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

SUPREME COURT OF NORTH CAROLINA

****

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,	)	From
	)	Gaston
Plaintiffs-Appellants,	)	County
	)	COA17-1280
vs.	)	
	)	
STATE HEALTH PLAN FOR TEACHERS AND STATE EMPLOYEES, a corporation, formerly Known as the North Carolina Teachers and State Employees' Comprehensive Major Medical Plan, TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM OF NORTH CAROLINA, a corporation, BOARD OF TRUSTEES TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM OF NORTH CAROLINA, a body politic and corporate, JANET COWELL, in her official capacity as Treasurer of the State of North Carolina, and the STATE OF NORTH CAROLINA,	)	
Defendants-Appellees.	)	

****

PLAINTIFFS-APPELLANTS' REPLY BRIEF

****

INDEX

TABLE OF CASES AND AUTHORITIES

CASES

STATE STATUTES

SESSION LAWS

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

SUPREME COURT OF NORTH CAROLINA

****

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,	)	From
	)	Gaston
Plaintiffs-Appellants,	)	County
	)	COA17-1280
vs.	)	
	)	
STATE HEALTH PLAN FOR TEACHERS AND STATE EMPLOYEES, a corporation, formerly Known as the North Carolina Teachers and State Employees' Comprehensive Major Medical Plan, TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM OF NORTH CAROLINA, a corporation, BOARD OF TRUSTEES TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM OF NORTH CAROLINA, a body politic and corporate, JANET COWELL, in her official capacity as Treasurer of the State of North Carolina, and the STATE OF NORTH CAROLINA,	)	
Defendants-Appellees.		

****

PLAINTIFFS-APPELLANTS' REPLY BRIEF

****

INTRODUCTION

This Court has repeatedly held that the relationship between the State and its employees is contractual, and that employment benefits – once earned – cannot be taken away. See, e.g., Simpson v. N.C. Local Gov't Emp. Ret. Sys., 88 N.C. App. 218, 363 S.E.2d 90 (1987), aff'd per curiam, 323 N.C. 362, 373 S.E.2d 559 (1988); Bailey v. State, 348 N.C. 130, 500 S.E.2d 54 (1998) and Faulkenbury v. Teachers' & State Emp. Ret. Sys., 345 N.C. 683, 483 S.E.2d 422 (1997). When faced with this binding precedent, the Defendants substantially ignore this Court's holdings in favor of federal cases that pre-date this Court's dispositive decisions, as if this Court reached its decisions in error. This Court has also repeatedly held that the State cannot take away deferred compensation that has been earned. Faced with this unfavorable law, the Defendants claim that the Retirement Health Benefit is not deferred compensation, even though it is both deferred until retirement, and is compensation for work performed. In order to accomplish this semantic feat, they rewrite this Court's precedent, frequently replacing the term "compensation" with "salary," as if to say what this Court *really* meant to say was that only deferred *salary* was contractual. (See, e.g., Def.'s Brief at 60, 65). But that is not what this Court has said.

When faced with the repeated statements of its own officials, employees and agencies that State employees would be compensated with a certain level of premium-free health insurance, the Defendants attempt to reason away their own statements. No matter how many times it was repeated, in how many contexts, by how many different government officials, Defendants say these assurances were all given by the wrong agencies or employees or officials in the wrong manner at the wrong time. Ultimately, they even try to claim that these officials did not really mean what they said – that, for example, when the State Treasurer testified in her deposition that she was vested into the Retirement Health Benefit, she did not *really* mean "vested." (See Def.'s Brief at 92). Next, when faced with overwhelming precedent and overwhelming evidence of promises to State retirees, the Defendants look to the reservation of a right to amend the statute, a thirteen-word clause that they claim undoes the thousands of words they used over the decades to make promises they now claim were "illusory." That clause, they claim, was the proverbial fingers crossed behind their backs.

When it comes to the breach of the contract in this case (while elsewhere saying that the potential liability presented by this case is so substantial as to have massive effects on the budget and to undermine the

State's credit rating), Defendants contend that the breach here is "*de minimis*." Finally, as the last line of defense, the Defendants contend that even if there was a contract and even if it was breached, that they were allowed to breach it because *they* failed to set aside the money to pay for the promises *they* made.

Plaintiffs, on the other hand, contend that this Court was correct in Simpson, Bailey and Faulkenbury, and that those cases govern this case. Plaintiffs contend that this Court should follow its own precedent in determining whether a contract exists here, not conclude that it was wrong by not restricting its analysis to federal law for all of these years. Plaintiffs contend that this Court actually meant "deferred compensation" when it chose those words, not just "deferred salary." Plaintiffs contend that it actually means something when the General Assembly, and numerous State officials, agencies and employees undertake to promise hundreds of thousands of State workers that they will receive a certain level of insurance premium-free for the rest of their lives. To the Plaintiff class – who worked their careers for less pay in exchange for much-lauded "State benefits" – there was nothing "illusory" about this promise. There was certainly nothing illusory about their years of work based on this promise.

Plaintiffs further contend that this Court knew what it was doing when it found contracts despite reservations of rights to amend in Simpson and Faulkenbury and that a right-to-amend is limited by the vesting requirements that the State itself has set forth. That is, if the State says you will have certain rights for doing certain work, and you do the work, you are vested and those rights cannot be taken away. The State can change benefits prospectively, but it cannot retroactively change the deal for those who have vested.

Plaintiffs also believe that if you break a promise to hundreds of thousands of people in a manner that costs them over a hundred million dollars, that is a real breach, not a *de minimis* one. Finally, Plaintiffs reject the notion that when you make such a promise but fail to set aside the money, that your own failure to prepare to fulfill your promises serves as a justification for breaking them, especially when you have numerous alternatives to address the problem other than violating vested rights.

There is something else vitally important that the Plaintiffs understand about this case. Plaintiffs understand what is really at stake here. When the Defendants state repeatedly that they are under no obligation to provide any particular health coverage of any kind, they are saying they have no obligation to provide health insurance *at all*. When they claim that any promise they

made to provide this health insurance – a promise made thousands of times in numerous ways – was "illusory," they mean they can say whatever they want, however they want, as many times as they want, and have absolutely no obligation to follow through on any of it. In 2011, when they felt the budget crunch, they solved it on the backs of the men and women who gave their careers to the State, by charging them premiums they promised never to charge. See Act of May 11, 2011, ch. 85, § 1.2(a), 2011 N.C. Sess. Laws 119, 120; Doc. Ex. 3062. When Defendants come into this Court and ask for a ruling that they have no obligations *at all*, they are really asking for this Court's blessing to do away with the Retirement Health Benefit in its entirety if that's what they think the next budget crunch requires.

ARGUMENT

I. There is a Contract Under This Court's Binding Precedent

This Court has addressed cases like this one before. In doing so, it has set forth its own standard which governs when the State and its employees are parties to a contract for employee benefits.

> We believe that when the General Assembly enacted laws which provided for certain benefits to those persons who were to be employed by the state and local governments and who fulfilled certain conditions, this could reasonably be considered by those persons as offers by the state or local

> government to guarantee the benefits if those persons fulfilled the conditions. When they did so, the contract was formed.

Faulkenbury, 345 N.C. at 691, 483 S.E.2d at 427. That is the standard promulgated by this Court, and which governs this case. By definition, the entirety of the Plaintiff class are persons who "fulfilled certain conditions" set forth by the State to receive the Retirement Health Benefit. "When they did so, the contract was formed." Id. Everything else in this case is an effort by Defendants to circumvent the plainly stated standard of this Court.

When you have such a direct precedent in a case, one would think it would be the primary topic of discussion in the briefing. However, Defendants first address it at page 58 of their brief. When faced with a standard they know their adversaries have satisfied, the Defendants, quite logically, go searching for a different standard. However, this search cannot undo the precedents of this Court.

Defendants look to federal law for a higher bar, claiming that Plaintiffs must essentially show that the statute itself and alone unmistakably states contractual intent.[1] This is simply not the standard this Court applies. The

[1] Plaintiffs fully believe that the statues in question do evidence an unmistakable intent to contract. For that discussion, see Plaintiffs' opening brief at § III(b). In one instance, Defendants attempt to do damage control

opinions in Bailey, Simpson, Faulkenbury and others never state this as the standard, nor do they state that such a standard was met *en route* to finding a contract. Defendants contend at great length that the standard is something other than what this Court has ruled it to be on multiple occasions. Make no mistake about it, this is an argument that this Court's precedents are wrongfully decided and that this Court should have been restricting itself solely to a federal analysis for all of these years.

The height of the fallacy of this contention is illustrated most clearly through the Defendants discussion of North Carolina Association of Educators v. State, 368 N.C. 777, 786 S.E.2d 255 (2016) ("NCAE"). Defendants represent NCAE as endorsing the federal standard, but this representation

---

on the General Assembly's use of the word "vesting" in the short title of Senate Bill 837 (Short Bill Title: "State Health Plan / 20-Year Vesting") by incorrectly stating that it was "excised from the enacted law." (Def.'s App'x at 11). The law changed the vesting requirement for the Retirement Health Benefit for newly hired employees from 5 years to 20 years for premium free coverage. See id. Short titles are used by the General Assembly to refer to a bill without having to state the full name of the bill, which is 37 words long in this case. The short title of this Bill further indicates that the General Assembly, in addition to the Treasurer, the Retirement System, and the State Health Plan intended the "eligibility" requirements to really be "vesting" requirements. See Dickson v. Rucho, 366 N.C. 332, 342, 737 S.E.2d 362, 370 (2013) ("The title of an act may be an indication of legislative intent.").

ignores two-thirds of this Court's analysis in the NCAE opinion. It is true that this Court first looked to federal law to determine whether there was a contract between the State and teachers for teacher tenure. See id. at 786–88, 786 S.E.2d at 262–63. However, after ruling that the federal standard was not met, this Court did not stop there. Instead, "[t]urning next to the opinions of this Court," the Court followed its own precedent, but distinguished Bailey and Faulkenbury on the grounds that teachers were not vested because there was still a discretionary act of local school boards necessary to grant tenure even after the eligibility requirements were met. Id. at 788, 786 S.E.2d at 263-264). Once again, however, this Court reasoned that "our analysis does not end here," but went on to find that tenured teachers had vested rights once they had entered tenure contracts with local boards. Id. at 789–90, 786 S.E.2d at 264.

Based on Defendants' theory of the case, this Court should have ended its analysis after considering the federal standard, and never gone through two more levels of reasoning. If the federal standard was not met – their theory dictates – you should not have been able to find a contract. Using Defendants' reading of NCAE would result in a reversal of that case as this Court in NCAE

did not find a contract under the federal standard. Thus, once again, the State implies that this Court's opinions are wrongfully decided.[2]

Far from undermining Bailey and Faulkenbury, NCAE reaffirms those opinions and cites them as binding precedent. In fact, NCAE's citation of these cases ultimately unwinds Defendants' eventual efforts to distinguish these cases when they finally get around to discussing them. Defendants later contend that these cases only apply in the context of pension payments. Aside

---

[2] Defendants contend in a footnote that only federal law governs whether a contract was formed between the State and its employees. (Def.'s Brief at 32, n.13). Aside from being contrary to the holdings in Bailey, Simpson and Faulkenbury, this contention also fails to fully and accurately set forth the federal law on the topic. First of all, the Fourth Circuit has held that "the issue of whether a contract right exists is governed by state law, while federal law governs a determination that a contract has been impaired under the Contract Clause." Kestler v. Bd. of Trs. of N.C. Local Governmental Employees' Ret. Sys., 48 F.3d 800, 803 (4th Cir. 1995). In support of their conclusion to the contrary, Defendants cite Gen. Motors Corp. v. Romein, 503 U.S. 181, 187 (1992). The issue in Romein, as well as the cases it followed, involved the extent to which the Supreme Court of the United States should defer to state supreme courts. See id. Those cases held that such courts should be given significant weight, but that the Supreme Court could still exercise independent judgment. See, e.g., Appleby v. New York, 271 U.S. 364, 379–80 (1926) (holding that the Court cannot "surrender the duty" to make its "own judgment"). Since we are not in the Supreme Court of the United States, this issue is not before the Court. Finally, these cases only deal with Contract Clause cases under the federal Constitution. Plaintiffs make their claims under the Law of the Land clause of the North Carolina Constitution, as well as a common law breach of contract claim. There is no precedent applying federal law to those obviously state law claims. Accordingly, this Court should continue to follow its own precedent.

from the fact that these cases never hold any such thing, NCAE makes no effort to distinguish them on this basis, even though the teacher tenure issue involved there was well outside the context of pensions.

Certainly this Court could have adopted the federal standard as it sole standard when given many opportunities to do so. It has not. Certainly this Court could have limited its rulings in employee benefit cases to pension payments when deciding NCAE. It did not. What this Court did do is establish a clear standard which holds that employees who meet the requirements to receive certain benefits have a contract to receive them. The inconvenience of this standard to Defendants makes it no less the proper standard in this case.

II. The Retirement Health Benefit is Deferred Compensation

Plaintiffs are somewhat hesitant to spend considerable brief space continuing to argue that a health benefit paid in compensation for your work but deferred until retirement is "deferred compensation." Again, it is clearly deferred (it comes after your work is over), and it is clearly compensation (you get it in exchange for your work), so it is clearly deferred compensation. Despite how obvious this point is, it is equally important.

And why is it so important? Because this Court has unequivocally ruled that deferred compensation is contractual and cannot be taken away. Simply

put, Defendants must continue denying this obvious point because they cannot win this case unless they convince this Court that a deferred form of compensation is not deferred compensation. It is a must-win issue for the defense.

This is because this Court's cases are perfectly clear on this point. "If a pension is but deferred compensation . . . then an employee has contractual rights to it." Bailey, 348 N.C. at 141, 500 S.E.2d at 60 (quoting Simpson, 88 N.C. App. 223–24, 363 S.E.2d at 94). Also, in Simpson, in a Court of Appeals opinion adopted by this Court, it was held:

> The agreement to defer the compensation is the contract. Fundamental fairness also dictates this result. A public employee has a right to expect that the retirement benefits bargained for in exchange for his loyalty and continued services, and continually promised him over many years, will not be removed or diminished.

Simpson, 88 N.C. App, at 223–24, 363 S.E.2d at 94. Defendants acknowledge this law in their brief when they state that "[p]ensions are contractual because they represent deferred compensation for an employee's work." (Def.'s Brief at 28).

This acknowledgement is where Defendants' admission of the obvious ends, and where their creative rewrite of this Court's precedent begins.

Throughout their argument on this point, Defendants substitute the word "salary" for the word "compensation" in an effort to make it seem like this Court was focused exclusively on salary rather than compensation more generally. It is a modification of existing Supreme Court holdings to say that this Court believes it is fine to break promises with regard to retirement benefits so long as those benefits are not in the form of mandatory, periodic payments that are based on your level of salary. The trouble with this argument is that this Court has had ample opportunities over multiple cases to base its reasoning on these fine points, but has repeatedly declined to do so.[3] In fact, most recently and most tellingly, when addressing the non-pension issue of teacher tenure agreements in NCAE, this Court had a golden opportunity to limit the scope of Bailey, Simpson and Faulkenbury solely to that of pensions, or as Defendants would say, "salary." This Court chose not to take that opportunity. If the Court had done so, it would have been a major

[3] For a detailed discussion of the fact that this Court's prior opinions do not in any manner rely upon the distinctions argued by the Defendants or relied upon by the Court of Appeals, see pages 30-35 of Plaintiffs' opening brief. This Court has found contracts for benefits not tied to salary or seniority, not paid out in regular payments, and which related to voluntary as opposed to mandatory programs. Cleary, this Court has never said it was relying on these considerations in reaching its decisions, nor has it limited its rulings to the context of pension payments.

departure from its prior precedent and other North Carolina cases, which have found contracts for several benefits other than pension payments. See, e.g., Faulkenbury (disability); Bailey, 348 N.C. at 138, 146, 500 S.E.2d at 58 (blanket tax exemption did not vary based on salary, seniority, etc.), Pritchard v. Elizabeth City, 81 N.C. App. 543, 545, 552–53, 344 S.E.2d 821, 822, 826–27 (1986), review denied, 318 N.C. 417, 349 S.E.2d 598 (1986) (vacation pay); Wiggs v. Edgecombe Cnty., 361 N.C. 318, 324, 643 S.E.2d 904, 908 (2007) (special separation allowances); Bolick v. County of Caldwell, 182 N.C. App. 95, 96, 100-01, 641 S.E.2d 386, 388, 390 (2007) (severance pay).

Aside from the patently obvious fact that health benefits are a form of compensation for work, once again one only needs to look at the pronouncements of this Court to see this clear fact in print. "Salary, pension, *insurance and similar benefits* received by public employees are generally not unconstitutional exclusive emoluments and privileges. *They constitute compensation in consideration of services rendered*." Leete v. County of Warren, 341 N.C. 116, 121, 462 S.E.2d 476, 479 (1995) (emphasis added).

For absolute clarity, this is Plaintiffs' position: (1) deferred compensation is contractual, (2) this Court has said that health benefits are compensation, and (3) benefits deferred until retirement are indisputably deferred.

Therefore, the deferred Retirement Health Benefit is deferred compensation. Defendants' position is as follows: (1) deferred compensation is contractual, but (2) health benefits are not compensation even though this Court has previously said that they are. So, Defendants contend that this Court was not only wrong in the development of the law of contract in Bailey, Simpson and Faulkenbury by not limiting itself to federal law, but that this Court was similarly wrong when it previously pronounced the obvious truism that health benefits are compensation.

The State's argument clearly departs from this Court's prior analysis, but it also departs from the State's own statutorily mandated requirement that the Retirement Health Benefit be booked as deferred compensation. The General Assembly has required that the Retirement Health Benefit be accounted for annually based upon the "other post-employment benefit accounting standards" promulgated by the Governmental Accounting Standards Board ("GASB"). N.C.G.S. § 135-48.12(a), (g) (2011). The GASB standards require that retirement health benefits be treated as deferred compensation and classified as a liability. (See Doc. Ex. 785–87). So when the State denies that the Retirement Health Benefit is deferred compensation, it does so in

contravention of its own express statutory requirement that they be treated as exactly that.

Finally, rather than look to how this Court has defined "compensation," Defendants now urge this Court to limit itself to the statutory definition of this term in the pension statute. However, a read of Simpson, Bailey and Faulkenbury makes clear that none of those cases relied upon that definition. Nor should they have. "Compensation" is defined in the Retirement System statute with an eye toward calculating how much of an employee's compensation is deducted for later pension payments. See N.C.G.S. § 135-8(b)(1) (setting forth the percentage of "compensation" deducted to fund pensions). Defendants confuse this definition for the absolute word on what benefits are or are not compensation for work performed. Looking at the statute, this misunderstanding leads to repeated absurdities. Not only would this definition exclude health insurance as Defendants insist, it would also exclude "[b]onuses paid incident to retirement," "[p]ayouts for unused sick leave," "[i]ncentive payments for early retirement," and "[e]mployer contributions to eligible deferred compensation plans." N.C.G.S. § 135-1(7a)(b)). Are retirement bonuses not compensation for work performed? Is pay for unused sick leave not to compensate workers who worked instead of

taking accrued time? Or perhaps, is this definition excluding certain things that did not make sense to deduct from to fund pensions, rather than giving the final word on what is or is not compensation for work performed? But it is the last of this list – "[e]mployer contributions to eligible deferred compensation plans" – which truly reveals the untenable nature of Defendants' contention. If Defendants are right and anything not included on this specific definition of compensation cannot be considered compensation for this Court's purposes, it would mean that "deferred compensation" cannot be "compensation." Clearly this cannot be the case, especially where this Court has already held those very pensions to be deferred compensation.

Similarly, there is further absurdity to be found in what *is included* in the pension statute's definition of "compensation." That lists includes, for example, "[c]onversion of additional benefits to salary (additional benefits such as health, life, or disability plans)." N.C.G.S. § 135-1(7a)(a). If health benefits are not compensation, how can they be monetized and converted to compensation? If this definition acknowledges the fact that health benefits are or can be compensation in this manner, how can this definition be a basis for this Court to hold that health benefits are not compensation at all? The "compensation" definition also includes "[p]erformance-based compensation

(regardless of whether paid in a lump-sum, in periodic installments, or on a monthly basis)." Id. But it is Defendant's position that health benefits are not compensation because they are not paid in regular periodic payments. Would this not also mean that performance-based compensation is also not compensation, even though it is included in the very definition Defendants are claiming is authoritative?

This statutory definition argument falls apart for the very fact that it is a desperate attempt to deny an obvious fact that dispositively dooms Defendants' entire position in this case. After hundreds of pages of briefs and thousands of pages of record material, this issue is as obvious as it sounds. It is an absurdity to claim that the Retirement Health Benefit is not really deferred compensation. This is a must-win argument for the defense, but it is one the defense simply cannot win.[4]

---

[4] Plaintiffs have frequently asked, and Defendants have never answered the following question: If the Retirement Health Benefit is not deferred compensation, what is it? If it is not compensation for public service, it is a gratuity, which creates an additional constitutional issue. See Faulkenbury, 345 N.C. at 691, 483 S.E.2d at 427 (rejecting notion that pensions were gratuities because "[i]f they were gratuities, . . . they would run afoul of proscription of special emoluments as provided in our state Constitution."). Defendants sole response to this dilemma is to reference two cases involving government programs for war veterans and claim that they create some middle ground between compensation and gratuity. (See Def.'s Brief at 58, n.17). This is not what these cases do. In both, the benefits to veterans were

III. The Non-Statutory Materials Cited by Plaintiffs Further Evidence the Contract

As discussed above, this Court has held that a contract exists where the State has set forth certain requirements for employees to receive certain benefits, and where the employees have fulfilled those requirements. "When they did so, the contract was formed." Faulkenbury, 345 N.C. at 691, 483 S.E.2d at 427. Every class member satisfied the vesting requirements here, so there is a contract. Although our analysis could have stopped there, we have gone on to discuss the obvious fact that the Retirement Health Benefit is deferred compensation, since this Court has consistently held that retirees have contractual rights to deferred compensation. See, e.g., Bailey, 348 N.C. at 141, 500 S.E.2d at 60. Because the Retirement Health Benefit is clearly deferred compensation, our analysis could have stopped there as well. However, for additional support, Plaintiffs have pointed to various non-statutory documents and representations that further demonstrate the contractual nature of the benefit. We do this not because we need to, but because this Court has looked to these very types of materials in the past in finding

---

classified as "consideration" for "pubic service." See Brumley v. Baxter, 225 N.C. 691, 696–97, 36 S.E.2d 281, 285 (1945); Hinton v. Lacy, 196 N.C. 496, 505, 137 S.E. 669, 674 (1927).

contracts for government employee benefits. See, e.g., id. at 138–39, 146, 500 S.E.2d at 58–59, 63 (considering a "totality of the circumstances," including but not limited to communications made to plaintiffs in both oral and written form, including handbooks). Here, reference to these representations is yet another means to the same result, that there is a contract for the Retirement Health Benefit.

Although the Court of Appeals refused to consider any of this evidence, the State perhaps realizes that this refusal runs afoul of this Court's precedent, and therefore spends a great deal of time trying to take back its own representations. While knowing that this Court has previously looked to representations in these kinds of non-statutory contexts, the Defendants refer to this practice as "stitching together snippets." (Def.'s Brief at 3). Ironically, the State then proceeds to cherry-pick from what they have accused Plaintiffs of cherry-picking, selecting certain of its own representations it believes it can attack. However, in the end, there are just too many times the State expressed its contractual intent in too many ways for them all to be taken back now. Moreover, upon closer examination, Defendants' efforts to minimize or withdraw these admissions are unavailing.

One of Defendants' most common criticisms of documents which demonstrate contractual intent is that they may not have been seen by Plaintiffs, and therefore may not have been relied upon. This Court rejected such an argument in Faulkenbury.

> The defendants say the evidence showed that the plaintiffs did not read the handbooks provided them, which explained their pension rights, and made no inquiries about these rights until they retired. For this reason, say the defendants, the plaintiffs had no particular expectations in regard to disability payments except that they would receive what the pension plan provided for them. The plaintiffs expected to receive what they were promised at the time of vesting. They may not have known the exact amount, but this was their expectation. The contract was substantially impaired when the promised amount was taken from them.

Faulkenbury, 345 N.C. at 692–93, 483 S.E.2d at 428.

Nonetheless, many of these documents (such as Your Retirement Benefit Booklets and State Health Plan documents) *were* seen and relied upon by Plaintiffs. In addition, aside from the issue of reliance, many of these documents evidence the contractual intent of the Defendants – regardless of whether they were relied upon by Plaintiffs.[5] As to some documents, however,

---

[5] Contrary to Defendants' arguments, the course of performance between parties and the words used therein is a strong indication not only of a contract, but also for the interpretation of the contract. "Sometimes the conduct of the

the problem is even more pronounced. For example, Defendants levy this criticism against the training materials given to benefit counselors. Unfortunately for Defendants, these were the very materials used by benefit counselors to explain the Retirement Health Benefit to class members. (See Doc. Ex. 12722 [Wall Dep. at 63:5–13]). Therefore, these materials, along with the testimony of the benefits counselors themselves, are perhaps the best evidence of what class members were told. In keeping with these manuals, benefits counselors consistently told State employees at presentations, on calls and in counseling sessions that they would get the same level of insurance they had had as active employees, premium-free, during their

---

parties after the contract is made indicates the meaning that they attach to the contract language subsequently in dispute. Such 'practical construction' is given great weight by the courts." E. Allan Farnsworth, *Contracts* § 7.13, at 489 (3rd ed. 1999). In fact, as Farnsworth noted in his treatise, "the interpretation placed upon a contract by the parties themselves, before a dispute has arisen, is entitled to the ***greatest weight***." Id. (quoting Reconstruction Fin. Corp. v. Sherwood Distilling Co., 200 F.2d 672, 676 (4th Cir. 1952) (emphasis added). As a necessary corollary to this long-standing doctrine of contract law, statements made by a contracting party during performance are likewise evidence of the contract itself and are considered admissions. "It would then seem that if the conduct takes the form of a statement (and surely statements must be at least as effective as other conduct in this regard), a single statement from which an inference can clearly be drawn should suffice." Id.

retirement. (See Doc. Ex. 12699–701 [Wall Dep. at 40:18–42:10]). On a "daily basis," such counselors informed employees that they needed five years of creditable service to get this benefit. (See Doc. Ex. 12702–04 [Wall Dep. at 43:14–45:24]). One such counselor testified that his own expectation was 80/20 premium-free insurance during retirement, and that he – as trained by the Defendants – instructed employees to expect the same. See id.

Based on the manuals, this counselor instructed properly. The training manual, when discussing the fact that one must be in the pension system to receive the Retirement Health Benefit, observed that "With growing concern about health insurance in our society today, this is an important piece of information that the member should know if he is vested with the 5 years of contributing membership in the State." (See Doc. Ex. 899-900). This is the State instructing counselors to represent to employees that they will vest into the Retirement Health Benefit with five years of service. This cannot be reasoned away. Nor can an email from a senior benefits counselor and trainer of other benefits counselors (Betty Fuller) clarifying changes in health care eligibility, when it states that it "does not alter the fact that a member still must have at least 5 years of retirement membership service earned," later

noting that "The member must still be vested with 5 years of membership service to meet the eligibility to retire." (See Doc. Ex. 901 and Doc Ex. 1069).

From these documents, it is not only clear that employees were instructed that they would be vested after five years, but also that the terms "eligibility" and "vesting" were used interchangeably in teaching employees about their health coverage. Defendants acknowledge this interchangeable use of "vesting" and "eligibility" (see Def.'s App'x at 5), but still argue that the word "eligible" means something less than "vested." This is not the way the words were used when it counted, when the State was making representations to its employees. There, they were one in the same.[6]

Plaintiffs rely on certain representations that come directly from the State Health Plan, and that are made directly to the public. Unable to attack either the source or the audience of these representations, Defendants turn to word games. For example, Defendants attack a press release from the State

---

[6] These documents also make clear the inextricable linkage between the pension system and the health benefit, with eligibility for one tied to that for the other. Given this link (which also includes their codification alongside one another and the deduction of the offending premiums directly from pensions), Defendants' efforts to avoid their representations in Your Retirement Benefits Handbooks and associated letters unravel. Therefore, when said handbooks recite that an employee will receive the Retirement Health Benefit upon retirement if they accrue five years of service, they mean exactly that. (See Doc. Ex. 4120).

Health Plan, which explains the reasons for the change in the vesting/eligibility requirements. (Def.'s App'x at 14). Defendants contend that because the word "vested" proceeds the phrase "in the retirement system," that there is no connection to the eligibility component of the State Health Plan. (Id.). This argument makes little sense based on simple context: the press release is from the State Health Plan and is specifically addressing the Retirement Health Benefit. So how can it *really* be about pensions? Even more tellingly, the Defendants cut out the most important words of the sentence in which the word "vested" appears, likely because these words establish what Defendants have been trying to avoid all along: "The benefits, provided through the State Health Plan, were *earned through past service* by North Carolina state employees and teachers who are now retired or already vested in the retirement system." (Doc Ex. 723 (emphasis added)). This is unmistakably the language of deferred compensation, spoken from the State Health Plan itself to the public. There is no basis to attack the substance, the source, or to whom it was communicated.

The aforementioned press release is also consistent with a "State Health Plan Update," in which the Executive Director described participants in the plan "with a vested retiree health benefit." (Doc. Ex. 719; see also Doc. Ex. 720

(describing "*Liability* associated with *benefits earned* in past years.") (emphasis added)). This is clearly about the State Health Plan, so there is no explaining away "vesting" in this instance as *really* referring to the pension system. Instead, Defendants provide what they claim to be an "uncontradicted affidavit" from Ms. Moon that "vest" is "shorthand to describe members who were, at the time, eligible under state law for certain benefits from the State Health Plan." (See Def.'s App'x at 14 (citing Doc Ex. 3503)). Again, this effort to drive a wedge between the term "vested" and the term "eligible" is unsuccessful, and in some ways is just another example of the two words being used interchangeably. Moreover – her self-serving affidavit aside – Ms. Moon's deposition testimony shows that she understood the word "vesting" to be analogous to "earning." When answering a question about whether the Retirement Health Benefit and retirement pension are a part of the same retirement package, Ms. Moon stated: "Yes, I believe that employees are earning, vesting, whatever word, a retirement benefit over the course of their employment that may include a retiree health benefit upon their retirement." (See Doc Ex. 11297-11298 [Moon Dep. at 234:23–235:8]). This is reminiscent of the State Treasurer's admission that she was vested into the health benefit. (See Doc. Ex. 10527 [Cowell Dep. at 28:5–10]) ("Q: Are you ***vested*** in the retiree

health benefits at this point? A: ***Yeah. I am*** . . .") (emphasis added). Defendants now contend that neither *really* meant "vested."[7]

This all appears to be part of a larger semantic game. As with virtually everything Defendants argue in this case, it is a matter of avoiding the binding precedent of this Court. Specifically, in Bailey the Court noted that under each of the systems at issue there, employees had to "work a predetermined amount of time in public service before they [were] *eligible* for retirement benefits", after which "they were deemed to have 'vested'". Bailey, 348 N.C. at 138, 500 S.E.2d at 58 (emphasis added). In cases such as Bailey and Faulkenbury, the

---

[7] As to other documents, such as actuarial documents, Defendants claim they have no weight because they were prepared by consultants or contractors. This argument is completely beside the point. These reports and the standards they followed were mandated by statute. See N.C.G.S. § 135-48.12(g) (2011) (requiring "an annual calendar-year actuarial valuation of retired employees' health benefits under accounting standards set forth by the Government Accounting Standards Board of the Financial Accounting Foundation."). The outside actuary (what the Defendants called an outside consultant) was a statutorily designated technical advisor and was required to follow standards which mandated that Retirement Health Benefits be treated as *deferred compensation* and classified as a *liability*. See N.C.G.S. § 135-38.1(f), recodified at § 135-43.4(f) and then § 135-48.12(f). Moreover, these actuarial reports were used by the Defendants in making decisions about the State Health Plan, including discussion about some of the very things at issue in this litigation. (See e.g. Doc. Ex. 906-910)(discussing prospective only changes, "limit[ing] future retirees to the Basic PPO" option, impacts from the "vesting schedule," and "whether current employees have a contract for these benefits"). Defendants ordered, authorized and relied upon these reports, and cannot run from them now.

term "vested" has been used to describe contractual rights which cannot be taken away – meaning rights gained by meeting certain criteria laid out by the State. This creates a significant inconvenience for Defendants, especially since we are in the same context, and dealing with the same vesting requirements as present in those cases. Faced with this dilemma, the State is forced to contend that in all of the many instances in which they have spoken of vesting into the Retirement Health Benefit, they *really* meant something different than "vesting" as understood by this Court, or as it is meant when discussing pensions. So the argument, essentially, is that when State officials say "vesting" in reference to pensions it carries contractual weight, but when they say "vesting" in reference to the Retirement Health Benefit it means nothing. It is also this dilemma that leads the State to contend that when the Executive Director of the State Health Plan said "vested" or "earned," she really meant neither, or that when the State Treasurer admitted in her deposition that she was vested into the Retirement Health Benefit, that she did not really mean "vested." This is nothing more than self-interested interpretive gloss on words that everyone actually understands to have contractual weight[8].

[8] While maintaining that they are entitled to summary judgment because there are no genuine issues of material fact, the Defendants go out of their way in the response brief to seemingly create issues of fact by contradicting

In order to avoid any confusion, let's take a step back and see how the word "vesting" has been defined.

> Vesting occurs when "the right to the enjoyment of [an interest], either present or future, is not subject to the happening of a condition precedent." Our case law has further defined a vested interest as "a right which is otherwise secured, established, and immune from further legal metamorphosis," Gardner v. Gardner, 300 N.C. 715, 718-19, 268 S.E.2d 468, 471 (1980); in other words, it is a right that cannot be canceled, Fountain v. Fountain, 148 N.C. App. 329, 337 n.11, 559 S.E.2d 25, 32 n.11 (2002) . . . .

Rice v. Rice, 159 N.C. App. 487, 494–95, 584 S.E.2d 317, 323 (2003) (quoting Black's Law Dictionary 816 (7th ed. 1999)); see also Black's Law Dictionary (3rd Pkt. Ed. 2006) (defining "vested" as "Having become a completed, consummated right for present or future enjoyment; not contingent; unconditional; absolute."). "Vesting" is a contractual term, and a vested rights cannot be taken away under North Carolina law. This Court certainly understood that in Bailey and Faulkenbury, and should continue with that understanding now.

---

the testimony of their own witnesses and the 'real meaning' of their own documents.

IV. There is a Contract for the Retirement Health Benefit Despite the Right to Amend the Statute and Certain Amendments Over Time

Once again, when faced with unfavorable North Carolina case law, Defendants look elsewhere. Essentially, Defendants claim that a right to amend a statute prevents any rights from vesting, and makes any promises made by the State illusory. Therefore, even if the State set forth vesting requirements for certain deferred compensation, and those vesting requirements are satisfied, the State can simply refuse to uphold its promises. Defendants cite no cases from this Court which stands for these propositions, because there are none.

To the contrary, this Court has found contracts between the State and private parties even in the face of statutory rights to amend. Plaintiffs have argued throughout the years of this case that any right to amend is limited by a restriction against amending away vested rights. Defendants attempt to dismiss this argument without citation – relying instead on the bare assertion that "a right-to-amend clause precludes the *creation* of statutory contract rights." (Def.'s Brief at 48) (emphasis original). This assertion cannot survive this Court's precedent. The constitutional right to amend or repeal corporate charters at issue in Elizabeth City Water & Power Co. v. Elizabeth City, 188

N.C. 278, 124 S.E. 611 (1924) was as broad as any right to amend can get. "All such laws and special acts may be altered from time to time, or repealed; and the General Assembly may at any time, by special act, repeal the charter of any corporation." Elizabeth, 188 N.C. at 287, 124 S.E. at 615 (quoting N.C. Constitution, Art. VIII, Sec. 1). Under Defendants' theory, it should therefore be impossible for any vested rights to arise in the context of this broad amendatory power. Nonetheless, this Court held that where "rights have been acquired and become vested, no amendment or alteration of the charter can take away the property or rights which have become vested under a legitimate exercise of the powers granted." Id. at 288, 124 S.E. at 615. If a right to amend renders all promises illusory and prevents the acquisition of any vested rights, then this Court's reasoning would be surplusage. Thus, once again, Defendants' primary stumbling block is the binding precedent of this Court. Of course, Defendants cite no North Carolina case which holds to the contrary, because there is none to be found. Even the federal law – to which Defendants consistently run when this Court's holdings present a problem – supports the holding in Elizabeth. The Supreme Court of the United States held in the Sinking Fund Cases that a right-to-amend provision is limited in that "it cannot undo what has already been done, and it cannot unmake

contracts that have already been made." Union Pac. R. Co. v. United States, 99 U.S. 700, 721 (1878) ("Sinking-Fund Cases").

Compounding Defendants' difficulty is the fact that both Simpson and Faulkenbury found binding contracts between the State and its employees for deferred compensation despite the existence of a right to amend. Although Defendants rely upon the limiting language in the right-to-amend provision at issue in those cases, it is notable that Simpson did not. See Simpson, 88 N.C. App. at 221, 363 S.E.2d at 92 (quoting N.C.G.S. § 128-38). In fact, when considering this clause, the Court of Appeals – in an opinion adopted by this Court – went out of its way to exclude this limiting language. It therefore considered the right-to-amend clause as follows: "the right at any time and from time to time . . . to modify or amend in whole or in part any or all of the provisions of the North Carolina Local Government Employees' Retirement System." Id. Nonetheless, as we all know, it found a contract. Defendants seem to presume that the most important motivating factor behind the Court's decision in Simpson was the words it specifically chose to leave out.

Defendants engage in an elaborate analysis of unrelated history in order to support the argument that "the one and only point of such a [right-to-amend] provision is to bar the creation of contract rights." (Def.'s Brief at 49).

Defendants begin this analysis by assuming that an 1819 federal case governs what the General Assembly really intended over a century-and-a-half later. Then, they discuss how the General Assembly wanted to maintain control over the State Health Plan rather than delegate it completely to an executive agency. This walk through history is long on assumptions and short on evidence or actual legal analysis. None of it is based on actual legislative history which demonstrates that the General Assembly's intent was what Defendants contend. Rather, Defendants argue that, based on historical events, barring contracts *must have been* what the General Assembly was thinking.

This entire argument is based upon two rather speculative assumptions: (1) that the General Assembly was engaged in an inter-branch power struggle and wanted to retain control over the State Health Plan, and (2) that if this first assumption is true, it somehow means that what the General Assembly was really trying to do was bar the formation of contracts. Even if you assume that (1) is true, (2) presents a problem Defendants cannot overcome. It is a *non sequitur*; one does not logically flow from the other. That is, if the General Assembly wanted to retain some level of control over the Plan rather than delegate it, how does this mean that barring contracts was the "one and only"

purpose of a right to amend, such that Plaintiffs' position would render the clause surplusage? One can imagine many other purposes of such a clause: (a) to make changes to the administrative structure of a quasi-independent executive agency, (b) to make changes that improve coverage (as many amendments have done) rather than decrease it, (c) to make prospective changes (again, as has often been done) that do not undermine vested rights, or, as Defendants suggest, (d) a simple desire not to delegate certain authority to a different branch of government. Any of these purposes and many more could be involved. In order to make its surplusage argument, however, the State needs to say that barring contracts is the one and only purpose, but there is no support for this conclusion other than assumption and speculation.

It seems that the reality of the General Assembly's intent is somewhat simpler than Defendants assume. The precise right-to-amend language at issue here was used one other time by the General Assembly during the same timeframe, and that was in the statute creating the Institute of Medicine[9]. See N.C.G.S. § 90-470 (establishing the Institute of Medicine and providing that

[9] Unlike the State Health Plan, the Institute of Medicine was not established to provide benefits to State employees – so the exact same right to amend language cannot possibly be construed as an intent to avoid creating contracts for employment benefits.

"The General Assembly reserves the right to alter, amend, or repeal this Article"). It is likely not a coincidence that this exact clause was used twice near the same time, and that in both instances it dealt with control over a "body politic and corporate" such as the State Health Plan or the Institute of Medicine. Retaining these rights with regard to such bodies need not have anything to do with whether contracts can be formed with regard to the subject matter of these statutes. It is far more likely that it amounts to retaining rights similar to those the State retains over corporate charters – other legally created entities like the State Health Plan or the Institute of Medicine. After all, as discussed above, the reservation of amendment rights with regard to corporate charters is just as broad as the rights over these separate government bodies. Also, as we know, despite the breadth of said reservation, this Court has recognized in just such situations the right to obtain vested rights which cannot be amended away. See Elizabeth, 188 N.C. at 288, 124 S.E. at 615. This, again, is consistent with Defendants' contention that the right to amend is about declining to delegate authority to an executive agency.[10]

[10] Defendants' claim that a right-to-amend clause must have the one and only purpose of preventing contract formation is belied by the fact that the General

Although Defendants argue that our interpretation renders the right to amend surplusage, it is their interpretation that leads to absurd results. If State retirees were considered to be under notice that all promises were illusory due to the right to amend such that no contracts could be formed, surely the same could be said of third parties dealing with the State Health Plan or the Institute of Medicine. Said third parties would know of the statutory provision as well. This must mean they too can have no rights against these government agencies, whether they be medical providers, insurance companies, third party administrators, or any other party acting in good faith in its dealings

---

Assembly has at times included explicit language in right-to-amend clauses which specifically bar contract formation. See, e.g., N.C.G.S. § 135-113 ("The benefits provided in this Article as applicable to a participant who is not a beneficiary under the provisions of this Article shall not be considered as a part of an employment contract, either written or implied, and the General Assembly reserves the right at any time and from time to time to modify, amend in whole or in part or repeal the provisions of this Article."); N.C.G.S. § 128-38.10 ("The General Assembly reserves the right at any time and, from time to time, to modify or amend, in whole or in part, any or all of the provisions of the QEBA. No member of the Retirement System and no beneficiary of such a member shall be deemed to have acquired any vested right to a supplemental payment under this section."); N.C.G.S. § 135-151 (same). If the mere right to amend barred contract rights, it would be surplusage for the General Assembly to have included this more specific language in these other statutes.

with the State. This Court has long cautioned against interpretations which lead to such absurd results. See Rhyne v. K-Mart Corp., 358 N.C. 160, 189, 594 S.E.2d 1, 20 (2004) (quoting State ex rel. Comm'r of Ins. v. North Carolina Auto. Rate Admin. Office, 294 N.C. 60, 68, 241 S.E.2d 324, 329 (1978)) ("Courts normally adopt an interpretation which will avoid absurd or bizarre consequences, the presumption being that the legislature acted in accordance with reason and common sense . . . .").

Finally, Defendants assert that the mere fact that the statutes underlying the Retirement Health Benefits have been amended over their nearly 40-year existence means there can be no contract related thereto. This Court has never adopted this logic as a reason not to acknowledge a retirement benefit program. In fact, the pension and disability retirement statutes underpinning this Court's opinions in Bailey and Faulkenbury have been amended as much (if not more) than the State Health Plan statutes. For example, the "Benefits" subsection of the Retirement System statutes contains hundreds of sub-sections that have been amended and added over several decades – with the last currently codified subsection being labeled as subsection "(www)." See N.C.G.S. § 135-5 (2020). Defendants' citation to NCAE in support of this argument is confusing given that this Court found a basis for a contractual

obligation for tenure using (at least in part) the tenure statutes that were amended over time. Although NCAE observed that the presence of amendments was worthy of consideration, those amendments ultimately did not prevent this Court from finding a contract in that case, nor did the presence of such amendments in the underlying statutes bar contracts in Bailey and Faulkenbury.

As Plaintiffs stated in their primary brief, changes in the administration and nature of certain benefits being offered is both natural and expected for an on-going health benefit program. The Defendants assert that these historical changes over a 40-year period show that there was no contract, and that Plaintiffs could have no reasonable expectation of a particular benefit, but in their response have failed to cite any actual evidence in the record to support this position.[11] Moreover, this Court has chosen to enforce the State's promises to its retirees even in the face of historical amendments to the

[11] In their response, the Defendants cite to two documents in the record in support of their conclusory statements that these historical amendments "reduced the plan's overall value." (Def.'s Brief at 52 (citing Doc. Ex. 14, 1137–45)). A quick glimpse at both documents reveal that they are nothing more than charts created by counsel for Defendants and attached to their summary judgment brief that do nothing more than summarize, from Defense Counsel's perspective, certain changes to the health plans over time. These documents are not evidence, but arguments of counsel and do not contain any evidence or even opinion as to the "plan's overall value."

relevant statutes, and even where those retirees' expectation cannot be measured to the penny. "The plaintiffs expected to receive what they were promised at the time of vesting. They may not have known the exact amount, but this was their expectation. The contract was substantially impaired when the promised amount was taken from them." Faulkenbury, 345 N.C. at 692–93, 483 S.E.2d at 428.

V. Defendants Impaired the Contract

Defendants contend there has been no substantial impairment of contract, and that in fact any such impairment is *de minimis*. Given the Defendants prior representations to this Court, that is an extraordinary argument to make. Although the parties to this case do not agree about much, there was a time when both sides filed a Joint Petition for Discretionary Review Before Determination by the Court of Appeals. See Bypass Petition, Lake v. State Health Plan for Teachers & State Emp., No. 436P13-3. Defendants drafted and signed off on that document, which emphasized that the stakes in this case were so high as to affect the State budget, that the damages for premiums paid alone would exceed 100 million dollars, and that the total cost of compliance with the trial court's order could exceed one billion dollars. (See id. at 12–13 (citing Doc. Ex. 3673)). Defendants know the massive nature of the

breach here, and have obviously acknowledged it before, but now claim it is insubstantial. Once again, this Court's prior precedent dictates otherwise. In fact, when faced with this same question of determining whether a breach was substantial, this Court relied upon an aggregate damages expectation of 100 million dollars – the same number the Defendants here have acknowledged for the refund of premiums *alone* – to hold that "the statutory amendment in question substantially impair[ed] the employees' contractual right to a tax exemption." Bailey, 348 N.C. at 151, 500 S.E.2d at 66.

The magnitude of this breach is alone sufficient to demonstrate the baselessness of Defendants' claim that it is *de minimis*. However, Plaintiffs feel compelled to reply briefly to Defendants remarkable contention that there was no impairment or breach because the 70/30 premium-free plan supposedly had an actuarial value that gave the Plaintiffs the benefit of their bargain. Without restating our previous arguments, there has always been a regular plan which has provided at least 80/20 co-insurance, and which was promised premium-free for life – that is, until 2011 when the State introduced premiums for this regular, default plan, and made the optional 70/30 plan the only premium-free option. What is remarkable about Defendants' claim that this lesser plan was sufficient, is that both the Executive Director of the State

Health Plan (and Rule 30(b)(6) designee) and Defendants' own expert have admitted that the 70/30 plan is less valuable than the regular state health plan. (R p 616 ¶ 31; Doc. Ex.11228 [Moon Dep. [9-15-15] at 165:6–9]("Q: [Y]ou would agree, would you not, that the 70/30 plan is generally a less valuable plan than an 80/20? A: Yes."); Doc. Ex. 11564 [Moon Dep. [2-26-16] at 183:15–19] ("Q: And the 80/20 would be the richer plan or the 70/30 would have less value then by that comparison; is that correct? A: Yes."); Doc. Ex. 1098–99 [McCarthy Expert Report]; Doc. Ex. 4605, 4624 [Fuhrer Expert Report] (***both*** Plaintiffs' and Defendants' expert witnesses found the 70/30 plan to be of less value to the retirees than the regular state health plan)). There is no evidence to the contrary. Defendants breached the contract in a massive way by charging premiums they promised never to charge on the regular state health plan, and by providing a lesser plan as the sole premium-free option. It seems Defendants seek to argue that subsequent changes to the plan made three years into this ongoing breach may have mitigated the problem, but given the magnitude of the breach, this would at most present a damages issue not presently before this Court.[12]

[12] Both here and elsewhere, Defendants seem to misunderstand the importance of actuarial value in this case. Defendants use this issue to try to make it appear that the Plaintiffs have frequently changed their theory about

The Bailey case continues to present a problem for Defendants when we consider their contention that the impairment was "reasonable and necessary to serve an important public purpose." Id. at 151, 500 S.E.2d at 66. As discussed in detail in Plaintiffs' opening brief, although Bailey concluded that there was an important purpose involved, the reduction of the tax-exempt status of pension payments was not reasonable and necessary where there were alternative means to accomplish this purpose "without impairing the contractual obligations." Id. at 152, 500 S.E.2d at 67. Whereas this Court in Bailey looked to two such alternatives, in this case it is an established fact that

---

what the contract is. This is incorrect. As Plaintiffs have previously pointed out, it is not our contention that the contract is for a specific actuarial value. The contract is for the regular state health plan, which has always provided at least 80/20 co-insurance and been provided premium-free. Nor did the trial court hold that the contract was for a specific actuarial value. Instead, it employed actuarial value in fashioning a remedy. The trial court understood the need to balance guaranteeing Plaintiffs the benefit of their bargain, while recognizing and allowing for the flexibility of health coverage. To strike this balance, the trial court required the State to provide a "non-contributory (premium-free) heath plan equivalent to the 80/20 regular state health plan," and observed that the most appropriate way to determine this equivalency was through an analysis of actuarial value. (R p 615). By doing so, the trial court recognized that the law was flexible enough to allow for certain changes to health insurance, but strong enough to enforce promises. See Duncan v. Retired Pub. Emples. of Alaska, Inc., 71 P.3d 882, 889, 891–92 (Alaska 2003) (adopting actuarial equivalency to allow health care to evolve while preserving the protected nature of the benefit). To rule otherwise would have been to allow those promises to be breached only because it might be complicated to enforce them.

fifteen alternatives were studied, and that a legislative report cited four such alternatives. (See Doc. Ex. 3634–75; Doc. Ex. 3663–72 [General Assembly Program Evaluation Division, June 14, 2007]). Moreover, the State Health Plan admitted the existence of such alternatives in sworn deposition testimony. (See Doc. Ex. 11178 [Moon Dep. (9-14-15) 115:8–12]).

Bailey governs this issue. However, in keeping with its *modus operandi* in dealing with unfavorable law, the State continues to ignore this precedent. Despite the clear ruling in Bailey, and Plaintiffs' reliance thereupon in its opening brief, Defendants refuse to deal with it at all. Instead, they suggest an allegedly sufficient public purpose of dealing with the State's mounting financial obligation to provide the State Health Plan. As public interests go, this one is certainly ironic: (1) the State undertook to provide the Plan, (2) the State failed to budget for the costs of the Plan, and (3) the State – the argument goes – is therefore justified in impairing its contract to provide the Plan to retirees because of its own failure to pay for it in another manner. This is the logical equivalent of saying you do not owe payment on a contract because you spent the money elsewhere.

When it comes to the requirement that the impairment be "reasonable and necessary," Defendants – without citation to any North Carolina case and

still not dealing with Bailey – simply state that their actions satisfy the test. They then go on to say that any holding to the contrary would render the "reasonable and necessary" component of the impairment analysis moot. Again, this Court saw the situation differently in Bailey. The concern expressed in that opinion is not that the reasonable and necessary analysis would be rendered moot, but that it would swallow whole the constitutional bar on impairing contracts. "If a State could reduce its financial burdens whenever it wanted to spend the money for what it regarded as an important public purpose, the Contract Clause would provide no protection at all." Bailey, 348 N.C. at 152, 500 S.E.2d at 66 (quoting U.S. Trust Co. of N.Y. v. New Jersey, 431 U.S. 1, 25–26 (1977)). So it is not enough simply to say that there was a financial crisis and therefore the State can do what it wants. An analysis of the kind we see in Bailey has to be undertaken in order to determine the reasonableness and necessity of the impairment. That means looking at the existence of alternative means of serving a public interest, including especially those that do not impair vested rights. Defendants attempt to circumvent this Court's analysis in Bailey because they do not like the inescapable result when it is applied here.

CONCLUSION

The Faulkenbury standard is clear. When employees are given requirements to fulfill to receive a benefit and they fulfill those requirements, they have a contract for those benefits. This standard is met here, so the Defendants go looking for a different standard. This Court has consistently held that deferred compensation is contractual, and the benefit here is clearly deferred compensation, so the Defendants seek to rewrite Supreme Court decisions as if to say this Court did not really mean "deferred compensation." This Court defines vested rights as contractual rights, and the State has repeatedly spoken of vesting into the Retirement Health Benefit, so the State contends that they didn't really mean *vesting* as it is understood by this Court, or as it is understood when discussing pension, but that they *really* meant some other kind of "vesting light" which has no contractual teeth. Nor is there any meaning to vesting in the presence of a right to amend, despite the fact this Court has clearly ruled otherwise. The General Assembly may have said they had a right to amend the statute, but the State now says all they *really* meant was there could be no contract, contrary to all of its prior representations and the rulings of this Court. Finally, the breach, though massive, is also *de minimis*, and the solution of gutting vested rights, though

one of over a dozen options, was "necessary," again directly contrary to this Court's decision in Bailey.

The reason we have so much precedent in this case is that the State has a bad habit of making promises about benefits, reaping the benefit of those promises by being able to pay its workers less, and then repudiating the promises to those workers years down the road when they would rather spend the money on something else. The only institution with the ability to protect the otherwise helpless retirees from the State's habit of promise-breaking is our court system. Here, the trial court saw a clear breach and fashioned a remedy which requires the State to give its retirees the benefit of their bargain. But the Defendants come here explicitly arguing that they can gut or even eliminate the benefit Plaintiffs already earned. This Court has applied the brakes to this type of treatment of State retirees in the past, and Plaintiffs hope it will again. In order to do so, Plaintiffs contend that all this Court needs to do is stick to its own precedents that the Defendants desperately try to rewrite, and to the plain meanings of words Defendants desperately seek to redefine. In doing so, this Court would uphold a time-honored principle that Defendants seek to relegate to the history books:

> These holdings reflect a principle as old as the Nation itself: The Government should honor its obligations. Soon after ratification, Alexander Hamilton stressed this insight as a cornerstone of fiscal policy. "States," he wrote, "who observe their engagements . . . are respected and trusted: while the reverse is the fate of those . . . who pursue an opposite conduct." Report Relative to a Provision for the Support of Public Credit (Jan. 9, 1790), in 6 Papers of Alexander Hamilton 68 (H. Syrett & J. Cooke eds. 1962). Centuries later, this Court's case law still concurs.

Maine Community Health Options v. U.S., 140 S. Ct. 1308, 1331 (2020).

For all the foregoing reasons, this Court should reverse the decision of the Court of Appeals and remand the case to the Court of Appeals for further remand to the trial court for reinstatement of the trial court's order.

Respectfully submitted this 17th day of August 2020.

/s/ Michael L. Carpenter
Michael L. Carpenter
N.C. State Bar 35202
mcarpenter@gastonlegal.com
GRAY, LAYTON, KERSH,
SOLOMON, FURR & SMITH, P.A.
Telephone: 704-865-4400
Post Office Box 2636
Gastonia, North Carolina 28053-2636

I certify that all of the attorneys listed below have authorized me to list their names on this document as if they had personally signed it

Sam McGee
N.C. State Bar 25343
smcgee@tinfulton.com
TIN, FULTON, WALKER & OWEN, PLLC
Telephone: 704- 338-1220
301 East Park Avenue
Charlotte, NC 28203

Christopher M. Whelchel
N.C. State Bar 31857
cwhelchel@gastonlegal.com
GRAY, LAYTON, KERSH, SOLOMON, FURR & SMITH, P.A.
Telephone: 704-865-4400
Post Office Box 2636
Gastonia, North Carolina 28053-2636

Marcus R. Carpenter
N.C. State Bar 42730
mrcarpenter@gastonlegal.com
GRAY, LAYTON, KERSH, SOLOMON, FURR & SMITH, P.A.
Telephone: 704-865-4400
Post Office Box 2636
Gastonia, North Carolina 28053-2636

Marshall P. Walker
N.C. State Bar 45040
mwalker@gastonlegal.com
GRAY, LAYTON, KERSH, SOLOMON, FURR & SMITH, P.A.
Telephone: 704-865-4400
Post Office Box 2636
Gastonia, North Carolina 28053-2636

Gary W. Jackson
N.C. State Bar 13976
gary.jackson@farrin.com
THE LAW OFFICE OF
JAMES SCOTT FARRIN
Telephone: 704-599-1078
1001 Morehead Square Dr. Ste 350
Charlotte, North Carolina 28203

J. Bryan Boyd
N.C. State Bar 27726
bboyd@farrin.com
THE LAW OFFICE OF
JAMES SCOTT FARRIN
Telephone: 919-688-4991
280 S. Mangum Street
Durham, North Carolina 27701

ATTORNEYS FOR PLAINTIFFS-APPELLANTS

CERTIFICATE OF SERVICE

I certify that today, I caused the attached documents to be served on all counsel by email, addressed to:

Marc Bernstein
Special Deputy Attorney General
mbern@ncdoj.gov

Ryan Y. Park
Solicitor General
rpark@ncdoj.gov

Attorneys for Defendants-Appellees

J. Michael McGuinness
jmichael@mcguinnesslaw.com

Verlyn Chesson Porte
Verlyn.chessonPorte@ncae.org

Attorneys for Amicus Curiae NCAE

Vernon Sumwalt
vernon@sumwaltgrp.com

Ali Naini
anaini@aarp.org

Attorneys for Amicus Curiae AARP and AARP Foundation

This 17th day of August 2020.

/s/ Michael L. Carpenter
Michael L. Carpenter