59.

1. The General Assembly has not clearly expressed any intent to create contract rights.

The benefit statute does not contain any clear expression of an intent to treat health benefits as a contract. For this reason alone, plaintiffs cannot overcome the strong presumption against legislative contracting.

"A party asserting that a legislature created a statutory contractual right bears the burden of . . . demonstrating that the legislature manifested a clear intention [for the State] to be contractually bound." *NCAE*, 368 N.C. at 786, 788, 786 S.E.2d at 262, 264. This clear-statement rule demands that the General Assembly express an "unmistakable legislative intent" to create a contract. *Id.* at 787, 786 S.E.2d at 263 (requiring the legislature's contracting intent to be "explicit"); *see also Winstar*, 518 U.S. at 875 (requiring "terms too plain to be mistaken"). For a statute to meet this clear-statement rule, the

statute itself must use the "recognize[d] . . . language of contract." *National Railroad*, 470 U.S. at 470; *see also NCAE*, 368 N.C. at 787, 786 S.E. 2d at 263 (to discern whether the legislature intended to create a statutory contract, "courts must consider the language used by the legislature").

The benefit statute fails this clear-statement test. For example, the statute never uses the word "contract," or any other contractual language, to describe health benefits provided to retirees. As this Court has held, "the use or omission of the word 'contract' in the statute" is a "critical" factor in discerning "legislative intent." *NCAE*, 368 N.C. at 787, 786 S.E.2d at 263. Indeed, the Court has found it pivotal that "the word 'contract' [does not] appear" in a statute's text. *Id.*; *see id.* (comparing the career-status law to another statute, where "the word 'contract' was peppered throughout nearly every section of the statute"). The U.S. Supreme Court has likewise held that a statute is noncontractual when it does not affirmatively "speak of a contract." *National Railroad*, 470 U.S. at 467; *see id.* at 470 (holding that a statute was noncontractual where it "does not contain a provision in which the United States 'covenants and agrees' with anyone to do anything").

Thus, the Court of Appeals correctly held that plaintiffs' claims fail at the threshold, because the benefit statute's text lacks a clear expression of the legislature's intent to make health benefits contractual.

This conclusion is reinforced by the legislature's highly selective use of the word "contract." As this Court has held, when a statute uses the word "contract" to describe *other* agreements, that selective use shows that the legislature did not intend other aspects of the statute to create contract rights. *NCAE*, 368 N.C. at 788, 786 S.E.2d at 263. This point echoes the *expressio unius* canon of statutory construction: When a statute mentions one item, it implies a decision to exclude other, related items. *Morrison v. Sears, Roebuck & Co.*, 319 N.C. 298, 303, 354 S.E.2d 495, 498 (1987).

Here, the health-benefit statute specifically refers to several other contracts, but it never even hints that the health coverage itself is a contract. For example, the statute describes several kinds of contracts between the Plan and vendors who provide services to the Plan. *E.g.*, N.C. Gen. Stat. §§ 135-48.1(3) (referring to contracts between the State Health Plan and a third party "to administer Plan benefits"), -48.10(b) (same, pharmacy benefit managers), -48.12 (same, actuaries), -48.33 (same, vendors "for supplies, materials, printing, equipment, and contractual services").

As the Court of Appeals held, these specific statutory references to other contracts show that the legislature never intended health coverage itself to be contractual. *Lake*, 825 S.E.2d at 654. "The use of contractual language in the statute in reference to service providers indicates the General Assembly specified situations and knew when to use the word 'contract,' and it did not intend to form a contractual relationship between the State and its employees related to health care insurance benefits." *Id.*

Plaintiffs do not dispute that the benefit statute never says at all—let alone unequivocally—that health benefits are contractual. Br. 47-55. Nor do they address the fact that the benefit statute repeatedly refers to other contracts but never describes health benefits as contractually guaranteed. *See id.* Thus, plaintiffs all but concede that their claim to a fixed level of health benefits has no support in the text of the benefit statute.

Although plaintiffs point to the statute's "undertaking" clause, that clause does not support their claim. *See* Br. 53-54. Section 135-48.2 says that the State "undertakes to *make available* a State Health Plan . . . which will pay benefits *in accordance with the terms of this Article*." N.C. Gen. Stat. § 135-48.2(a) (emphasis added). A legislative desire to "make available" a health plan is a mere statement of policy, not a binding contract. Moreover,

even that tepid statement is explicitly qualified: Any undertaking must be "in accordance with" the rest of the statute. And the very next section of the statute is the right-to-amend provision, which states that "[t]he General Assembly reserves the right to alter, amend, or repeal this Article." *Id.* § 135-48.3. Thus, even if the "undertak[ing]" in section 135-48.2 were treated as an enforceable promise, it would promise only a health plan that is subject to change or repeal.

The General Assembly further confirmed that it did not intend the State Health Plan to be contractually guaranteed in another way: It explicitly describes certain consequences if the Plan is terminated. For example, the statute states that the State will no longer provide certain health benefits upon "termination of the Plan." *Id.* § 135-48.44(h). By describing the consequences of the Plan's termination, the General Assembly has expressly disclaimed the possibility that the Plan is contractually guaranteed.

In sum, the benefit statute does not show the "unmistakable legislative intent" that is required to create a statutory contract. *NCAE*, 368 N.C. at 787, 786 S.E.2d at 263. Instead, like any public-welfare law, the statute merely announces a government policy that the legislature can change in the future.

2. The right-to-amend provision prevents the statute from forming a contract.

Another key feature of the benefit statute confirms that the General Assembly does not intend the statute as a contract: The General Assembly has expressly reserved the right to amend, or even repeal, the statute. N.C. Gen. Stat. § 135-48.3. The right-to-amend provision has been on the books since 1982, before any of the plaintiffs allegedly "vested" into benefits. Under the Contract Clause, as well as ordinary principles of contract law, this express reservation of rights defeats plaintiffs' claims.

As the U.S. Supreme Court has repeatedly affirmed, it "has been settled" for over a century that a legislature's express reservation of the right to amend a statute prevents the statute from forming private contract rights. *Bowen*, 477 U.S. at 52. Indeed, this doctrine traces all the way back to the Supreme Court's foundational Contracts Clause case, the *Dartmouth College* case. *See* 17 U.S. 518. In that case, the Supreme Court famously held that King George III's colonial-era corporate charter to Dartmouth College constituted a private contract. *Id*. at 658-59. The Court went on to hold that the New Hampshire legislature's attempt to convert the college to a public institution was invalid under the Contracts Clause. *Id.* at 664.

Justice Joseph Story issued a concurring opinion in which he clarified that the Court's holding was limited in an important way: The legislature was barred from overriding the King's charter only because "no power is reserved to the crown or government in any manner to alter, amend or control the charter." *Id.* at 680. However, he explained that a legislature *could* amend future charters if "a power for that purpose be reserved to the legislature in the act of incorporation." *Id.* at 708; *see also id.* at 712 ("If the legislature mean to claim such an authority [to amend contracts issued by the legislature], it must be reserved in the grant [of the contract]").

State legislatures quickly embraced this invitation to limit the scope of the Court's ruling. Specifically, "many a State in the Union" reacted to the *Dartmouth College* case by including right-to-amend provisions in statutes to make clear that those statutes did not confer contractual rights. *Looker v. Maynerd*, 179 U.S. 46, 52 (1900).

Over the last two centuries, these reservations have been repeatedly upheld as valid by the U.S. Supreme Court. For example, in *Miller v. State of New York*, another corporate charter case, the Court observed that "the power to alter, modify, or repeal an act" that creates private contract rights "is frequently reserved to the State by a general law applicable to all acts of

incorporation." 82 U.S. 478, 488 (1872). When legislatures do so, the Court found it "clear" that the reserved "power may be exercised whenever it appears that the act of incorporation is one which falls within the reservation." *Id.* at 489 (explicitly incorporating the reasoning of Justice Story's concurrence). Thus, as a matter of blackletter law, "where a State legislature reserves to itself, in the very charter it grants to a private corporation, the right of altering, amending, or repealing the act of incorporation, a subsequent repeal of the charter is valid and constitutional." *Id.* at 497; *see also In re Pennsylvania Coll. Cases*, 80 U.S. 190, 212-14 (1871) (applying this rule even absent an express reservation of rights, where the reservation is clear "by necessary implication").

The U.S. Supreme Court has also long applied this rule to any statute that could otherwise be construed as creating private contract rights. For example, in 1879, the Court held that when a legislature explicitly reserves the power to alter, amend, or repeal a statute, it "not only retains, but has given special notice of its intention to retain, full and complete power" to revise the statute without abridging private contract rights. *The Sinking Fund Cases*, 99 U.S. 700, 720 (1879). Thus, in that case, a statutory provision

that "Congress may at any time alter, amend, or repeal this act" foreclosed the creation of a statutory contract. *Id.* at 709.

In recent times as well, the U.S. Supreme Court has held that a right-to-amend provision conclusively establishes that a legislature did not intend to create a statutory contract. For example, in *National Railroad*, the Court considered the effect of a statute that, like here, "'expressly reserved' [a legislature's] rights to 'repeal, alter, or amend' the Act at any time." 470 U.S. at 467 (quoting 45 U.S.C. § 541 (1970)). The Court noted that this blanket reservation is "hardly the language of contract." *Id.* To the contrary, by "reserv[ing] the right to revoke or repeal the act," Congress affirmatively "declined to offer assurances about future activity," thus dispelling "any doubt" about whether Congress intended to create a contract. *Id.* at 467. In other words, the right-to-amend provision unequivocally signaled that Congress intended the statute only to create "policy that, like all policies, is subject to revision and repeal." *Id.*; *see also Bowen*, 477 U.S. at 52 (same).

This Court has likewise held that when the General Assembly "reserves the right to amend or repeal" a statute, later statutory amendments "d[o] not result in impairment of contract in violation of" the Contract Clause. *Adair v. Orrell's Mut. Burial Ass'n*, 284 N.C. 534, 538, 201 S.E.2d 905, 908 (1974)

(citing *Looker*, 179 U.S. at 52). Thus, this Court echoed the holdings of the U.S. Supreme Court that the scope of private rights under a legislative grant "is qualified by the measure of control which the state retains" to amend the contract. *Spearman v. United Mut. Burial Ass'n*, 225 N.C. 185, 187, 33 S.E.2d 895, 896 (1945) (citing *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 432, 434 (1934)). Under this principle, when a statute states that "its provisions could be 'modified, cancelled or abridged' by legislative enactment," the General Assembly does not impair contract rights when it exercises that reserved power to amend the statute. *Id.*; *see also Oglesby v. Adams*, 268 N.C. 272, 273, 150 S.E.2d 383, 385 (1966) ("if a State makes a grant . . . *without any reservation of a right to alter, modify, or repeal it*, this constitutes an executed contract, and the State is forbidden to pass laws impairing the obligation arising therefrom") (emphasis added).[14]

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[14] Other courts have similarly concluded that a right-to-amend provision prevents the creation of unalterable contractual rights to retiree health benefits. *See, e.g., Gable v. Sweetheart Cup Co.*, 35 F.3d 851, 856 (4th Cir. 1994) (the "express reservation of the company's right to modify or terminate the participants' [retiree health] benefits is plainly inconsistent with any alleged intent" to guarantee those benefits); *Emerling v. Village of Hamburg*, 680 N.Y.S.2d 37, 38 (N.Y. App. Div. 1998) (a government "may, by a clear reservation of rights, retain the power to terminate [retiree health] benefits that would otherwise be" legally protected).

To counter all of this precedent, plaintiffs can only point to the far more limited right-to-amend provision in the pension statute. Br. 56-57. The General Assembly reserved the power to amend the pension statute, but only "to coordinate with any changes[ ] in the benefit and other provisions of the Social Security Act made after January 1, 1955." N.C. Gen. Stat. § 135-18.4. As this Court has held, this limited provision "only allow[s] amendments to coordinate the retirement system with the Social Security Act." *Faulkenbury v. Teachers' & State Emps.' Ret. Sys.*, 345 N.C. 683, 691, 483 S.E.2d 422, 427 (1997). In other words, by listing only a single purpose that could justify amending the pension statute, the General Assembly impliedly gave up its power to make other statutory changes. *Id.* Here, in contrast, the health-benefit statute contains no comparable limit on the General Assembly's powers. *See* N.C. Gen. Stat. § 135-48.3.

Plaintiffs are also wrong that the right-to-amend applies only to "non-vested employees." Br. 56. That argument assumes the conclusion. It has been blackletter law for more than a century that a right-to-amend provision precludes the *creation* of statutory contract rights. Because the right-to-amend provision here was enacted in 1982, years before the contract was

allegedly formed, no plaintiff could have reasonably expected the benefit statute to create an unalterable contract right to benefits at a fixed level.

Moreover, plaintiffs' reading of the right-to-amend provision would render the provision meaningless. Because the legislature always retains the power to amend statutes, the one and only point of such a provision is to bar the creation of contract rights. Thus, plaintiffs' argument clashes with the canon against interpreting statutory provisions to be surplusage. *See Porsh Builders, Inc. v. Winston-Salem*, 302 N.C. 550, 556, 276 S.E.2d 443, 447 (1981) ("It is presumed that the legislature intended each portion [of a statute] to be given full effect and did not intend any provision to be mere surplusage.").

In sum, for over a century, courts have recognized that a right-to-amend provision offers a valid way for legislatures to convey noncontracting intent. The benefit statute's unqualified right-to-amend provision therefore precludes the statute from creating contract rights.

3. Under traditional contract principles, the right-to-amend provision makes any contract illusory.

The rule that a right-to-amend provision bars the formation of any statutory contract accords with ordinary principles of contract law.

Under North Carolina law, if a contracting party reserves "an unlimited right to determine the nature or extent of his performance," that party's promise to perform is illusory. *State v. Philip Morris USA Inc.*, 363 N.C. 623, 641-42, 685 S.E.2d 85, 96 (2009) (quoting *Wellington-Sears & Co. v. Dize Awning & Tent Co.,* 196 N.C. 748, 752, 147 S.E. 13, 15 (1929)). When a contracting party offers an illusory promise, the contract fails for lack of consideration. *Kadis v. Britt*, 224 N.C. 154, 163, 29 S.E.2d 543, 548 (1944); *see also McLamb v. T.P. Inc.*, 173 N.C. App. 586, 591, 619 S.E.2d 577, 581 (2005) ("consideration which may be withdrawn on a whim is illusory consideration which is insufficient to support a contract"). For example, the Court of Appeals has held that an employment contract was invalid because it gave the employer complete power to amend the contract's terms. *Wilmar, Inc. v. Liles*, 13 N.C. App. 71, 78-79, 185 S.E.2d 278, 283 (1971).

Here, the right-to-amend provision gives the General Assembly the unilateral right to change health benefits. N.C. Gen. Stat. § 135-48.3. Under North Carolina contract law, the provision therefore makes any statutory contract illusory and unenforceable.

4. The constant amendments to the benefit statute show that the statute is not a contract.

The General Assembly's continuous changes to the benefits statute further prove that it never intended the statute to be contractual.

As this Court has held, the fact that a detailed regulatory program is "oft-amended . . . over the decades is evidence that the State did not intend to create a contract." *NCAE*, 368 N.C. at 788, 786 S.E.2d at 264. Thus, when the General Assembly frequently "alter[s] details of" a regulatory program "while leaving the overall [program] intact," that history shows the legislature intended to retain the power to make "future modifications and amendments as needs ar[i]se." *Id.* at 789, 786 S.E.2d at 264. After all, it would invite chaos for "[e]ach new version of the statute [to] immediately create a vested contract between the State" and statutory beneficiaries.[15] *Id.* Thus, frequent statutory amendments reflect an assumption that a statute is not a contract, but "a policy to be pursued until the legislature shall ordain otherwise." *Id.* at 786, 786 S.E.2d at 263 (quoting *Dodge*, 302 U.S. at 79).

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[15] Plaintiffs here attempt to avoid that chaotic response by proposing that they all receive a uniform remedy, pegged to the 2011 version of the 80/20 PPO plan. But this arbitrary benchmark cannot be reconciled with established precedent that, for statutory contracts, a plaintiff is entitled to the terms of the statute when the contract is formed. *See infra* pp 90-91.

Here, the General Assembly has amended the benefits statute nearly every year since it was first enacted. In the twenty-nine years between 1982 and the filing of this lawsuit, the legislature amended the statute twenty-seven times—and those amendments made hundreds of changes to the State Health Plan. *Supra* pp 13-14. The statute has been changed far more frequently than other statutes whose changes have been held to undermine any inference of legislative intent to create a statutory contract. In *NCAE*, for example, this Court held that seven statutory amendments to the career-status law over forty years proved that the General Assembly did not intend that law to be a contract. 368 N.C. at 789, 786 S.E.2d at 264.

Moreover, many of these statutory amendments made significant changes to the State Health Plan that reduced the plan's overall value. (Doc. Ex. 1137-45) For example, the General Assembly has repeatedly increased the coinsurance level on premium-free benefits—to 10% in 1985, 20% in 1991, and 30% in 2011. (Doc. Ex. 14) Thus, the legislature has made clear from the beginning that it viewed as noncontractual the precise benefit term that is at the core of plaintiffs' lawsuit. In addition, every one of these value-reducing changes was applied to all plan members, including retirees.

Plaintiffs note that some changes to the plan were applied only prospectively. Br. 54-55 (noting that a 20-year eligibility requirement was not applied to existing employees). But the mere fact that *some* changes were prospective simply reflects a legislative policy choice—not an assumption that contract law required this kind of policy.[16]

Finally, the State Health Plan has communicated all of these changes directly to plan members, putting members on notice that the benefit statute is subject to change. For example, in 1985, when the General Assembly raised the coinsurance rate from 5% to 10%, the benefit booklet for the State Health Plan explicitly advised members that the General Assembly could make "further benefit changes" of that kind. (Doc. Ex. 1280) Another booklet similarly warned that, because of increases in health costs, retirees could face "higher contributions and/or copayments" and other "benefit

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[16] Indeed, almost immediately after the trial court entered its injunction in this case, the General Assembly enacted yet another change to the statute: It eliminated health benefits during retirement for future state employees. Act of June 17, 2017, ch. 57, § 35.21(c), 2017 N.C. Sess. Laws 631. This change reinforces the need for legislative flexibility to amend public benefit programs in response to changing conditions. It also shows how the NCAE's concerns about this case's effect on the "supply of teachers" has things backwards. NCAE Br. at 3. Without flexibility to make minor modifications to benefit programs in response to changing conditions, the legislature may hesitate to offer benefits in the first place. *See infra* p 103.

changes" in the future. (Doc. Ex. 1240) *See also infra* pp 74-79 (explaining why these and other record materials fail to show a contract offer). Thus, the plaintiffs regularly saw the General Assembly apply these value-reducing changes to all plan members, including retirees.

In sum, the General Assembly's extensive history of amending the benefit statute makes clear that the General Assembly never intended any particular version of the statute to create a contract.

5. The benefit statute's enactment history shows that the legislature did not intend to create a contract.

Finally, the history leading up to the General Assembly's decision to codify the State Health Plan further confirms that the legislature did not intend the health benefits provided by the statute to be contractual.

"[T]he circumstances of the Act's passage" can show that a legislature did not intend a statute to be a contract. *National Railroad*, 470 U.S. at 468; *see also Lanvale Props., LLC v. Cnty. Of Cabarrus*, 366 N.C. 142, 164, 731 S.E.2d 800, 815 (2012). The alleged statutory contract in *National Railroad* was a law that lifted certain obligations that Congress had previously imposed on railroad companies. Because of Congress's "pervasive prior regulation in this area," the Court held that "the railroads had no legitimate expectation that regulation would cease" permanently. *National Railroad*, 470 U.S. at 468.

Thus, Congress's longstanding practice of regulating railroads "strongly cut[ ] against any argument that the statute created binding contractual rights." *Id.*

Here, likewise, the circumstances that led to the State Health Plan's codification in 1982 refute any suggestion that the General Assembly intended the statute to create private contract rights. Instead, the enactment history shows that the General Assembly intended the statute to accomplish exactly the opposite result: to maintain the legislature's plenary power over the Plan's terms.

Before 1982, the State provided health coverage to state employees and retirees by purchasing insurance directly from private insurers. (Doc. Ex. 1178) In 1981, the General Assembly appointed a committee of legislators to administer the State Health Plan instead. 1981 N.C. Sess. Laws 1248, 1264-66. The committee was given broad authority to dictate the plan's terms, as well as to administer benefits, "either directly or through the purchase of contracts." *Id.* § 13.16 at 1265. The committee's members were all sitting legislators. *Id.* § 13.18 at 1265.

The very next year, however, this Court cast doubt on the committee's constitutionality. In the landmark case of *Wallace v. Bone*, the Court held

that separation-of-powers principles in our state Constitution prohibited the General Assembly from appointing a "committee of its own members to implement specific legislation." 304 N.C. at 603, 286 S.E.2d at 86. The Court held that, because implementing legislation is a core "executive function," any such committee cannot be subject to majority legislative control. *Id*. The Court went on to explain that an executive committee that was composed *entirely* of sitting legislators (like the health benefits committee) represented a "logical extreme" that illustrated the "constitutional infirmity" of less overtly unconstitutional arrangements. *Id.*; *see also In re Separation of Powers*, 305 N.C. 767, 779, 295 S.E.2d 589, 596 (1982) (holding that the General Assembly could not delegate its legislative powers to a subcommittee of individual legislators).

After *Wallace*, the Attorney General sent a letter to the General Assembly that specifically identified the legislature's health-benefits committee as unconstitutional. (Doc. Ex. 4674)

To comply with *Wallace*, the General Assembly faced a choice: It could cede control over the plan to an executive agency, or it could control the plan's details through legislation. It chose the latter option. Specifically, it codified the plan's terms in the benefit statute itself, minutely cataloguing

covered medical services, as well as the plan's financial terms. 1981 N.C. Sess. Laws 292-311.

This codification allowed the General Assembly to avoid the constitutional problems raised by its delegation of authority to a legislative committee, while also advancing its overall objective: retaining full control over the terms of the State Health Plan.

At the same time, the General Assembly recognized that codifying the plan posed risks as well. To guard against the possibility that the law could be construed as a contract, the General Assembly included a right-to-amend provision—a time-honored way to signal that it did not intend to create a statutory contract. *See supra* pp 44-48.

This history shows that the General Assembly enacted the benefits statute specifically to maintain its plenary power over the terms of the State Health Plan. Yet plaintiffs here contend the opposite: that the General Assembly enactment of the 1982 law represents a choice to cede its authority over the plan by making it a contract. Plaintiffs' theory cannot be reconciled with the statute's enactment history.

For all of these reasons, plaintiffs have not carried their burden to show an unmistakable legislative intent to create a statutory contract. To

the contrary, the statute's text, structure, and history show that the General Assembly never intended the statute to create contract rights.[17]

C. North Carolina decisions on statutory contracts show that the benefit statute is not a contract.

North Carolina decisions on statutory contracts are consistent with the above analysis. Although this Court has recognized statutory contracts in the context of public-employee pensions, it has never extended those rulings to health benefits.

Health benefits differ from pensions in every way that matters here. These differences expose the false premise on which plaintiffs rest their entire case: that because they have a statutory contract right to their pensions, they must also necessarily have a contract right to health benefits

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[17] Plaintiffs argue that any public benefit must either be contractual or an unconstitutional emolument. Br. 14-15, 52. But this Court has already rejected the claim that any public benefit is either contractually guaranteed or unconstitutional. *Hinton v. Lacy*, 193 N.C. 496, 508, 137 S.E. 669, 676 (1927). Although some cases used a "deferred compensation" rationale to avoid an emoluments claim, it does not follow that a benefit is either contractual or an emolument. *See id.* (recognizing noncontractual benefit that is not an emolument); *see Brumley v. Baxter*, 225 N.C. 691, 36 S.E.2d 281 (1945) (same). Accepting plaintiffs' position would cast doubt on the constitutionality of countless government benefits that are clearly not contractual. *See, e.g.*, N.C. Gen. Stat. § 96-14.1 (unemployment insurance).

during retirement. This false framing misunderstands the history, structure, and regulatory context of the State Health Plan.

1. This Court has recognized statutory retirement contracts in only one specialized context: pensions.

This Court has recognized statutory contracts in only one setting: when a statute gives employees either direct or deferred compensation, usually in the form of a pension. Plaintiffs cannot cite any case from this Court that recognizes a statutory contract in any other circumstance.

Pensions are contractual because they involve deferred salary. Under the State's main pension statutes, the State defers a stated percentage of a public employee's salary, confers explicit legal protections on that salary, then makes fixed monthly payments to the employee after she retires. *See* N.C. Gen. Stat. §§ 135-5, -8; N.C. Const. art. V, § 6(2). In a trio of cases, this Court has recognized that these unique features make pensions contractual.

First, in *Simpson*, the Court of Appeals held that the pension statute for local-government employees is a contract. *Simpson v. Local Gov't Emps.' Ret. Sys.*, 88 N.C. App. 218, 223, 363 S.E.2d 90, 94 (1987), *aff'd per curiam*, 323 N.C. 362, 372 S.E.2d 559 (1988). As the Court explained, the statute there was a contract because "a pension is but deferred compensation, already in effect earned, merely transubstantiated over time into a retirement

allowance." *Id*. The Court thus held that the General Assembly violated the Contract Clause when it reduced pension payments to retirees. *See id.* at 220, 223, 363 S.E.2d at 93-94.

Second, in *Faulkenbury*, this Court held that the pension statute for teachers and state employees was also a contract. 345 N.C. at 691, 483 S.E.2d at 427. Like the Court of Appeals in *Simpson*, the Court held that pensions are contractual because they are "delayed salaries." *Id.* On that basis, the Court held that a statute that reduced expected pension benefits to disabled retirees violated the Contract Clause. *Id.* at 690, 483 S.E.2d at 426.

Third, in *Bailey*, this Court held again that pension statutes for government employees are contracts. 348 N.C. at 136-38, 500 S.E.2d at 56. *Bailey* confirmed that a deferral of salary is what makes a pension statute contractual. The Court wrote, "*If* a pension is but deferred compensation . . . *then* an employee has contractual rights to it." *Id.* at 141, 500 S.E.2d at 60 (emphasis added). The Court went on to hold that a pension is indeed "a deferred portion of the compensation earned for services rendered." *Id.* Because that feature makes state pensions contractual, the Court held that a

new tax on pension payments implicated the Contract Clause. *Id.* at 140, 500 S.E.2d at 60.[18]

By contrast, this Court has declined to recognize statutory contracts outside the pension context. When the Court recently rejected another alleged statutory contract, it stressed the absence of a deferred-compensation scheme. Specifically, *NCAE* held that a statute that gave teachers career status after three years of service did not, by itself, create contract rights. 368 N.C. at 788, 786 S.E.2d at 264. The Court explained that, unlike pension benefits, which are "presently earned" but "deferred

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[18] Plaintiffs cite four other cases that they claim show that health benefits for retirees are contractual. Br. 27-28. Two of those cases dealt explicitly with pensions. *Bridges v. City of Charlotte*, 221 N.C. 472, 482, 20 S.E.2d 825, 832 (1942) (teacher pensions); *Wiggs v. Edgecombe Cty.*, 361 N.C. 318, 323-24, 643 S.E.2d 904, 908 (2007) (supplemental pension payments). Two others are decisions by the Court of Appeals regarding local government benefits, both of which involved *current* compensation. In *Pritchard v. Elizabeth City*, the Court addressed vacation pay that had been already earned and for which employees had been provided individual account statements, "signed by the city manager," showing the "monetary value" of that "compensation." 81 N.C. App. 543, 546, 553, 344 S.E.2d 821, 823, 826-27 (1986). In *Bolick v. County of Caldwell*, the Court addressed severance pay, which was calculated entirely on the basis of the employee's salary. 182 N.C. App. 95, 641 S.E.2d 386 (2007). None of these cases address health benefits, let alone benefits that were subject to a right-to-amend clause and that had been regularly amended for decades.

until a later time," the career-status law simply contemplates *future* benefits that the General Assembly can withdraw at its discretion.[19] *Id.*; *see also Adams v. State*, 248 N.C. App. 463, 469-70, 790 S.E.2d 339, 344 (2016) (rejecting statutory contract claim arising outside pension context).

In sum, this Court has recognized statutory retirement benefits as contractual only when they represent a deferred part of an employee's salary. Because the health-benefit statute lacks this feature, it is not a contract.

2. Health benefits are not contractual because they are not deferred compensation.

Comparing the pension and health-benefit statutes makes clear that, unlike pensions, health benefits are not deferred compensation. Pensions are structured to serve as a direct deferral of an employee's salary. Health benefits, by contrast, operate as a general welfare benefit. Several features of the statute make this distinction clear.

First, health benefits are explicitly excluded from the pension statute's definition of "compensation." The statute states that "'compensation' shall

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[19] The Court in *NCAE* went on to hold that teachers' express, nonstatutory contracts with school districts incorporated the career-status law. 368 N.C. at 789, 786 S.E.2d at 264. For many reasons, that reasoning does not apply here. *See infra* pp 71-72. For example, unlike in *NCAE*, the benefit statute never authorized the State Health Plan to offer contractual health benefits.

not include . . . [e]mployer-provided . . . benefits such as health . . . plans." N.C. Gen. Stat. § 135-1(7a)(b). The statute further makes clear that when an employer gives employees money to help them "purchase additional benefits such as health . . . plans," even that money is not compensation. *Id.* Thus, under the pension statute's plain text, health benefits cannot be deferred compensation. [20]

Second, pensions are based on an employee's salary and length of service, whereas health benefits are available on equal terms to all

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[20] The pension statute's express exclusion of health benefits shows the folly of plaintiffs' claim that health and pension benefits are an integrated system merely because they are both codified in "Chapter 135 of the General Statutes." Br. 51. Indeed, the benefit statute's key clauses—the "undertaking" clause and the "right to amend" clause, are both explicitly limited to "this Article." N.C. Gen. Stat. §§ 135-48.2(a), -48.3. The article in question is Article 3B of chapter 135, which discusses only health benefits.

Article 3B has historically addressed health benefits beyond state employees. For example, when the General Assembly created a program to provide health coverage for low-income children, it housed that program in Article 3B. *See* Act of Apr. 30, 1998, ch. 1ES, § 1, 1997 N.C. Sess. Laws 1.

In addition, Chapter 135 also includes an entire article on federal Social Security benefits, which the U.S. Supreme Court has held are not contractual in part because the Social Security Act contains a right-to-amend clause. *See Flemming v. Nestor*, 363 U.S. 603, 611, 617 (1960) (social security is a "noncontractual government benefit" in part because "Congress included in the original Act . . . a clause expressly reserving to it 'the right to alter, amend, or repeal any provision' of the Act.").

employees. The government defers paying part of its employees' salaries and then repays those salaries at regular intervals after the employees retire. The State calculates a retiree's pension under a formula that considers, among other factors, her salary and years of service. N.C. Gen. Stat. § 135-5; *Bailey*, 348 N.C. at 146, 500 S.E.2d at 63 ("the employee generally is guaranteed a percentage payment at retirement based upon years of service"). Because "the amount of benefits to be received in retirement is based and computed upon the individual's salary and years of service," pensions effectively constitute "retirement salary." *Davis v. Mich. Dep't of Treasury*, 489 U.S. 803, 808 (1989).

Pension payments are also distributed like salary: They entail "periodic payments to retired employees" in exchange for work performed during the employee's working years. *Watkins v. Watkins*, 228 N.C. App. 548, 553, 746 S.E.2d 394, 398 (2013). Indeed, an employee can precisely calculate the monthly pension that she will receive when she retires.[21] For these reasons, a "pension is a quantifiable, legally enforceable property interest." *Jones v. Jones*, 121 N.C. App. 523, 524, 466 S.E.2d 342, 343 (1996).

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[21] *See* State Treasurer of N.C., *Retirement Benefit Estimator*, https://orbit.myncretirement.com/Common/PublicCreateEstimate.

Health benefits, by contrast, do not vary based on an employee's salary or years of service. At all times relevant here, all eligible employees and retirees had access to the same health plans, regardless of seniority or pay. (Doc. Ex. 284-99) And state employees who decline health benefits do not receive any additional salary.

Health benefits are thus like any other statutory benefit that the State makes available to its employees. *See, e.g.*, N.C. Gen. Stat. § 126-3(b)(2) (training programs). Like these other benefits, and unlike pension payments, "the value of [a health benefit] cannot be quantified" in advance. *Kirk v. Dep't of Correction*, 121 N.C. App. 129, 136, 465 S.E.2d 301, 306 (1995). The value of a health benefit is based on the frequency and manner in which an individual utilizes the health care system, as well as a number of other "unstable variables," including "changes in medical practice and technology" and "increases in the costs of treatment," that "prevent accurate predictions of future needs and costs." *Wise v. El Paso Natural Gas Co.*, 986 F.2d 929, 935 (5th Cir. 1993).

In sum, pensions are . . . 'deferred compensation,'" because they are substitute for salary: "without the pension it is assumed that the employee would have received a commensurately greater salary during his working

years." *Seifert v. Seifert*, 82 N.C. App. 329, 333, 346 S.E.2d 504, 506 (1986) *aff'd*, 319 N.C. 367, 354 S.E.2d 506 (1987). Health benefits are not deferred compensation, however, because "there is no evidence that the State's contributions to [public employees'] health insurance were made in lieu of wages." *Kirk*, 121 N.C. App. at 136, 465 S.E.2d at 306.

Third, pensions and health benefits diverge in another fundamental way: Pensions are mandatory, but health benefits are optional. All state employees are required to participate in the State pension plan. *See* N.C. Gen. Stat. §§ 135-5, 135-8. Not only are employees automatically enrolled in the pension system, they have no right to opt out of it. *See id.* The pension statute provides that a mandatory contribution "shall" be automatically deducted from "each and every" paycheck issued to a state employee. *Id.* § 135-8(f)(1)(a). In exchange, when the employee retires, she "shall receive" pension benefits according to a fixed statutory formula. *Id.* § 135-5(b)-(b19). Indeed, to describe the benefits owed to retirees under the pension formula, the pension statute uses the word "shall" 146 times. *See id.*

Health benefits, by contrast, are completely optional. No employee or retiree is required to enroll in the State Health Plan. (Doc. Ex. 1183, 2554-55) Many employees and retirees decline to enroll in the State Health Plan and

instead obtain health benefits in another way, often through a family member's insurance. (Doc. Ex. 1450) These employees do not receive any additional salary to offset their forgone state health benefits. *See Kirk*, 121 N.C. App. at 136, 465 S.E.2d at 306.

The benefit statute further confirms that health benefits are optional. For example, the statute defines a "[p]lan member" as someone "who is eligible *and* currently enrolled in the Plan." N.C. Gen. Stat. § 135-48.1(15) (emphasis added). And in contrast to the mandatory payroll deductions for pensions, the benefit statute merely provides that a "[p]ayroll deduction shall be *available* for coverage under the Plan." *Id.* § 135-48.2(b) (emphasis added). In sum, the optional nature of health benefits distinguishes them from pensions, which are provided through a mandatory deferred-compensation system.

Finally, pensions are subject to explicit legal protections that health benefits lack. Because pensions are deferred compensation, the North Carolina Constitution makes the State's pension fund "inviolab[le]." N.C. Const. art. V, § 6(2). To enforce this constitutional command, the General Assembly has enacted multiple statutory protections for pensions. For example, the State must maintain adequate reserves to pay pension benefits.

N.C. Gen. Stat. § 135-12. In addition, employees have a nonforfeitable right to their individual contributions to the pension fund. *Id.* § 135-18.6. A former state employee may request, and will receive, a return of their contributions. *Id.* § 135-5(f). Likewise, the General Assembly is statutorily barred from altering the terms of pension benefits, except to the extent necessary to comply with federal law. *See id.* §§ 128-38, 135-18.4. Health benefits have none of these legal protections.

Thus, health benefits lack the unique features that have led this Court to treat pensions as contractually guaranteed. The Court of Appeals faithfully applied this Court's precedents when it declined to extend statutory-contract doctrine beyond the pension context.[22]

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[22] The conclusion that health benefits are not deferred compensation aligns with the holdings of other courts. For example, the U.S. Supreme Court has held that "retiree health care benefits are not a form of deferred compensation." *M&G*, 574 U.S. at 441. The Court expressly rejected the conclusion that "retiree health benefits are 'a form of delayed compensation or reward for past services,' like a pension." *CNH Industrial*, 138 S. Ct. at 764.

Likewise, courts in several states have agreed that pension payments are protected by statutory contracts, but health benefits are not. For example, the highest court of New York has held that pensions are contractual because they form "part of the compensation which [employees] accept" when they agree to work for the State. *Lippman v. Bd. of. Educ.*, 487

D. Nonstatutory materials cannot establish a contract in the circumstances here.

To try to overcome the above precedent, plaintiffs principally rely on nonstatutory materials. Those documents cannot create a contract here for two independent reasons.

First, the General Assembly has not authorized the State Health Plan (or any other state agency or official) to make contracts with state employees for lifetime health coverage. Thus, any supposed nonstatutory contract is invalid and unenforceable.

N.E.2d 897, 899 (N.Y. 1985). By contrast, the court held, retirees' health insurance premiums are *not* contractual, because those payments do not stem from deferred income. *Id.*; *see also, e.g.*, *Studier v. Mich. Pub. Sch. Emps.' Ret. Bd.*, 698 N.W.2d 350, 358-64 (Mich. 2005); *Davis v. Wilson Cty.*, 70 S.W.3d 724, 727-28 (Tenn. 2002); *Colo. Springs Fire Fighters Ass'n v. City of Colo. Springs*, 784 P.2d 766, 771-74 (Colo. 1989). More recently, the California Supreme Court has explained, in a unanimous opinion, that pensions are deferred compensation because their "magnitude is roughly proportional to the time of that service." *Cal. Fire Local 2881 v. Cal. Pub. Emps. Ret. Sys.*, 435 P.3d 433, 448 (Cal. 2019). "Just as each month of public service earns an employee a month's cash compensation, it also earns him or her a slightly greater benefit upon retirement." *Id.* Because "health insurance benefits" lack these features, they are merely an "optional benefit" that is not "entitled to protection under the contract clause." *Id.* at 449.

Plaintiffs and their amici cite decisions from other states. Br. 64-65; AARP Br. 4-8. As the Court of Appeals recognized, those states are distinct because their constitutions, unlike ours, make retiree benefits contractual. *Lake*, 825 S.E.2d at 652-53.

Second, the nonstatutory materials that plaintiffs cite do not support the claimed contract. For example, most of the cited materials discuss pensions, not health benefits. And the nonstatutory materials issued by the State Health Plan affirmatively refute any contract here.

1. The claimed contract lacks the necessary statutory authorization.

A contract with the State is valid only if it is "enter[ed] . . . through an agent of the State expressly authorized by law to enter into such contract." *Whitfield v. Gilchrist,* 348 N.C. 39, 42-43, 497 S.E.2d 412, 415 (1998); *accord Home Telephone*, 211 U.S. at 273. Applying this principle, this Court has invalidated a city's agreement to give its former employees separation payments. That agreement was void because no "statute authoriz[ed the city] to enter a contract for" that benefit. *Bowers v. City of High Point*, 339 N.C. 413, 423, 451 S.E.2d 284, 291 (1994).

In the absence of explicit statutory authority, even cabinet-level officials are barred from making contracts for employment-related benefits. *McCaskill*, 204 N.C. App. at 396, 695 S.E.2d at 125. In *McCaskill*, a cabinet member purported to enter a contract that would grant retirement benefits to a state employee. *Id.* at 376-77, 695 S.E.2d at 113. This Court held that "because the Secretary of the Department of Health and Human Services

lacked authority to sign the settlement agreement binding the State Retirement System," the contract was "unenforceable." As the Court of Appeals had explained, any other conclusion would allow agencies to enter contracts "without regard to their impact on other agencies or on state government at large." 204 N.C. App. at 376-77, 695 S.E.2d at 113.

Thus, just as the Department of Health and Human Services cannot enter a contract binding the Retirement System, the Retirement System cannot enter into contracts that bind the State Health Plan—which was housed in an entirely different agency at all times relevant here.

Plaintiffs do not dispute these points of law. Nor do they claim that the General Assembly has ever authorized the State Health Plan, or any other agency or official, to make contracts for health benefits.

Instead, plaintiffs merely note that North Carolina courts have sometimes cited written and oral representations in decisions that recognize statutory contracts. Br. 26. But those cases confirm that plaintiffs cannot weave a contract out of nonstatutory materials alone.

- In *Bailey*, the contract was "statutorily created." 348 N.C. at 146, 500 S.E.2d at 63; *see NCAE*, 368 N.C. at 788, 786 S.E.2d at 263 (The contracts in *Bailey* were "created by the statutes at issue.").

- In *Bolick*, the Court of Appeals held that a county ordinance created contract rights. 182 N.C. App. at 99, 641 S.E.2d at 389 ("[T]he ordinance at issue here turns this action into one based on contract."). The court discussed nonstatutory materials only because the county argued such materials showed a contract had *not* been formed, an argument the court rejected. *Id.*
- Similarly, in *Stone v. State*, the Court of Appeals relied only on statutes to hold that a contract had been formed. 191 N.C. App. 402, 412-14, 664 S.E.2d 32, 39-40 (2008) ("Upon review of these statutes, it is clear that Plaintiffs had a contractual right."). The court discussed nonstatutory materials only to amplify that statute-based holding. *Id.* at 414, 664 S.E.2d at 40.
- In *NCAE*, the contracts were specifically authorized by statute. The General Assembly had granted local school boards explicit "authority to grant teacher[s] career status" if the teachers had satisfied certain conditions. 368 N.C. at 780, 786 S.E.2d at 258;

see Pritchard, 81 N.C. App. at 552, 344 S.E.2d at 826 (same, relying on statutory grant of contracting authority to cities).[23]

Here, no statute authorizes anyone to make the contract that plaintiffs allege. The benefit statute gives the State Health Plan limited contracting authority, but this case falls outside that limited authority. Under the statute, any contracts worth more than $500,000 require the approval of the Plan's Board of Trustees. N.C. Gen. Stat. § 135-48.33(a). The contract alleged here far exceeds $500,000 and was not approved by the Board of Trustees.

When a statute delegates only limited authority to an agency, that narrow delegation "is strong evidence that the legislature did not intend" to delegate other, unlisted powers as well. *Bowers*, 339 N.C. at 419, 451 S.E.2d at

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[23] For this reason, *NCAE*'s holding that the career-status law was incorporated into teachers' contracts with local school boards does not apply here. Here, unlike in *NCAE*, the benefit statute does not authorize express contracts with state employees. *See NCAE*, 368 N.C. at 788, 786 S.E.2d at 264 (stating that the career-status law affirmatively "contemplates the creation of individual contracts" whose terms depend on the statute); *see also Adair*, 284 N.C. at 538, 541, 201 S.E.2d at 908, 910 (a statute is implicitly incorporated into a contract only when the statute "affect[ed] the validity, construction and enforcement of [the] contract at the time of its making").

Moreover, even if the benefit statute were incorporated into plaintiffs' ordinary employment contracts, those contracts would incorporate the whole statute, including the right-to-amend provision. *See supra* pp 44-50 (discussing this provision). On that theory, when the General Assembly amended the benefit statute, it was exercising an express contractual right.

288-89. Here, the contracting limits in the benefit statute show that the General Assembly never intended to authorize state agencies to guarantee a fixed level of health benefits for state retirees—let alone authorize agencies to make such a guarantee through stray references in employee handbooks.

2. The cited nonstatutory materials do not establish a contract for lifetime health benefits.

Even if nonstatutory materials could theoretically form the contract asserted here, the materials cited by plaintiffs fail to do so.

Nearly all of the materials that plaintiffs cite were issued by agencies other than the one that actually provides health benefits—the State Health Plan. *See* Br. 38-45. Plaintiffs extensively cite materials issued by the Teachers' and State Employees' Retirement System, the state agency that administers pensions. N.C. Gen. Stat. §§ 135-1(22), -2; *see* Doc. Ex. 10684 (Treasurer Janet Cowell: "The retirement system is the pension system.") The Retirement System does not provide health benefits. Indeed, from 1982 until 2012 (after this lawsuit was filed), the Retirement System and the State Health Plan were completely independent agencies with no overlapping regulatory structure. Thus, when materials from that period refer generically to "[t]he benefits provided by the State Retirement System," they are referring to pension benefits. (Doc. Ex. 3849); *see* App. 1-5.

This administrative separateness makes sense: Pensions, by their very nature, are for retirees alone. The State Health Plan, by contrast, provides health coverage for *current* state employees and their families, in addition to retirees. Indeed, until after all of the plaintiffs had retired, the State Health Plan had always offered uniform coverage to both current and retired state employees.

Although some Retirement System materials do mention health benefits, those references confirm that health benefits fall outside the Retirement System's purview. For example, a 1988 handbook mentioned health benefits in only three sentences, after twenty-six pages devoted exclusively to pensions. (Doc. Ex. 3849-62) The reference to health benefits appeared alongside a brief discussion of the federal Social Security and Medicare programs, which the Retirement System also does not administer. (Doc. Ex. 3862) By treating health benefits as a side topic on par with *federal* benefit programs, the handbook confirmed that health benefits were outside the Retirement System.

In another, more recent example, the Retirement System's 2008 handbook informed plaintiffs that they "become vested in the Retirement System" after five years of state government service. By contrast, it states

only that "[y]ou may also be *eligible* for retiree health coverage as described on page 20" of the handbook. (Doc. Ex. 4340 (emphasis added)) On page 20, the handbook tells retirees to "please contact the State Health Plan . . . [f]or more information." (Doc. Ex. 4356) The Retirement System handbooks also describe pensions as "continu[ing] for the rest of [one's] life," but notably do not use similar language to describe health benefits. (Doc. Ex. 4344, 4356)

This understanding of the Retirement System handbooks was confirmed by former Treasurer Janet Cowell in her deposition. For example, she testified that the handbooks' description of the "retirement benefit" as deferred compensation was "referring to the state pension." (Doc. Ex. 10671-72; *see also* Doc. Ex. 10679-80) She testified further that where the handbook indicated that employees may become "vested in the retirement system" and receive "lifetime monthly retirement benefits," the handbook was describing the "pension plan," not health benefits. (Doc. Ex. 10681-82)

Even further afield, many of the cited materials were prepared not by the State but by government contractors. *E.g.*, Br. 43 (citing actuarial reports). Plaintiffs do not claim, nor could they, that government contractors were authorized to make contract offers that bind the State.

Similarly, many of the materials cited by plaintiffs were prepared for internal government use only. *E.g.*, Br. 45-46 (citing training manuals and a presentation). Because plaintiffs did not see these internal materials until this lawsuit, these materials cannot be contract offers. *See Howe v. Links Club Condo. Ass'n*, 263 N.C. App. 130, 139, 823 S.E.2d 439, 448 (2018) ("In order for a valid contract to exist between two parties, . . . '[t]he offer must be communicated.'") (quoting *Yeager v. Dobbins*, 252 N.C. 824, 828, 114 S.E.2d 820, 823 (1960)).

More importantly, the most authoritative documents in the record—the booklets produced by the State Health Plan that comprehensively summarized plan benefits—make clear that they cannot be the source of any contract rights. (*E.g.*, Doc. Ex. 1281, 1300, 1324, 1349, 1377, 1407, 1440) They did so by repeatedly warning that "[t]he North Carolina General Assembly determines benefits for the State Health Plan and has the authority to change benefits." (*E.g.,* Doc. Ex. 1486) They further warned that benefits could be reduced in the future—and they communicated specific reductions in benefits on an ongoing basis. (*See* Doc. Ex. 1240, 1280)

Plaintiffs quote the booklets' statement that retirees become "eligible" or "qualify" to receive health benefits "under the Plan" by accruing five years

of service. Br. 41; *see* Doc. Ex. 1305, 1329. That guarded language, however, is nothing like a promise of a fixed level of health benefits for retirees' whole lives. At most, the booklets acknowledged that retirees are eligible to enroll in the same plan that state employees receive—a plan with benefits that evolve from year to year.

Plaintiffs only other attempt to tease support from the booklets produced by the State Health Plan quotes one booklet that states "[t]he Plan offers the following contracts: 1. Employee Only—covers only the employee or retiree." Br. 42. This language does not show a contract of the kind that plaintiffs allege. The contract being described was an offer to both current "employee[s] and retiree[s]" alike to enroll in an *annual* health plan, under the benefit terms offered for *that plan year*. Nothing in any State Health Plan booklet suggests that the plan ever offered a *lifetime* contract for premium-free benefits, let alone lifetime benefits at a fixed level.

These are only a few of the fatal deficiencies in plaintiffs' record citations. An appendix to this brief describes in more detail the reasons none of the record documents that plaintiffs cite can serve as evidence of the asserted contract. *See* App. 1-17. In total, the record here hardly evidences the type of "multiple unequivocal written statements in official publications

and employee handbooks" that this Court discussed in *Bailey*, 348 N.C. at 138-39, 500 S.E.2d at 58-59. Thus, plaintiffs' attempt to weave a contract from a disparate patchwork of documents—most of which did *not even discuss health benefits*—fails as a matter of fact.

E. Even if plaintiffs could show the existence of some statutory or implied contract, it would not have the terms that plaintiffs propose.

As shown above, the benefit statute does not create a contract. However, if there were a contract here, that contract could at most give plaintiffs the right to enroll in the State Health Plan in its evolving form. Plaintiffs, however, assert a remarkably specific contractual guarantee: a lifetime, premium-free health plan with an actuarial value equivalent to the 80/20 PPO plan as it existed in September 2011. Nothing in the law or the record creates a contract with those terms.

1. The most any contract would provide is the right to enroll in the State Health Plan.

Plaintiffs' proposed contract terms have no support in the text of the benefit statute. The only statutory text that even approaches the language of contract is the "undertaking" clause, but that clause is limited in two ways. *See also supra* p 42 (explaining that these limitations prevent contract formation in the first place). First, health benefits are available only "in

accordance with the [statute's] terms." N.C. Gen. Stat. § 135-48.2. Second, benefits are subject to the legislature's reserved right to amend the statute. *Id.* § 135-48.3. Thus, at most, the statute promises only the right to enroll in a state health plan of some kind—a plan that is subject to change or repeal.[24] Nothing in the statute remotely supports plaintiffs' claim to a health plan with a fixed value. *See National Railroad*, 470 U.S. at 466 (warning courts to "proceed cautiously in defining the contours of any contractual obligation").

2. The State Health Plan has never been designed to achieve a minimum actuarial value.

In their complaint, plaintiffs claim the right to an "80/20" plan. (R p 15) But plaintiffs' theory for the meaning of this term has fluctuated widely as this litigation has progressed. None of plaintiffs' theories have any support in the benefit statute or the record of this case.

Plaintiffs' references in the complaint to an "80/20 plan" and an "80/20 health insurance benefit" refer to coinsurance. (R p 15, 17) Plaintiffs do not

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[24] Other courts have held that governments did not guarantee retirees lifetime access to a specific set of benefits, but promised only eligibility for whatever health plan was offered to current employees. *Sappington v. Orange Unified Sch. Dist.*, 119 Cal. App. 4th 949 (Cal. Ct. App. 2004); *Anderson v. Town of Smithfield*, 2005 R.I. Super. LEXIS 181 (2005).

dispute that this is the only manner in which terms like "80/20" have ever appeared in the benefit statute or materials distributed by the State Health Plan.[25] Their alleged contract thus asserts a right to a premium-free plan with a 20% coinsurance rate.

However, there's no evidence that a particular coinsurance rate was ever set in stone. Indeed, although the 1982 law originally set coinsurance at 5%, the General Assembly increased the coinsurance rate twice within the next few years. *See supra* p 14. These changes were immediately communicated to plan members, along with warnings that further changes might be necessary to keep the plan solvent. *See supra* pp 20-21. Given these immediate increases, plan members could have no basis to believe that they had a contract right to a health plan with a particular level of coinsurance. In any event, plaintiffs cannot explain why the alleged contract would include a coinsurance term that was introduced in 1991, nine years after the

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[25] N.C. Gen. Stat. § 135-45.1(18) (2008) (repealed 2011) ("80/20 coinsurance"); *id.* § 135-40.4(a) (1998) (repealed 2007) ("coinsurance of 80%/20%"); *see also, e.g.*, Doc. Ex. 53 ("the terms 70/30, 80/20 and 90/10 . . . are references to the coinsurance rates for the specific plans in specific years"); Doc. Ex. 4746-50 (the "80/20 PPO Plan" has a "Plan Coinsurance" of "20%" whereas the "70/30 PPO Plan" has a "Plan Coinsurance" of "30%").

benefit statute was codified in 1982, or why the contract would allow the legislature to increase the rate from 5% to 20%, but no higher.

Perhaps sensing these weaknesses, plaintiffs changed their theory. They later asserted that "80/20" referred to a plan with an 80% actuarial value. (Doc. Ex. 470, 475, R p 357) But there is no evidence that plaintiffs were guaranteed a health plan with a certain actuarial value. In the forty-six-year history of the State Health Plan, the General Assembly has never defined the State's health benefits by actuarial value. Nor can plaintiffs cite a single instance of the State using the term "80/20" to refer to actuarial value. And the record shows that the actuarial values of the State's health plans have routinely fluctuated—and often not reached 80%. (*See* Doc. Ex. 132) For example, the 2008 version of the standard premium-free Major Medical Plan was only 75%. (Doc. Ex. 132)

Likewise, nothing in the record suggests that the State Health Plan ever used actuarial values to define plan benefits. (Doc. Ex. 11565-69) For example, the Plan's benefit booklets never listed the actuarial values of its health plans, even though they listed the Plan's coinsurance rates and other financial terms. (*E.g.*, Doc. Ex. 2678-81, 2691. 2737) And plaintiffs can point

to nothing to show that they even *knew* the Plan's actuarial values until this lawsuit. (*See, e.g.*, Doc. Ex. 6104:17-23, 6530:21-6531:9)

None of these evidentiary gaps should come as a surprise. Unlike coinsurance, actuarial value is not a term of health coverage. Instead, it is a financial accounting metric that, when applied to health plans, seeks to "approximat[e] the actual average spending by a wide range of consumers in a standard population."[26] Actuarial values are forward-looking statistical estimates of the percentage of total health costs that a plan is expected to cover. The quality of these estimates depends on a model's underlying assumptions, among many other factors. For example, an actuary must estimate how many plan members will utilize certain kinds of services.[27]

Given these problems, plaintiffs abandoned their 80% actuarial-value theory. For example, they now admit that "actuarial value is not itself a term of the contract" and that ratios like 80/20 refer only to coinsurance. Br. 49.

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[26] Ctrs. For Medicare & Medicaid Servs., Dep't of Health & Human Servs., *Final 2020 Actuarial Value Calculator Methodology* (Mar. 19, 2019).

[27] Unlike the benefit statute, the federal Affordable Care Act explicitly categorizes health plans by actuarial value. For example, a "gold plan" has an actuarial value of 80 percent. 42 U.S.C. § 18022(d). Because actuarial values are estimates, federal rules establish an allowable "de minimus" variation of "-4/+2 percentage points." Thus, health plan with actuarial values ranging from 76% to 82% constitute "gold plans" under federal law. *Id.*

However, plaintiffs still claim that they have a contract right to health benefits with a fixed value. They now define that value as a plan that is "actuarially equivalent" to the 80/20 PPO plan as of September 2011. Br. 65.

This new theory suffers from the same lack of evidence as the now-abandoned 80%-actuarial-value theory. After all, plaintiffs' only measure of equivalence is the actuarial value of the State Health Plan. *See id.* Moreover, like plaintiffs' coinsurance theory, this new theory cannot explain why the contract would lock benefits on an arbitrary date. For example, plaintiffs cannot explain why a state employee who retired in 1991 would have her contract defined by a metric that would not exist for two decades.

To try to overcome these obstacles, plaintiffs have argued that one of the current plans, the 80/20 PPO plan, is the continuation of the "regular state health plan." Br. 58. That theory finds no support in the benefit statute. The term "regular state health plan" has *never* been used by the General Assembly or the State Health Plan. For example, Mona Moon, who was then the administrator of the State Health Plan, testified that she could not recall any documents in which the Major Medical Plan was referred to by that phrase. (Doc. Ex. 11366, 11592-93)

It is true that the term was used by the *Retirement System*, a different agency. But even then, the pension agency used it only to refer to the Major Medical Plan. The record contains no evidence that *any* statute, agency, or official has ever used the term "regular state health plan" to describe the 80/20 PPO plan. Indeed, the evidence in the record shows the contrary.

For example, the Retirement System has used forms that distinguished between HMO plans and the "regular state health plan," which was used as a shorthand for the Major Medical Plan. (*E.g.*, Doc. Ex. 5670-74) Likewise, in 2006, when the Plan first began offering the PPO plans alongside the Major Medical plan, a Retirement System brochure *distinguished* between the "regular State insured plan"—again, a shorthand for the Major Medical plan—and the new PPO plans. (Doc. Ex. 4500) This distinction had ample basis. Structurally, PPO plans are fundamentally different from the Major Medical Plan. The defining feature of a PPO plan is that members pay favorable rates when they use providers in a specified network. *See supra* pp 14-15. In contrast, benefits under the Major Medical Plan generally do not vary by provider. (Doc. Ex. 1780-81)

Because of these and other differences, when the 80/20 PPO plan and the Major Medical plan were both offered, the two plans had actuarial values

that differed widely. For example, in fiscal year 2008, the actuarial value of the Major Medical Plan was 75%, but the value of the 80/20 PPO plan was 80.9%. (Doc. Ex. 132) These differences belie plaintiffs' claim that the 80/20 PPO Plan is the modern incarnation of the Major Medical Plan. After all, plaintiffs' current contract theory is based on the assertion that "a plan's actuarial value" is "[t]he most appropriate way to . . . compare the value between offered plans." R p 616; *see* Br. 65.

Meanwhile the actuarial value of the 70/30 PPO plan has historically been far closer to that of the Major Medical Plan. In 2011, for example, the 70/30 PPO plan had an actuarial values that was nearly identical to the Major Medical Plan in the year before it was terminated. (Doc. Ex. 132) Thus, under plaintiffs' own theory, the 70/30 PPO plan would be the logical continuation of the Major Medical Plan. Br. 6. In fact, a Retirement System benefits counselor testified that if a "regular state health plan" existed, it would have included the 70/30 PPO plan. (Doc. Ex. 16480)

In sum, nothing in the statute or record promises that health coverage will have specific financial terms, let alone the "80/20" term that plaintiffs' propose. Indeed, as one of the named plaintiffs conceded at his deposition,

"The whole 80/20 business comes about as a result of this lawsuit." (Doc. Ex. 8519:13-15) It has nothing to do with the terms of any contract.[28]

F. Plaintiffs' vesting arguments do not establish a contract.

Plaintiffs also claim to have a contract because they "vested" in the State Health Plan. That argument fails for numerous reasons.

First, when an employer reserves the right to amend benefits, that reservation of rights prevents any vested contract rights from forming. Here, as noted, the General Assembly has reserved the unlimited right to amend health benefits. N.C. Gen. Stat. § 135-48.3. The State Health Plan likewise informed plaintiffs when the legislature reduced benefits and warned them that further benefit reductions were likely in the future. These warnings, and the right-to-amend provision itself, came years before the 1987 amendments that clarified the five-year eligibility requirement for the health

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[28] Plaintiffs' theory that the 80/20 PPO plan and the Major Medical Plan are, despite their structural differences, both part of the "regular state health plan" appears to be an effort to evade the limitations bar. If plaintiffs had a contract right to the "regular state health plan," that right was impaired when the General Assembly repealed the Major Medical Plan in 2008. Because contract claims have a three-year limitations period, any claims based on the 2008 repeal are time-barred. *See* N.C. Gen. Stat. § 1-52(1).

benefits offered to retirees. *See supra* p 10. Thus, the statute's right-to-amend provision prevents health benefits from vesting.[29] After all, the suite of statutory benefits in which plaintiffs would have vested would *include* the right-to-amend provision. *See Simpson*, 88 N.C. App. at 223, 363 S.E.2d at 93 (when an employee vests into a statutory contract, she is entitled to the benefits *on the terms then set out* in the statute).

Second, the benefit statute never says at all—let alone explicitly—that health benefits vest. The 1987 law that plaintiffs cite says only that retirees who worked as state employees for five years are "*eligible* for group [health] benefits." 1987 N.C. Sess. Laws 2101 (emphasis added). That guarded language contrasts sharply with how statutes describe the vesting of pension

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[29] *See Elizabeth City Water & Power Co. v. Elizabeth City*, 188 N.C. 278, 291, 124 S.E. 611, 617 (1924) (Where the State reserves the right "to alter or revoke" a contract, "a law altering or revoking, or which has the effect to alter or revoke" it "cannot be regarded as one impairing the obligation of the contract"). Plaintiffs incorrectly claim that *Elizabeth City* holds that vested rights may not be limited by a right-to-amend provision. Br. 57. Instead, the Court held that when a party to a statutory contract makes *another contract* that is *based* on that statutory contract, the *third party*'s vested rights against its *counterparty* remain, even if the legislature amends the underlying statutory contract. *See Elizabeth City*, 188 N.C. at 288-91, 124 S.E. at 615-17. Tellingly, *Elizabeth City* relied on this Court's earlier decision in *State v. Cantwell*, which held that a right-to-amend provision allowed the General Assembly to override a lifetime contract with a five-year eligibility provision. *See id.* (citing 142 N.C. 604, 606-07, 55 S.E. 820, 821 (1906)).

benefits. The operative sections of the pension statute say sixty-five times that retirees "shall receive" their pension benefits, and refers to pensions as "vested" twenty times. *E.g.*, N.C. Gen. Stat. §§ 135-4(f), -5(b), (d), (r). The pension statute also says that even if the pension system is terminated, accrued pensions "shall be nonforfeitable and fully vested." *Id.* § 135-18.6.

No similar statutory language is found in the health-benefit statute. Indeed, the one time that the benefit statute uses the word "vest," it refers to pension benefits. N.C. Gen. Stat. § 135-48.41(f); *see* App. 12. And in contrast to the pension statute, the health-benefit statute explicitly contemplates that the State Health Plan and its benefits may be terminated. *Id.* § 135-48.44(h).

Third, plaintiffs' vesting theory rests on a misunderstanding of the 1987 session law on which the theory is based. That law states that, "to be eligible for group [health] benefits" during retirement, a state employee "must have completed at least five years of contributory retirement service *with an employing unit*." 1987 N.C. Sess. Laws 2101 (emphasis added). Contrary to plaintiffs' theory, this law did not create a five-year vesting period. Retirees were already required to have worked five years to be eligible for health benefits, even before the 1987 amendment. *See* N.C. Gen. Stat. §§ 135-1(a)(1) -40.2 (1986). Instead, the 1987 law was designed to close a loophole that

allowed *local government employees* who worked briefly for the State to enroll in the State Health Plan. Because all of the plaintiffs were teachers and state employees—not local government employees—none of them were affected by the 1987 statutory amendment.

This understanding of the 1987 law's limited scope was confirmed by the General Assembly's fiscal research staff, who advised that the law "was intended to stop local employees" from "transferring local service . . . to the State . . . and retiring with State paid hospital/medical benefits." (Doc. Ex. 4522) The Department of State Treasurer memorialized that interpretation of the 1987 law in a formal administrative interpretation. (Doc. Ex. 4522) This administrative interpretation has long since been implicitly ratified by the General Assembly. *See Wells v. Consol. Judicial Ret. Sys.*, 354 N.C. 313, 319, 553 S.E.2d 877, 881 (2001) ("When the legislature chooses not to amend a statutory provision that has been interpreted in a specific way, we assume it is satisfied with the administrative interpretation.").

Fourth, plaintiffs' vesting theory clashes with precedent on how vesting operates for statutory contracts. Under established precedent, when a vesting scheme establishes a statutory contract right, the contract guarantees plaintiffs a "retirement plan [on the] terms [that] existed at the

moment their retirement rights became vested." *Simpson*, 88 N.C. App. at 224, 363 S.E. at 94. Thus, state employees are contractually guaranteed to receive pension benefits according to the specific statutory formula that was in place when they reached five years of service. *Id.* This means that different state employees are subject to different statutory formulas to calculate their pensions.[30]

Applying this standard here (and even putting aside that here plaintiffs would have vested into a contract with the right-to-amend provision), different plaintiffs would have vested into numerous different health plans, spanning many decades. In the health care context, guaranteeing different suites of health benefits would create chaos—as benefits are amended frequently, based on improvements in medicine, among other factors. It should therefore come as little surprise that plaintiffs seek to depart from this Court's prior vesting precedents by claiming that they all vested into a single, uniform plan—no matter when individuals allegedly vested.

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[30] Because pensions are based on mathematical formulas that result in a lump-sum payout per month, providing different cohorts with different benefit levels is relatively easy to administer. *See* N.C. Gen. Stat. § 135-5 (specifying different benefit formulas based on date of retirement).

Fifth, to the extent plaintiffs rely on stray references to "vesting" in the record and deposition testimony, that reliance is misplaced. As the California Supreme Court recently explained, these kinds of vesting arguments conflate the distinction between the term's ordinary usage and its specialized meaning in the context of statutory contract rights. *Cal. Fire*, 435 P.3d at 438 n.3. "The use of the term 'vested' is potentially confusing," because it has two meanings. *Id.* In ordinary parlance, to say something has "vested" simply means that certain eligibility criteria have been satisfied. It does not necessarily mean that something is guaranteed by contract. By contrast, the term "'vested right' . . . has come to refer to a benefit of public employment whose repeal or other divestment is constrained by the constitutional contract clause." *Id.* Accordingly, the Court held that a five-year eligibility requirement for a benefit did not mean that the benefit was contractually guaranteed. *Id.* at 437.

Similarly, for example, when former Treasurer Janet Cowell referred to health benefits as "vested" in her deposition in this case, she was using the term in its ordinary meaning: as a noncontractual eligibility requirement. Doc. Ex. 10527-28, 10585-86, 10773; *see* Br. 46.

Finally, the nonstatutory materials cited by plaintiffs do not support their vesting theory. Br. 45-46; *see* App. 1-17. For example:

- Plaintiffs cite a *draft* bill that use the word "vest" to describe health benefits. Br. 45, 54. The actual statute that emerged from the bill, however, says nothing about vesting. N.C. Gen. Stat. § 135-48.40; *see* App. 12. "Courts can find the intent of the Legislature only in the acts which are in fact passed." *Styers v. Phillips,* 277 N.C. 460, 472-73, 178 S.E.2d 583, 591 (1971). If anything, the decision to omit "vest" from the enacted law shows that the legislature did not consider health benefits to be a vested right.
- Most of the cited materials were prepared by the Retirement System, not by the State Health Plan. *See* Br. 45-46 (citing booklets). As shown above, these materials refer only to pensions. *See supra* p 19.
- Many of the cited materials were prepared for internal government use only or by outside contractors. *See* Br. 45-46 (citing training manuals and presentations). These materials cannot possibly constitute contract offers by the government. *See supra* p 77.

Thus, even if nonstatutory materials could create a "vesting scheme," those materials do not help plaintiffs here. *But see Cal. Fire* at 454 (holding that agency materials referring to a benefit as "vested" cannot create a contract).

G. The absence of an enforceable contract defeats all of plaintiffs' claims.

To succeed on their Contract Clause claim, plaintiffs must show an enforceable contract. *NCAE*, 368 N.C. at 784, 786 S.E.2d at 261. Their failure to make this threshold showing defeats all their claims, including their takings claim. In statutory-contract cases, Contract Clause claims and takings claims rise and fall together. *See, e.g.*, *NCAE*, 368 N.C. at 792, 786 S.E.2d at 266; *Bailey*, 348 N.C. at 153-56, 500 S.E.2d at 67-69. Here, plaintiffs have never argued that their takings claim can succeed independently. To the contrary, the only property interests that plaintiffs identify are their alleged contract rights under the benefit statute. Br. 71. Because plaintiffs have not shown that they have a contract at all, their takings claim fails.[31]

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[31] Plaintiffs' amici also raise other possible claims. *See* NCAE Br. 12-15 (discussing the fruits-of-the-labor clause). But none of those claims have ever been raised by plaintiffs.

II. Plaintiffs' Claims Fail the Remaining Elements of the Contract Clause Test.

Even if plaintiffs had shown an enforceable contract, their claim would still fail on the remaining parts of the Contract Clause test. They cannot show either that the State substantially impaired any alleged contract or that the State's actions were not justified by a legitimate public purpose.

A. Plaintiffs have not shown that any contract impairment was substantial.

"[N]ot all [contract] impairments are substantial for Contract Clause purposes." *Baltimore Teachers Union v. Mayor of Baltimore*, 6 F.3d 1012, 1017 (4th Cir. 1993). Here, even if plaintiffs had the contract that they now allege—a contract for a premium-free health plan that is actuarially equivalent to the "regular state health plan"—the State did not substantially impair such a contract. That is the case for two reasons.

First, the State has offered health plans that met the alleged terms, and any impairment of such a contract was minimal, not substantial.

Second, any changes to such a contract did not disrupt plaintiffs' reasonable expectations.

1. The State has complied with the alleged contract.

For many reasons, the State has not impaired the alleged contract at all, let alone substantially.

First, over 75% of the plaintiff class—a class that consists entirely of retirees—is eligible to enroll in Medicare. (Doc. Ex. 108) For these class members, there is no dispute that the State offers health benefits with the allegedly required terms. The 70/30 PPO plan is, and always has been, premium-free for retirees. Moreover, it is undisputed that the 70/30 PPO plan, combined with Medicare, offers benefits with an actuarial value over 90%, a figure that far exceeds the alleged contract value. (Doc. Ex. 132, 1098) Thus, for the large majority of the plaintiff class, the State has complied with the alleged contract.[32]

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[32] Nearly all Americans over age 65 receive at least some Medicare benefits premium-free. *See* Ctrs. for Medicare & Medicaid Servs., *2018 Medicare Fact Sheet* (Nov. 17, 2017) ("About 99 percent of Medicare beneficiaries do not have a Part A premium.").

Given these facts, the AARP's concerns about the well-being of "households headed by those 65 or older" are not implicated here. AARP Br. 9. No matter the outcome of this case, health benefits for retirees over 65 will remain the same. The only persons affected by the trial court's order are: (1) retired state employees and teachers, (2) who are under 65.

Moreover, since at least 2014, the State has also offered other health plans that would comply with plaintiffs' alleged contract. For Medicare-eligible retirees, the State has offered Medicare Advantage plans that do not charge a premium and that have an actuarial value that exceeds the value of the September 2011 80/20 PPO plan. (Doc. Ex. 132) Even the trial court held that these plans comply with the alleged contract. (R p 616) For non-Medicare-eligible retirees—i.e., those retirees under age 65—the State offered the Consumer-Directed Health Plan, which was also premium-free and had an actuarial value that complies with the alleged contract.[33] (Doc. Ex. 104, 114)

Thus, the record shows that the State has offered most plaintiffs health benefits that comply with the alleged contract for the entire relevant period. The State offered *all* plaintiffs these benefits from at least 2014 until 2017.

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[33] The Consumer-Directed Health Plan did not charge a premium if the member completed certain wellness activities. As plaintiffs themselves testified, these activities involved "very minimal" effort. (Doc. Ex. 8087-88) They included selecting a primary-care doctor and completing a survey. (Doc. Ex. 104) Over 95% of enrollees in the plan completed all three activities and thus did not pay a premium. (Doc. Ex. 104-05) This plan was eliminated in 2017, after the summary judgment hearing.

But even if there were some impairment of plaintiffs' alleged contract rights, that impairment was too minor to violate the Constitution. Under the Contract Clause, "[m]inimal alteration of contractual obligations" is allowed. *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 245 (1978). For this reason, a state substantially impairs a contract only if plaintiffs prove a "material breach." *Bailey*, 348 N.C. at 156, 500 S.E.2d at 69.

Here, plaintiffs did not prove that any impairment of their contract rights was material. The record shows that the premium-free 70/30 PPO plan had an actuarial value that was equivalent to the Major Medical Plan, the plan that plaintiffs call "the regular state health plan." Br. 59-60. For example, in 2008, the Major Medical Plan had an actuarial value of 75%. (Doc. Ex. 132) By comparison, in 2015, the premium-free 70/30 PPO plan (for non-Medicare members) had a higher value: 75.5%. *Id.* Even plaintiffs' own expert found that, over the five years he studied, the 70/30 PPO plan's actuarial values ranged from 77.4% to 79.9%—values that *exceed* the value of the Major Medical Plan the year before it was discontinued. (Doc. Ex. 1097) Although defendants' expert estimated that the 70/30 PPO plan had actuarial values that were slightly lower than plaintiffs' estimates, those values were always within 2% of the actuarial value of the Major Medical

Plan. (Doc. Ex. 132) Departures of this magnitude are insubstantial. For example, a variation of only 2% is considered *de minimus* under federal law. *Supra* p 84, n.27.[34]

At the very least, in light of these modest differences, a reasonable jury could conclude that the 70/30 PPO plan did not differ materially from the terms of the alleged contract. *See Snider v. Hopkins*, 314 N.C. 529, 529, 334 S.E.2d 776, 777 (1985) (whether a breach is material is usually a question of fact for a jury). Thus, the most that plaintiffs could be entitled to is a jury trial on the question of substantial impairment.

2. The State did not impair any reliance interests.

A contract impairment is substantial only when a state violates a contract right on which the plaintiffs actually relied. *City of Charleston v. Pub. Serv. Comm'n*, 57 F.3d 385, 392 (4th Cir. 1995); *see Bailey*, 348 N.C. at

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[34] Plaintiffs resist this conclusion by moving the goal posts once again. Despite their theory that the Major Medical Plan was the "regular state health plan," Br. 61, they depart from that theory to claim that the relevant difference is between the 70/30 and the 80/20 PPO plans. Br. 68. But even if that were true, the record shows that the 80/20 PPO plan's actuarial value was sometimes as low as 76%. (Doc. Ex. 132) Plaintiffs also overinflate the alleged impairment by referring to the 80/20 PPO plan's maximum monthly premium of $104.20 in 2015. Br. 68. However, 91% of retirees paid the minimum premium of only $14.20 a month. (Doc. 3515, 4565)

146, 500 S.E.2d at 63. Here, plaintiffs did not show the reliance necessary to prove a violation of the Contracts Clause.

To prove reliance, plaintiffs must show that the challenged statute disrupted their "reasonable expectations." *Energy Reserves*, 459 U.S. at 416; *accord City of Charleston*, 57 F.3d at 392. This standard cannot be satisfied when a plaintiff has notice that his alleged contract might be "subject to legislative impairment." *Baltimore Teachers Union*, 6 F.3d at 1018; *accord City of Charleston*, 57 F.3d at 392-93.

For multiple reasons, the record shows that plaintiffs knew or should have known that their health benefits could change:

- The right-to-amend provision put plaintiffs on notice that the General Assembly had the power to alter health benefits for state employees and retirees. *See supra* pp 20-21.
- The General Assembly has amended benefits almost every year since the State Health Plan was first codified. *See supra* p 13.
- Twice before, in fact, the legislature made the exact benefit change at issue here: increasing the coinsurance term for premium-free plans. *See supra* pp 14, 53.

- The State has repeatedly notified plan members of these changes, and that the General Assembly could reduce health benefits further in the future. *See supra* pp 20-21, 54-55.

Given this history, plaintiffs could not possibly have had a reasonable expectation that the General Assembly would leave the benefit statute unchanged.[35] They therefore cannot show the reasonable reliance necessary to prove substantial impairment. *See Energy Reserves*, 459 U.S. at 416.

B. The State's actions here had a legitimate public purpose.

Plaintiffs also cannot prevail on the third part of the Contract Clause test. In the unique circumstances here, the General Assembly's changes to the benefit statute served an important public purpose.

The Contract Clause allows States to impair contracts, even substantially, if the impairment is reasonable and necessary to serve an important public purpose. *NCAE*, 368 N.C. at 791, 786 S.E.2d at 265. Under this standard, "[t]he economic interests of the state may justify . . .

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[35] Plaintiffs' suggestion that they actually relied on the existence of these benefits is also belied by the record. *See* Br. 19; *see also* NCAE Br. 4. All but four of the twenty-six named plaintiffs accepted state employment even before the 1982 statute was enacted. (*See* Doc. Ex. 27-32) For these plaintiffs and similarly situated members of the plaintiff class, they could not possibly have accepted employment in reliance on benefits that did not yet exist.

interference with contracts" if "the legislation is addressed to a legitimate end and the measures taken are reasonable and appropriate to that end." *Blaisdell*, 290 U.S. at 437-38. When courts decide whether a contract impairment is sufficiently justified, they "weigh a state's interest in exercising its police power against the impairment of individual contract rights." *NCAE*, 368 N.C. at 791, 786 S.E.2d at 265; *see also Adair*, 284 N.C. at 540, 201 S.E.2d at 910 ("retroactive statutory modification of contracts . . . are permissible [when] contracts are in a business area subject to the broad regulatory police power of the State").

Here, plaintiffs have not established that the State's statutory amendments were unjustified. On the state-interest side of the equation, the changes were designed to address a massive problem: the State Health Plan's estimated thirty-five billion dollars in unfunded future outlays.[36] That figure far outstrips the State's entire budget for fiscal year 2017-2018. *See* Act of June 22, 2017, ch. 57, § 2.1, 2017 N.C. Sess. Laws 248-252. In recent years, the Plan's expenditures have risen steeply because of increases in medical costs and accelerating retirements by state employees. To avert this fiscal

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[36] Office of the State Controller, *Comprehensive Annual Financial Report, Fiscal Year Ending June 30, 2017* 41, 207 (Dec. 1, 2017).

danger, the State has made efforts to reform the Plan's funding structure. (Doc. Ex. 3655) The State's efforts include the reform that the trial court enjoined here: a modest premium for the 80/20 PPO plan. (Doc. Ex. 3645)

This modest change was a reasonable and necessary response to the State Health Plan's funding shortfall. The circumstances here parallel those in *Baltimore Teachers Union*, in which the Fourth Circuit held that reducing employee salaries was a reasonable and necessary response to address a budget crisis. 6 F.3d at 1020. Plaintiffs here argue that the State could have just raised taxes or cut other government programs, Br. 70, but that glib statement cannot defeat reasonableness and necessity. If it could, the third part of the Contracts Clause test would be meaningless.

Instead, this part of the test recognizes that statutory contracts cannot unduly constrain the legislature's authority to enact policies to advance the common good. For example, if this Court accepted plaintiffs' theory, it would dramatically constrain the General Assembly's "sovereign responsibilit[y]" to manage the public fisc in ways that benefit all North Carolinians. *Winstar*, 518 U.S. at 874. It would also "unduly discourage" the legislature "from offering [benefit] plans in the first place." *Heimeshoff v. Hartford Life & Accident Ins. Co.*, 571 U.S. 99, 108 (2013); *see supra* p 53 n.16.

Finally, the most that plaintiffs could be entitled to is a remand for further fact-finding on the third part of the Contract Clause test. Because of the fact-intensive nature of the balancing analysis at this stage, it can require a full evidentiary presentation at trial. *See Simpson*, 88 N.C. App. at 226, 363 S.E.2d at 95 (reversing a summary judgment and remanding for further evidentiary proceedings on whether the State's actions served an important public purpose).

CONCLUSION

Defendants respectfully request that this Court affirm the judgment of the Court of Appeals.

This 31st day of July, 2020.

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Contents of Appendix

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Responses to record documents and other evidence cited in section III of plaintiffs' brief

A. Documents from the Retirement System and other non-State Health Plan entities

Document	Record page(s)	Where cited	Reasons why the document does not support plaintiffs
TSERS, "Your Retirement Benefits" series of handbooks	Doc. Ex. 3849, 3940, 4094, 4336, 4340, 4380	Br. 39-42	• These handbooks were authored by Retirement System, which does not have authority over health benefits. • The handbooks address the "retirement benefit," which is the pension benefit, not the State Health Plan. • The handbooks refer to benefits provided by the Retirement System, which are pension benefits, not health benefits provided by the State Health Plan. • The handbooks refer to becoming "vested in the Retirement System," but use the term "eligible" when referring to "retiree health coverage."
TSERS, "Your Retirement Benefits" (2009)	Doc. Ex. 4376	Br. 42	• The handbook's reference to "life long benefits" that "are guaranteed and protected by the Constitution" immediately follows a reference to "pension plans" and precedes a reference to "Retirement System benefits." These are references to the pension benefit only, and nowhere in this passage does the handbook even allude to health benefits. • This handbook was authored by the Retirement System, which does not have authority over health benefits for retirees. • This handbook was published in 2009, after every plaintiff allegedly "vested" and after all but five had retired.
Retirement Sys. Div., "Intro. to Retirement, Vol. II" (July 2006)	Doc. 899-900	Br. 45-46; Pls.'	• There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied.

		App'x 1-2	• The term "vested" in the phrase "vested deferred" refers to being "vested in the Retirement System" not the State Health Plan. The document explicitly states this. (*See* Doc. Ex. 5664-66) • Plaintiffs' focus on the phrase "vested with the 5 years of contributing membership service in the State," Br. 46 (emphasis removed), ignores everything that precedes it. Before that phrase is used, the document details a number of aspects of the requirements for retirees to be eligible for the State Health Plan. Never in that discussion does the document use the word "vest," including in three prior references to the "five year[ ]" requirement that are on the same page to which plaintiffs refer. The context shows that the use of the term "vest" was informal and not intended to train benefits counselors that retirees had the lifelong rights for which plaintiffs are advocating. • This document was updated in 2006, after every plaintiff allegedly "vested," and after most of the plaintiffs retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract.
Retirement Sys., "Std. Op. Procedure: Health Ins. Content" (2008)	Doc. Ex. 876	Pls.' App'x 2	• As with the previous document from the same author, the reference to "vested deferred retirees" is to being vested in the Retirement System, not the State Health Plan. • There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied. • This document was generated in 2008, after every plaintiff allegedly "vested," and after all but five retired. No plaintiff could have reasonably relied on this document to form an

			understanding that the State had offered that plaintiff a contract. • The document also indicates elsewhere that only one "special group" was "entitled to free health insurance paid premiums for life," meaning that all other retirees were not. (Doc. Ex. 874, 12079-80) This "special group" consisted of spouses of retirees where the retiree died before 10/1/1986. The group is closed and includes very few living members. (Doc. Ex. 12079)
Email from B. Fuller to MEM – Membership Servs. (undated)	Doc. Ex. 901	Pls.' App'x 2	• The reference to "vesting" in this document refers to the Retirement System, not the State Health Plan. The excerpt on which plaintiffs rely refers to being "vested with 5 years of membership service to meet the eligibility to retire." "Membership service" is a parameter used by the Retirement System to determine eligibility to retire and receive a retirement benefit. *E.g.*, N.C. Gen. Stat. § 135-5(a)(1). The State Health Plan uses "contributory retirement service," not "membership service." *Id.* § 135-48.40(a). • This document appears to be an internal state email, and its contents strongly suggest that that it was generated around 2007. There is no evidence that it was sent to any plaintiff. Therefore, plaintiffs could not have reasonably relied on this document. • Plaintiffs reference that "Ret. Sys. Emails" support their position, but they cite only to this single email.
Ltr. from E. Hundley to R. Williams (Mar. 10, 2005)	Doc. 1069	Pls.' App'x 2	• This letter was not addressed to any plaintiff and there is no evidence that any plaintiff ever saw it. The letter is not signed and appears to be an internal training document (although there is no testimony to provide any context). Therefore, plaintiffs could not have reasonably relied on

			this document, particularly given that it post-dates the alleged "vesting" dates of all plaintiffs and the retirement dates of most of them. • The letter uses the term "vest" interchangeably with "eligible," and more frequently uses "eligible." • The purpose of this letter was to explain that the referenced individual had not yet fulfilled the eligibility requirements to receive health benefits as a retiree, not to comment on whether the State could change those benefits.
Univ. of N.C. Chapel Hill, "1998 Personal Benefits Statement" (for Pl. Currie)	Doc. Ex. 12925	Br. 42-43	• Contrary to plaintiffs' characterization, this document was not a "publication[ ] promulgated by Defendants." Br. 42. It is a personal benefits statement provided by UNC-CH to a single plaintiff. UNC-CH is not a defendant. • The document specifically references the "Comprehensive Major Medical Plan" as "continuing for life" and not health benefits in general. Plaintiffs are not claiming a contract right to the Comprehensive Major Medical Plan. • The document does not indicate that any lifetime benefits would be premium-free, or have a fixed level of coverage. • Despite plaintiffs' use of the term "vested" in connection with this document, the document never uses that term.

B. Documents from outside actuaries

Document	**Record page(s)**	**Where cited**	**Reasons why the document does not support plaintiffs**
Aon Consulting, Inc., "Report of the Actuary on the Postemployment Medical Benefits Valuation" (Dec. 31, 2005)	Doc. Ex. 732-66	Br. 43	• The document was authored by an actuarial consultant and not any agency of the State. It therefore cannot constitute a contract offer on behalf of the State. • There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied. • This document was generated in 2005, after every plaintiff allegedly "vested" and after most had retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered them a contract. • There is no indication in this report that the term "liability" was intended to imply an unavoidable legal debt as opposed to a debt that would be incurred based on then-current program parameters.
Segal Consulting, "Summary of GASB 43/45 OPEB Valuation As of December 31, 2012" (Oct. 11, 2013)	Doc. Ex. 1042	Br. 43	• This report was prepared by an actuarial consultant, and then submitted to a government committee. It therefore cannot constitute a contract offer on behalf of the State. Plaintiffs are incorrect to characterize the document as a "publication[ ] promulgated by Defendants." Br. 42. • There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied. • The document was generated in 2013, after every plaintiff retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract.

			• The actuary's statement that "[c]overage duration[ ]" was "[l]ifetime" does not indicate the actuary's belief that a lifetime benefit was guaranteed. The statement reflected the state of the health plan that existed at the time (and still does exist), which was that coverage under the State Health was available to eligible retirees until death.
Aon Hewitt, "OPEB Strategy Study" (Mar. 21, 2011)	Doc. Ex. 935-36, 939, 967-68	Br. 46	• This document was authored by an actuarial consultant, not by the State. It therefore cannot constitute a contract offer on behalf of the State. In addition, the document's use of the word "vested" in relation to health benefits for retirees therefore cannot, as plaintiffs argue, constitute an "admission[ ]" by "Defendants." Br. 45. • There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied. • There is no indication in this document that the use of the term "vested" was intended to refer to a legal obligation instead of referring informally to individuals who had satisfied the State Health Plan's eligibility criteria. • One of the actuaries who likely reviewed this report testified that the term "vest" in this context is synonymous with "eligible" and was not intended to suggest that the State lacked authority to change any benefits even as to individuals who are "vested." (Doc. Ex. 12281-84) • This document was generated in 2011, after every plaintiff allegedly "vested," and after all but two retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract.

Aon Hewitt, "Rep. of the Actuary on Postemployment Medical Benefits Valuation" (Sep. 28, 2011)	Doc. Ex. 1031, 1033	Pls.' App'x 2	• This document was authored by an actuarial consultant, not by the State. It therefore cannot constitute a contract offer on behalf of the State. In addition, the use of the word "vested" in relation to health benefits for retirees cannot, as plaintiffs argue, constitute an "admission[ ]" by "Defendants." Br. 45. • There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied. • There is no indication in this document that the use of the term "vested" was intended to refer to a legal obligation instead of referring informally to individuals who had satisfied the State Health Plan's eligibility criteria. • One of the actuaries who likely reviewed this report testified that the term "vest" in this context is synonymous with "eligible" and was not intended to suggest that the State lacked authority to change any benefits even as to individuals who are "vested." (Doc. Ex. 12281-84) • This document was generated in 2011, after every plaintiff allegedly "vested," and after all but one retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract.
Ltr. from K. Vieira and R. Ward to D. Soper (Oct. 19, 2006)	Doc. Ex. 902-03	Pls.' App'x 3	• This document was authored by an actuarial consultant, not by the State. It therefore cannot constitute a contract offer on behalf of the State. In addition, use of the word "vested" in relation to health benefits for retirees cannot, as plaintiffs argue, constitute an "admission[ ]" by "Defendants." Br. 45.

			• There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied. • There is no indication in this document that the use of the term "vested" was intended to refer to a legal obligation instead of referring informally to individuals who had satisfied the State Health Plan's eligibility criteria. • The author of this letter testified that the term "vest" in this context is synonymous with "eligible" and was not intended to suggest that the State lacked authority to change any benefits even as to individuals who are "vested." (Doc. Ex. 12281-84) • This document was generated in 2006, after every plaintiff allegedly "vested," and after most had retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract.
Misc. actuary charts	Doc. Ex. 928	Pls.' App'x 2	• This document is not properly considered by a court, because there was no foundation laid for it. The witness who was shown this document, when asked "What is this?," responded, "I don't know." (Doc. Ex. 12215) Also, the document is not self-authenticating. • Based on some similarities between the document and documents authored by Aon Hewitt, it is probable that the document was also generated by this outside actuary. Therefore, the document cannot constitute a contract offer on behalf of the State. For this same reason, use of the word "vested" in relation to health benefits for retirees cannot, as plaintiffs argue, constitute an "admission[ ]" by "Defendants." Br. 45.

			• This document indicates that it was printed in January 2011, after every plaintiff allegedly "vested," and after all but one had retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract. • Given the context, it is likely that the term "vested" is intended as synonymous with "eligible" and was not to suggest that the State lacked authority to change any benefits even as to individuals who are "vested."

C. Documents from the General Assembly and legislative branch entities

Document	**Record page(s)**	**Where cited**	**Reasons why the document does not support plaintiffs**
Fiscal Research Div., N.C. Gen'l Assembly, "State-Funded Health Benefit Coverage for Retired Employees" (Feb. 14, 2007)	Doc. Ex. 777	Br. 43	• There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied. • This document was authored by the fiscal research staff of the General Assembly, which does not have authority over health benefits for retirees. • The document was generated in 2007, after every plaintiff allegedly "vested," and after all but six had retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract. • The document is a discussion of a new accounting standard for certain post-employment benefits. It does not address legal requirements, which the author recognizes: "Ability to change premium contributions to current retired employees or current active employees once they retire is unknown from a legal perspective." (Doc. Ex. 815)

Fiscal Research Div., N.C. Gen'l Assembly, "Legis. Actuarial Note" (June 30, 2006); Fiscal Research Div., N.C. Gen'l Assembly, "Legis. Actuarial Note" (July 14, 2005)	Doc. Ex. 727, 4768	Br. 54-55	• There is no indication in the record that these documents were ever provided to any plaintiff and therefore they are not something on which any plaintiff could have relied. • These documents were authored by the fiscal research staff of the General Assembly, which does not have authority over health benefits for retirees. • The documents were generated in 2005 and 2006, after every plaintiff allegedly "vested," and after most had retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract. • As plaintiffs observe, the fiscal note indicates that the proposed change to the State Health Plan is prospective only. Br. 54. Nonetheless, there is no indication that the General Assembly believed it was required by law to apply the change prospectively. This was just a policy choice. • The fiscal note's observation that certain "obligations" of the State Health Plan regarding retirees will continue simply recognizes the current state of the law, which was important to understand for the purpose of the fiscal note, which was to make financial projections.
S.B. 837; Sess. L. 2006-174	—	Br. 45, 54; Pls.' App'x 1	• Although the short title appearing in a bill used the term "vest," that term was excised from the enacted law, demonstrating, if anything, that the General Assembly did not endorse that term.

N.C. Gen. Stat. 135-48.41(f)	—	Pls.' App'x 1	• Consistent with the General Assembly's other uses of the term "vest" in Chapter 135, the lone use of the word "vest" in the health plan statutes appears to refer to members who are "vested" in the Retirement System, not the State Health Plan. • This statutory subsection was a technical correction regarding funding of health benefits by certain licensing boards and associations. 1983 N.C. Sess. Laws ch. 499. It did not affect the general retiree population and was not intended as a statement regarding retirees' rights.

D. Documents from the State Health Plan

Document	**Record page(s)**	**Where cited**	**Reasons why the document does not support plaintiffs**
State Health Plan, "Summary Plan Description" (Mar. 1, 1988)	R pp 67-68	Br. 41	• This State Health Plan benefits booklet indicates how retirees "qualify for benefits under the Plan" and that the Plan was offered "at no cost to you," i.e., without a premium. Both statements were accurate in 1988 when the booklet was published, but nothing supports plaintiffs' suggestion that one was "consideration," Br. 41, for the other. • Plaintiffs' citation to a single paragraph of defendants' Answer improperly suggests that the quoted language appeared together in the 1988 State Health Plan booklet. In their Answer, defendants "[d]enied that the quoted text accurately reflect[ed] the source document" (R p 68) because the quoted language is drawn from separate parts of the 1988 State Health Plan booklet (*compare* R pp 67-68 *with* Doc. Ex. 1302, 1305), which refutes plaintiffs' suggestion of a closer tie-in between the two concepts.

State Health Plan, "Summary Plan Description" (Nov. 1989)	Doc. Ex. 1329	Br. 41	• Plaintiffs quote this State Health Plan publication as stating, "The State of North Carolina pays for coverage under the Plan . . . . Employees who retire on or after January 1, 1988, must complete at least 5 years of creditable service prior to retirement to be eligible." Br. 41. Both statements were accurate in 1989 when the booklet was published, but plaintiffs' suggestion that one was "consideration," *id.*, for the other is unwarranted. • Plaintiffs incorrectly cite for this excerpt a single page—Doc. Ex. 1329. The first sentence of the quote appears only on Doc. Ex. 1324, refuting plaintiffs' suggestion of a closer tie-in between the two concepts.
State Health Plan, "Summary Plan Description" (2004)	Doc. Ex. 1663	Br. 42	• This State Health Plan publication uses the word "contract" in reference to "offer[ing]" benefits to both "employee[s] and retiree[s]." This is an offer of current benefits to employees and retirees under the terms described in the booklet. Nothing in the publication suggests that this "offer[ ]" was to guarantee lifetime benefits to future retirees at a certain value. • The document was published in 2004, after every plaintiff allegedly "vested" and after most of them had retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract. • The first paragraph of this document, under the heading "**NOTICE**" states: "The North Carolina General Assembly determines benefits for the Plan and has the authority to change benefits" and that "[i]f any information in this booklet conflicts with North Carolina state law . . . North Carolina law . . . will prevail." (Doc. Ex. 1652)

State Health Plan, "N.C. State Health Plan Issues Report on Retiree Health Benefits" (Dec. 7, 2006)	Doc. Ex. 723	Br. 45	• Contrary to plaintiffs' contention, this document does not discuss being "vested into the RHB." Br. 45. Instead, it states that "the State Health Plan" "provide[s]" benefits to those who are "vested in the retirement system," which is the separate pension system. • Plaintiffs allege that "Press Releases" support their argument, but cite only a single press release. Br. 45. • This document was generated in 2006, after every plaintiff allegedly "vested," and after most of the plaintiffs retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract.
M. Moon, "State Health Plan Update" (Dec. 12, 2012)	Doc. Ex. 719	Br. 46	• There is no indication that this document was ever provided to any plaintiff and therefore it is not something on which any plaintiff could have relied. • The author of this document explained in an uncontradicted affidavit that she was "using the term 'vest' as a shorthand to describe members who were, at the time, eligible under state law for certain benefits from the State Health Plan." She testified further that the term "vest" is "occasionally" used this way by the Plan and its actuary. She testified also that the use of the term "vest" in this way is not intended to convey any conclusion about members' future rights. (Doc. Ex. 3503) • Plaintiffs allege that "PowerPoint Presentations" support their argument, but cite only a single such presentation. Br. 46. • This document was generated in 2012, after every plaintiff had retired. No plaintiff could have reasonably relied on this document to form an understanding that the State had offered that plaintiff a contract.

E. Deposition testimony

Document	**Record page(s)**	**Where cited**	**Reasons why the document does not support plaintiffs**
Deposition of Janet Cowell	Doc. Ex. 10585-86, 10588-89, 10697	Br. 43	• Despite plaintiffs' counsel using the word "obligation," the Treasurer described retirees as being "eligible" for benefits. • In the cited passage, far from describing health benefits for retirees as an "obligation," the Treasurer described them as "undefinable" and agreed that they were "difficult, if not impossible, to quantify." • In the cited passage, the Treasurer agreed that retirees are eligible for health care from the State "until the month they die," which is an accurate characterization of current law and does not suggest that the State has no ability to change that benefit. • Despite plaintiffs' characterization that the Treasurer "conced[ed]" that the State is "obligated to provide at least some form of health insurance to already vested retirees," Br. 43, the transcript shows that the Treasurer agreed only that retired employees were "eligible" for health benefits, as stated in the Retirement System's handbooks.
Various deposition citations	Doc. Ex. 626-30, 6574, 6806, 6864-72, 7023, 7527-31, 12694	Br. 43-44	• Despite plaintiffs' representation that these cites support that "Plaintiffs themselves relied on the promise of RHB in deciding to work for the State," Br. 43, two of the seven citations are not from depositions of a plaintiff. • Two of the five plaintiffs listed in plaintiffs' brief (Blanton and Carpenter) could not have "relied on the promise of RHB in deciding to work for the State" because they began working for the State before health benefits were being offered to any retirees. (Doc. Ex. 1148)

			• Another of the listed plaintiffs (Cooper) was hired before the State was providing retirees with health benefits that were premium-free. (Doc. Ex. 1148) • The deposition excerpts for the final two plaintiffs (Buchanan and Evans) only describe the information that each was provided when they were hired. There is no indication in the cited material that they "relied" on any of this information regarding health care "in deciding to work for the State." • Plaintiffs' expert report (referred to as the Kursh Report) is based on data from 2009-13 only. It has no relevance to plaintiffs' employment decisions because the last-hired plaintiff was hired in 1990. (Doc. Ex. 1148-50) • Mr. Wall was a state employee, but is not a plaintiff. His testimony does not show what, if anything, "the Plaintiffs *themselves* relied on . . . in deciding to work for the State." Br. 43 (emphasis added).
Deposition testimony regarding the word "vest"	Various citations	Br. 46-47 & App'x 3-6	• Despite the term "vest" appearing in the cited depositions, each deponent explained that he or she did not understand that term in relation to the State Health Plan to mean that a member was entitled to a specific level of benefits. • The Treasurer testified that being "vested" in a health benefit means only that one is "eligible" for a benefit but is not entitled to any specific benefits. (*E.g.*, Doc. Ex. 10527-28, 10585-86, 10773) • Ms. Moon testified that the term "vest" when used with respect to health benefits for retirees was not intended to imply that health benefits cannot be changed for those who have "vested." (Doc. Ex. 11302) • Mr. Trogdon testified specifically that when he used the word "vest" in relation to the State Health Plan, he did not

			mean that the "retiree health benefit cannot be changed." (Doc. Ex. 11784) • Ms. Crabtree testified that she was not aware of any documents that said that plaintiffs are vested. (Doc. Ex. 10988) Ms. Crabtree's further acknowledgment that she was "unaware of any documents that say the RHB is not vested upon completion of the eligibility requirements," App'x 5, is not, as plaintiffs' argue, an admission that "the Plaintiffs are vested into the RHB." Br. 45. • Mr. Vieira is an actuary employed by a private company hired by the State. His testimony cannot constitute an "admission," Br. 45, by the State. Regardless, he testified that the term "vest" in this context is synonymous with "eligible" and was not intended to suggest that the State lacked authority to change any benefits even as to individuals who are "vested." (Doc. Ex. 12281-84) • Ms. Spruill was one of many retirement benefits counselors employed by the Retirement System, not the State Health Plan. Her informal use of the term "vest" in a deposition cannot be construed as an admission by the State as to what benefits the State Health Plan was required to provide.

North Carolina General Statutes

Chapter 135

Article 1

Retirement System for Teachers and State Employees

§ 135-1. Definitions

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7a.

b. “Compensation” shall not include any payment, as determined by the Board of Trustees, for the reimbursement of expenses or payments for housing or any other allowances whether or not classified as salary and wages. "Compensation" includes all special pay contribution of annual leave made to a 401(a) Special Pay Plan for the benefit of an employee. Notwithstanding any other provision of this Chapter, "compensation" shall not include:

1. Supplement/allowance provided to employee to purchase additional benefits such as health, life, or disability plans;
2. Travel supplement/allowance (nonaccountable allowance plans);
3. Employer contributions to eligible deferred compensation plans;
4. Employer-provided fringe benefits (additional benefits such as health, life, or disability plans);
5. Reimbursement of uninsured medical expenses;
6. Reimbursement of business expenses;

7. Reimbursement of moving expenses;
8. Reimbursement/payment of personal expenses;
9. Incentive payments for early retirement;
10. Bonuses paid incident to retirement;
10a. Local supplementation as authorized under G.S. 7A-300.1 for Judicial Department employees;
11. Contract buyout/severance payments; and
12. Payouts for unused sick leave.

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§ 135-18.4. Reservation of power to change

The General Assembly reserves the right at any time and from time to time, and if deemed necessary or appropriate by said General Assembly in order to coordinate with any changes, in the benefit and other provisions of the Social Security Act made after January 1, 1955, to modify or amend in whole or in part any or all of the provisions of the Teachers' and State Employees' Retirement System of North Carolina.

Article 3B

State Health Plan for Teachers and State Employees

Part 1

General Provisions

§ 135-48.2. Undertaking

a) The State of North Carolina undertakes to make available a State Health Plan (hereinafter called the "Plan") exclusively for the benefit of eligible employees, eligible retired employees, and certain of their eligible dependents, which will pay benefits in accordance with the terms of this Article. The Plan shall have all the powers and privileges of a corporation and shall be known as the State Health Plan for Teachers and State Employees. The State Treasurer, Executive Administrator, and Board of Trustees shall carry out their duties and responsibilities as fiduciaries for the Plan. The Plan shall administer one or more group health plans that are comprehensive in coverage. The State Treasurer may operate group plans as a preferred provider option, or health maintenance, point-of-service, or other organizational arrangement.

(b) Payroll deduction shall be available for coverage under the Plan for subscribers able to meet the Plan's requirements for payroll deduction.

§ 135-48.3. Right to amend

The General Assembly reserves the right to alter, amend, or repeal this Article.