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,	)	From Gaston County COA17-1280
Plaintiffs-Appellants,	)	
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.	)	

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PLAINTIFFS-APPELLANTS' NEW BRIEF

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ISSUES PRESENTED

I. Did the Court of Appeals err by concluding that there is no contractual obligation from the State to the Plaintiff Class for the provision of any retirement health benefit or for any specific retirement health benefit?

II. Did the Court of Appeals err by holding that the State had not breached and/or impaired any contracts with Plaintiffs and had not violated the Law of the Land Clause or due process rights by reducing the retirement health benefit that said Plaintiffs had previously vested into?

III. Did the Court of Appeals err in holding that the retirement health benefit is neither deferred compensation nor a vested retirement benefit?

IV. Did the Court of Appeals err in not applying all three standards set forth in NCAE in determining whether there was a contractual obligation between the Defendants and the Plaintiffs?

INTRODUCTION

Since the early 1980's, state employees who fulfilled certain service requirements in the employ of the State were promised premium-free health insurance through the State Health Plan's regular plan for the duration of their retirement (hereinafter referred to as the "Retirement Health Benefit(s)" or "RHB"). The enabling legislation contains a vesting provision and evidences an intent to obligate the State to provide the Retirement Health Benefits as part of an overall retirement compensation package. In addition, numerous documents and oral representations made to employees and retirees evidence

an unmistakable intent to offer a contractual benefit, by using words such as "earned," "obligation," "compensation," "vested," and "contract" to refer to the Retirement Health Benefits. The Plaintiff Class in this case composed of over 222,000 state retirees all received the same promise and performed their end of the bargain by working for the State for the required term of years.

For decades, this Court has consistently held that retirement benefits earned by public employees are contractual in nature and legally protected from retroactive reduction. This simple precedent has been uniformly followed and applied by lower courts of this state for a range of different types of benefits offered during retirement. The trial court in this case judiciously followed this precedent. Unfortunately, this unbroken string of consistent precedent was upended by a panel of the Court of Appeals in this case who completely failed to follow this Court's holdings in cases such as Bailey v. State, 348 N.C. 130, 500 S.E.2d 54 (1998), Faulkenbury v. Teachers' and State Employees' Retirement System of North Carolina, 345 N.C. 683, 483 S.E.2d 422 (1997), and Simpson v. North Carolina Local Government Employees' Retirement System, 88 N.C. App. 218, 363 S.E.2d 90 (1987), aff'd per curiam, 323 N.C. 362, 372 S.E.2d 559 (1988), and misapplied this Court's more recent ruling in N.C. Ass'n of Educators v. State, 368 N.C. 777, 786 S.E.2d 255 (2016)

("NCAE"). The Court of Appeals erred in failing to consider any evidence beyond the statutes themselves, ignored contractual language contained in the statutes, and failed to apply this Court's standard for determining the existence of a contract for retirement benefits.

No different than the Plaintiff Classes in Bailey or Faulkenbury, the Plaintiff Class here only asks for what they were promised and had already earned through years of service to the State. Despite the correct ruling by the trial court, the Court of Appeals' decision not only denied them the relief they requested, but went far beyond that in holding that the Retirement Health Benefits that have been a part of the State Retirement System for nearly 40 years are not contractual in any way – thereby endorsing the complete termination of a benefit that hundreds of thousands of retirees and current employees already are or will rely upon in their retirement.

STATEMENT OF THE CASE

Plaintiffs brought this suit on behalf of themselves and all other similarly situated North Carolina retirees on 20 April 2012 alleging breach of contract, unconstitutional impairment of contract, unconstitutional violation of due process and the Law of the Land, and requested a writ of mandamus or

in the alternative injunctive relief, a declaratory judgment and a constructive trust/common fund. The Chief Justice designated the case as exceptional under General Rule of Practice 2.1 and assigned the case to Superior Court Judge Edwin G. Wilson, Jr. (R pp 33–34).

Defendants moved to dismiss the Complaint on 29 June 2012 pursuant to Rule 12(b). (R pp 27–32). Judge Wilson denied the Defendants' motion to dismiss in full on 21 May 2013. (R pp 35–36). Defendants appealed that order on the basis of sovereign immunity. See Lake v. State Health Plan for Teachers & State Emples., 234 N.C. App. 368, 760 S.E.2d 268 (2014). On 17 June 2014, the Court of Appeals affirmed the denial of the Defendants' Motion to Dismiss finding that the benefits at issue were in the nature of a contractual obligation. See id. at 374–75, 760 S.E.2d at 273–74. The Defendants petitioned this Court for discretionary review and for issuance of a writ of certiorari and this Court denied said petition/writ. Lake v. State Health Plan for Teachers & State Emp., Nos. 436P13-1, 436P13-2.

On 11 October 2016, the trial court certified a class that includes nearly all retired state employees who were eligible to enroll in the State Health Plan as of 1 September 2016. The class includes over 222,000 retirees or their estates. (R pp 375–80). After discovery, the Plaintiffs moved for partial

summary judgment and the Defendants moved for summary judgment. The trial court entered partial summary judgment for the Plaintiffs, and denied Defendants' motion. (R pp 612–20). The summary judgment order relied upon this Court's prior rulings in Bailey and Faulkenbury and, consistent with those precedents, found that the retired Plaintiff class members had vested rights to premium-free health insurance under the current continuation of the Regular State Health Plan. (R pp 612–20). The trial court also entered a declaratory judgment in Plaintiffs' favor declaring the rights of the Plaintiff class members to retirement health benefits consistent with the evidence and applicable Supreme Court decisions and finding that such benefits were deferred compensation and contractual in nature. (R pp 620).

Defendants appealed from the trial court's order, and the Court of Appeals docketed the appeal on 20 November 2017. The parties filed a Joint Petition for Discretionary Review to Bypass the Court of Appeals. See Bypass Petition, Lake v. State Health Plan for Teachers & State Emp., No. 436P13-3. On 9 October 2018, an "Administrative Statement of the Clerk of the Supreme Court" was issued stating that there was not at that time a quorum on the Court to take action on the Petition and that a decision was being deferred, but that if the Court later determined it had a quorum sufficient to permit it

to act, the Court could then take action on the Petition. See Administrative Statement of the Clerk of the Supreme Court, Lake v. State Health Plan for Teachers & State Emp., No. 436P13-3 (N.C., Oct. 9, 2018). After the issuance of the Administrative Statement, the Court of Appeals held oral argument on 29 November 2018. On 5 March 2019, the Court of Appeals issued an opinion reversing the decision of the trial court and remanding for entry of summary judgment in favor of the Defendants. See Lake v. State Health Plan for Teachers & State Emples., _____ N.C. App. _____, 825 S.E.2d 645 (Ct. App. 2019). The opinion did not address nor make a specific holding as to the determination of the declaratory judgment claim. See id. The Plaintiffs filed their Petition for Discretionary Review and Writ for Certiorari on 9 April 2019. This Court granted that Petition on 26 February 2020.

STATEMENT OF THE GROUNDS FOR APPELLATE REVIEW

Pursuant to Article IV, Section 12(1) of the North Carolina Constitution, this Court has "jurisdiction to review upon appeal any decision of the courts below" and is empowered to "issue any remedial writs necessary to give it general supervision and control over the proceedings of the other courts." Further, under the statutory authority in N.C.G.S. § 7A-31, this Court may

specifically exercise discretionary review of opinions from the Court of Appeals.

Following the decision of the Court of Appeals, which disposed of the entire case by remanding to the trial court for entry of summary judgment in favor of Defendants on all claims and dismissal of Plaintiffs' complaint, the Plaintiffs filed their Petition for Discretionary Review and Writ for Certiorari seeking review by this Court[1]. By Order dated 26 February 2020, this Court allowed discretionary review pursuant to N.C.G.S. § 7A-31.

STATEMENT OF THE FACTS

A. The Retirement Health Benefit

In 1982, the State codified the terms of coverage under the State Health Plan, including the eligibility provisions for retired state employees and teachers. See Act of June 23, 1982, ch. 1398, § 6, 1982 N.C. Sess. Laws 288, 289–311. In order to receive the Retirement Health Benefit portion of their retirement compensation package, State retirees had to vest, that is, to meet certain requirements of service to the State. Initially, employees vested merely by retiring from their employment with the State and receiving pension

[1] To the extent review by the Court of Appeals was improper as interlocutory, the decision of the Court of Appeals must be vacated.

benefits. See N.C.G.S. § 135-40.1(17) (1986). Effective in 1988, this was prospectively changed to require that all employees would need to have at least five years of "contributory retirement service" to vest. Session Law 1987-857, codified at N.C.G.S. § 135-40.1(17). Every class member vested into the retirement system. (R pp 378–79, ¶ 1). By definition, all 222,000+ class members completed all of the work required by the State to receive the Retirement Health Benefit. (See id.). The class itself is defined to exclude anyone who did not. (See id.)

Under the Retirement Health Benefit's statutory scheme, the State "undertakes" to provide the Retirement Health Benefit, and "will pay" Retirement Health Benefits in accordance with the statutory terms. N.C.G.S. § 135-40 (1982) ("Undertaking"). Subsequent legislative history regarding prospective changes to eligibility requirements in 2006 specifically references retiree "vesting" and refers to the Retirement Health Benefit as an "obligation" that is "earned" by employees. See Session Law 2006-174 (S.B. 837) (Short Bill Title "State Health Plan / 20 Year Vesting"); Session Law 2006-174 (S.B. 837) (prior un-enacted version listing the Short Bill Title as "State Health Plan / 10 Year Vesting"); (Doc. Ex. 725 [Legislative Actuarial Note forming the basis for Session Law 2006-174 showing "short title" as "State Health Plan/20-Year

Vesting]); (Doc. Ex. 4764 [earlier edition of Actuarial Note based on 10-year vesting]).

B. The State's Representations of a Contract[2]

In representing the Retirement Health Benefit to its potential and current employees, the State consistently used contractual language in describing the Retirement Health Benefit. This language has been used repeatedly in "Your Retirement Benefits" booklets given to Plaintiffs as well as in actuarial reports, press releases, and oral communications to the retirees. These publications communicated to employees what they must do to become "vested" or to "earn" the "compensation" of the Retirement Health Benefit. They used words like "earned," "vested," and "obligation." They characterized the Retirement Health Benefit as being part of the employee's total deferred compensation package with the State. These benefits were represented to be for a "lifetime." Defendants have conceded that there was an obligation to provide at least some form of retirement health benefits to those who had already vested. Plaintiffs relied upon the Retirement Health Benefit in making their employment decisions to work for the State for a lower salary.

[2] For detailed citations with regard to the use of contractual language by the State, see § III, infra and the attached Vesting References List.

C. The Breach

Before 2011, retirees were not required to pay a monthly premium for individual coverage under the Regular State Health Plan. (See Doc. Ex. 3056–60). Alternative plans, that sometimes charged additional premiums, were added as options from time to time in order to provide flexibility, but for decades the Retirement Health Benefit was always provided and has always been described by the State as the "Regular State Health Plan" or the "Standard Plan." (See, e.g., Doc. Ex. 12910–16 (citing SHP enrollment forms from 1988 to 2011 referring to the primary health benefit plan as the "Regular State Health Plan" and "Standard" plan); Doc. Ex. 4496 [Highlights of Your Retirement Benefits, July 2004] ("When you retire … provided you have at least 5 years of retirement membership service earned as a teacher or State employee. The State pays the full cost of your individual coverage under *the regular State insured plan*.") (emphasis added); Doc. Ex. 4240 [Your Retirement Benefits, January 2005] (stating same); Doc. Ex. 4079 [Your Retirement Benefits, 2001]) (same); Doc. Ex. 4278 [Your Retirement Benefits, January 2006] ("[T]he State will pay for your individual coverage under *the regular State insured plan* . . . .")).

In 2011, the General Assembly authorized the State Health Plan to charge state employees and retirees a monthly premium for individual coverage for the Regular State Health Plan for the first time. See Act of May 11, 2011, ch. 85, § 1.2(a), 2011 N.C. Sess. Laws 119, 120. Pursuant to that authorization, in September 2011, the State Health Plan began charging premiums for the Regular State Health Plan. (See Doc. Ex. 3062). The State continued to offer a premium-free plan to retirees, but those plans were of lesser value than the Regular State Health Plan previously provided to retirees. (See Doc. Ex.11228 [Moon Dep. [9-14-15] 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. 132 [Fuhrer Report]; Doc Ex. 1097 [McCarthy Report]; Doc Ex. 12835 [Response to Request for Admission No. 30]). From 2011 to 2016, the base premium charged for the Regular State Health Plan increased by a factor of five. (Compare Doc Ex. 3061 [Monthly Contribution Rates for 2011] (showing base premium rate of $26.62) to Doc Ex. 3515 [Enhanced 80/20 Plan Monthly Premium Rates] (showing a base premium of $104.20); R p 617).

ARGUMENT

I. Standard of Review

"This Court reviews appeals from summary judgment de novo." United Cmty. Bank (Ga.) v. Wolfe, 369 N.C. 555, 558, 799 S.E.2d 269, 271 (2017) (quoting Ussery v. Branch Banking & Tr., 368 N.C. 325, 334–35, 777 S.E.2d 272, 278 (2015)). "Summary judgment is properly granted when the forecast of evidence 'reveals no genuine issue as to any material fact, and when the moving party is entitled to a judgment as a matter of law.'" Dobson v. Harris, 352 N.C. 77, 83, 530 S.E.2d 829, 835 (2000) (quoting Koontz v. City of Winston-Salem, 280 N.C. 513, 518, 186 S.E.2d 897, 901 (1982)).

II. The Court of Appeals Misapplied this Court's Precedent as Set Forth in NCAE, Bailey, and Faulkenbury

This Court has established a long line of precedent concerning alleged violations of the Contracts Clause in the context of government-employment contracts. In those cases, this Court treated the relationship between governmental employers and employees as fundamentally contractual in nature. In granting summary judgment in favor of the Plaintiffs, the trial court properly relied on this Court's prior precedent, specifically as set forth in Bailey and Faulkenbury, in determining that the Retirement Health Benefit was deferred compensation and therefore contractual. (R pp 612–20). The

precedent set in Bailey and Faulkenbury was re-visited and confirmed in this Court's latest opinion on the subject – NCAE. Unfortunately, the Court of Appeals in the case *sub judice* altogether disregarded the standards set forth in Bailey and Faulkenbury, and misapplied NCAE. In doing so, the Court of Appeals effectively created a new test out of whole cloth that is not consistent with this Court's jurisprudence.

a. Relevant Case History

Since 1942, this Court has recognized that retirement benefits earned by State employees are deferred compensation and contractual in nature. See Bridges v. City of Charlotte, 221 N.C. 472, 482, 20 S.E.2d 825, 832 (1942). Specifically, in Bridges, the Court held that benefits paid to retired teachers were deferred compensation and not a mere gratuity. See id. The Court indicated that were it to hold otherwise, the retirement plan would be unconstitutional under the exclusive emoluments clause of the state constitution. See id. at 482, 20 S.E.2d at 832 (citing N.C. Constitution, Art. I, Sec. 7); see also Leete v. County of Warren, 341 N.C. 116, 121, 462 S.E.2d 476, 479 (1995) ("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.").

Some years later, this Court further reinforced the application of contract law and deferred compensation principles to public employees, and specifically their retirement benefits, when it affirmed *per curiam* the Court of Appeals' detailed opinion in Simpson. In Simpson, the court was tasked with determining whether "the pension rights of vested members of the North Carolina Local Government Employees' Retirement System (Retirement System) may be made subject to adverse legislative modification" without violating the Contracts Clause. Id. at 219, 363 S.E.2d at 91. The court answered that question in the negative and held that the State could not reduce the retirement benefits of an employee who had met the five-year eligibility criteria of creditable service. See id. at 219 & n.2, 223–26, 363 S.E.2d at 91 & n.2, 93–95. This is because an employee has a contractual, vested right to a benefit that is deferred compensation already earned through his or her prior service. See id. at 223, 363 S.E.2d at 94. As the court further elaborated:

> 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 rights bargained for in exchange for his loyalty and continued

> services, and continually promised him over many years, will not be removed or diminished.

Id. at 223–24, 363 S.E.2d at 93–94.

Just prior to Simpson, the Court of Appeals had recognized contractual rights to vacation leave for certain firefighters. See Pritchard v. Elizabeth City, 81 N.C. App. 543, 344 S.E.2d 821 (1986) review denied, 318 N.C. 417, 349 S.E.2d 598 (1986). In Pritchard, the Court of Appeals held that the firefighters were owed accumulated vacation leave under a vacation leave policy that was mentioned in an ordinance but carried out through oral promises made by the fire chief. See id. at 551–53, 344 S.E.2d at 826–27. The Court of Appeals held that the vacation leave was previously earned through the firefighters' employment service, stating "the firefighters are not seeking to prevent the city from changing the benefits to be earned in the future; they seek to recover for benefits allegedly already conferred on them by virtue of the ordinance and their contracts for services previously rendered." Id. at 552–53, 344 S.E.2d at 826. The court further noted that, while the ordinance there was not the actual contract, it became a part of the employment contract between the employees and government: "Although the 1972 ordinance fixed the terms of the vacation leave benefit program, it did not, in itself, form a contract with

the employees. Once employment was offered and accepted under the compensation plan set out in the ordinance, however, its provisions become part of the contract." Id. at 552, 344 S.E.2d at 826; see also Bolick v. County of Caldwell, 182 N.C. App. 95, 96, 100–01, 641 S.E.2d 386, 388, 390 (2007) (citing Pritchard and holding that a personnel policy could supply the terms of a contractual right to a severance package that had been offered to employees).

A decade later, this Court again addressed the foregoing principles in a case concerning disability retirement benefits for State employees. In Faulkenbury, this Court held that disability retirement benefits earned by employees who worked for the requisite period were contractual and could not be impaired. As this Court explained:

> The Court of Appeals held and we affirmed in *Simpson v. N.C. Local Gov't Employees' Retirement Sys.,* 88 N.C. App. 218, 363 S.E.2d 90 (1987), *aff'd per curiam,* 323 N.C. 362, 372 S.E.2d 559 (1988), a case almost on all fours with this case, that the relation between the employees and the governmental units was contractual. *Simpson* governs this case. At the time the plaintiffs' rights to pensions became vested, the law provided that they would have disability retirement benefits calculated in a certain way. These were rights that they had earned and that may not be taken from them by legislative action.
>
> The defendants argue *Simpson* is wrong and should be overruled. They say this is so because the statutes upon which the plaintiffs rely are not promises, but only state a

> policy which the General Assembly may change. We believe that a better analysis is that at the time the plaintiffs started working for the state or local government, the statutes provided what the plaintiffs' compensation in the way of retirement benefits would be. The plaintiffs accepted these offers when they took the jobs. This created a contract.

Id. at 690, 483 S.E.2d at 427. Identically to this case, the State in Faulkenbury further argued that the statute did not sufficiently demonstrate an intent that the benefits be offered as part of a contract. Id. at 691, 483 S.E.2d at 427. This Court soundly rejected those arguments:

> The defendants argue that there is nothing in the statutes that shows the General Assembly intended to offer the benefits as a part of a contract, and without such an intent, there can be no contract. *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*.

Id. (emphasis added). Once the employees fulfilled the requisite condition, their "rights to benefits in case they were disabled became vested" and the State "could not then reduce the benefits." Id. at 692, 483 S.E.2d at 428.

Soon after Faulkenbury, this Court had yet another occasion to evaluate the contractual nature of public retirement benefits in Bailey. In that case,

retired state employees challenged legislation that placed a $4,000 cap on the state-tax-exempt status of retirement payments from several differing mandatory, optional, and supplementary retirement programs. See Bailey, 348 N.C. at 136–39, 500 S.E.2d at 58–59. In summarizing the various retirement programs at issue, Chief Justice Lake, writing for the Court, stated as follows:

> Each of these systems contains certain preconditions to the receipt of benefits. The primary one is the requirement that employees work a predetermined amount of time in public service before they are eligible for retirement benefits. After employment for the set number of years, an employee is deemed to have "vested" in the retirement system. Thereafter, the employee generally is guaranteed a percentage payment at retirement based upon years of service.

Id. at 138, 500 S.E.2d at 58. In addition, aside from the relevant statutes themselves, there was evidence of representations concerning the exemptions by the State and reliance by the employees on such representations:

> Numerous employee witnesses testified that defendants' agents offered the exemptions as a type of compensation to employees of state and local governments. The testimony reveals that often the exemption of benefits from taxation was communicated to prospective employees with the intent of inducing individuals to either begin or continue public service employment. Moreover, testimony and exhibits offered at trial establish that innumerable communications were made to plaintiff public employees

> throughout their careers, both orally and in writing (including multiple unequivocal written statements in official publications and employee handbooks) that their retirement benefits would be exempt from state taxation. Plaintiffs assert they relied on such statutes and communications as assuring compensation in the form of such exemption in exchange for public service.

Id. at 138–139, 500 S.E.2d at 58–59.

This Court reaffirmed the contractual and deferred compensation principles espoused in Simpson, and then went through an exhaustive examination of North Carolina case law "confirm[ing] that the contractual relationship approach taken by the Court of Appeals in *Simpson* and [the Court's] subsequent decisions is the proper one." Id. 142–46, 500 S.E.2d at 60–63. This Court noted that North Carolina cases "have long demonstrated a respect for the sanctity of private and public obligations from subsequent legislative infringement." Id. at 142, 500 S.E.2d at 61. Citing a number of such cases, including Pritchard, this Court stated that "[t]his respect for individual rights has manifested itself through the expansion of situations in which courts have held contractual relationships to exist, and in which they have held these contracts to have been impaired by subsequent state legislation." Id. at 143–44, 500 S.E.2d at 61–62. "The basis of the contractual relationship determinations in these and related cases is the principle that where a party

in entering an obligation relies on the State, he or she obtains vested rights that cannot be diminished by subsequent state action." Id. at 144, 500 S.E.2d at 62.

Ultimately, the Court in Bailey concluded that the plaintiffs had a contractual right to the tax exemption, as a term of their retirement contracts, relying on a variety of non-dispositive evidence, including, for example, the proximity of the tax exemption to other statutorily created benefit terms, "communication of the exemption by governmental agents in both written and oral form, use of the exemption as inducement for employment," the "establishment of a set time period for vesting, and the reliance of employees upon retirement compensation in exchange for their services." Id. at 146, 150, 500 S.E.2d at 63, 66.

Building on certain of the principles from Bailey and Pritchard, the Court of Appeals held in Stone v. State, 191 N.C. App. 402, 664 S.E.2d 32 (2008), that State retirees had a "contractual right to the funding of the Retirement System in an actuarially sound manner." Id. at 414, 664 S.E.2d at 40. The court in Stone, in addition to looking at the statutes, evaluated the record evidence in reaching its holding, including representations concerning the funding. See

id. Such representations included statements in a "Your Retirement System" pamphlet and a "Your Retirement Benefits" pamphlet. See id.

The latest in the line of cases from this Court concerning contractual rights of government employees is NCAE. There, the plaintiffs filed suit against the State alleging that the General Assembly's repeal of North Carolina's Career Status law violated the Contract Clause. See NCAE, 368 N.C. at 778–79, 786 S.E.2d at 257–58. That repeal revoked the career status of teachers who had already earned that status by working the requisite number of years and entering into contracts with their local school board. See id. In evaluating whether a contractual obligation existed, the Court effectively applied three separate tests: (1) focusing on whether the statute at issue contained certain specific language of contract pursuant to federal case law; (2) evaluating the benefit and statute at issue according to the standard established by this Court's own jurisprudence as set forth in Bailey and Faulkenbury; and (3) alternatively assessing whether a contract had been formed that incorporated the law at issue under the long-standing tenet that "[l]aws which subsist at the time and place of the making of a contract . . . enter into and form a part of it . . . ." Id. at 786–89, 786 S.E.2d at 262–64. The opinion in NCAE makes clear that if any *one* of the foregoing standards are

satisfied, then there is a contractual obligation. See id. (holding that there was no contractual obligation under the first two tests but that there was a contractual obligation to career status under the third test).

This Court in NCAE first looked to the standard under federal case law, and, relying on two federal cases specifically involving teacher tenure, the Court evaluated whether the Career Status Law "provides for the execution of a *written* contract on behalf of the state." Id. at 787, 786 S.E.2d at 263 (quoting Dodge v. Bd. of Educ., 302 U.S. 74, 78 (1937)) (internal quotation marks omitted) (emphasis added). The Court held, however, that it did not meet the standard from those cases because the word "contract" did not appear in the relevant portion of the Career Status Law[3]. See id.

This Court did not stop its analysis with the federal standard, as this Court then turned to its own prior cases to apply the second of the three tests. In next looking to Bailey and Faulkenbury to determine whether the Career

[3] It bears noting that prior to NCAE this Court had not expressly referenced the federal standard in evaluating whether our State's statutes give rise to contractual obligations for public employees. In fact, these types of arguments had been seemingly rejected by this Court in Faulkenbury and in the *per curiam* adoption of Simpson. See Faulkenbury (rejecting argument by State the statutes were not promises, but merely state a policy); Simpson (rejecting approach that would require "an unmistakable expression of legislative intent to contract").

Status Law created contractual rights under our State jurisprudence, this Court recognized and reaffirmed the well-established principle in North Carolina that the requisite intent to contract is present in situations where benefits are earned in the present and the fruits deferred until a later time:

> In [Bailey and Faulkenbury], this Court held that vested contractual rights were created by the statutes at issue because, at the moment the plaintiffs fulfilled the conditions set out in the two benefits programs, the plaintiffs earned those benefits. Though the benefits would be received at a later time, the plaintiffs' right to receive them accrued immediately, became vested, and a contract was formed between the plaintiffs and the State. In other words, neither the retirement benefits in *Bailey* nor the disability payments in *Faulkenbury* were based upon future actions by the plaintiffs. Instead, those benefits had been presently earned and became vested as the plaintiffs performed, even though payment of those benefits was deferred until a later time.

NCAE, 368 N.C. at 788, 785 S.E.2d at 263–64. Regardless of the specific verbiage used in the relevant statute (e.g., the use of the word "contract"), "when the General Assembly [has] 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" a contract is created upon fulfilment of those conditions. Faulkenbury, 345 N.C. at 691, 483 S.E.2d at 427. In such situations any required intent to contract is impliedly present. See id.

In NCAE, the Career Status Law merely provided that a teacher could *potentially enter* into a career contract, upon working for the requisite period, and *only if* their local school board thereafter voted to grant career status. See NCAE, 368 N.C. at 788, 785 S.E.2d at 264. The Career Status Law therefore did not meet the Bailey/Faulkenbury deferred compensation and vested right standard.

After determining that the Career Status Law did not meet the Bailey/Faulkenbury standard, the Court applied the third test under the principle that "[l]aws which subsist at the time and place of the making of a contract . . . enter into and form a part of it . . . ." Id. at 789, 786 S.E.2d at 264 (quoting Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 429–30 (1934)). This Court held that the plaintiffs' right to career status, while not vested by the statute alone, became vested upon entering into those subsequent individual contracts with their school boards and thereafter could not be impaired. See id. This Court held that the "contracts between the local school boards and teachers with approved career status included the Career Status Law as an implied term upon which teachers relied." Id. at 790, 786 S.E.2d at 264.

In reaching its ultimate determination that there was a contractual relationship, this Court in NCAE considered the evidence in the record, including statements by the plaintiffs and a school superintendent regarding the value of the benefits to the plaintiffs and the plaintiffs' reliance on those benefits in accepting and continuing in their positions. See id. at 789, 786 S.E.2d at 264 (discussing, for example, record evidence that " '[t]eachers rely upon their career status rights in making employment decisions'; '[w]hen interviewing and hiring teachers, teachers frequently ask about career status rights'; and such protections have value to prospective teachers which "makes up for not having better monetary compensation.' "). This Court's reliance on such materials in NCAE further buttressed the extensive precedent in this State that benefit handbooks, pamphlets, written correspondence and even oral representations to public employees can serve to create or evidence a contract between the employee and the State. See Stone, 191 N.C. App. at 411, 414, 664 S.E.2d at 38, 40; Bailey, 348 N.C. at 138–39, 146, 500 S.E.2d at 58–59, 63; Bolick, 182 N.C. App. 95, 100, 641 S.E.2d 386, 390; Pritchard, 81 N.C. App. at 552–53, 344 S.E.2d at 826–27.

b. What the Long Line of Cases all Have in Common

In sum, North Carolina Courts have consistently applied certain basic notions of contract construction from the same line of precedent in various pension and non-pension cases and held the benefits to be contractual in nature, including the following examples:

- Pension (Bridges);
- Disability (Simpson / Faulkenbury);
- Tax Exemptions for Certain Retirement Benefits (Bailey);
- Special Separation Allowances (Wiggs v. Edgecombe Cnty., 361 N.C. 318, 324, 643 S.E.2d 904, 908 (2007));
- Vacation Leave (Pritchard); and
- Severance (Bolick).

A close examination of these sampling of cases reveals a pattern of factors and elements that our Courts have used to determine the existence of a contractual benefit. The chart below summarizes the similarities between those cases.

	Bridges	Simpson	Faulkenbury	Bailey	**Lake**	Wiggs	Pritchard	Bolick
Employer/ Employee Relationship	■	■	■	■	■	■	■	■
Eligibility Requirements	■	■	■	■	■	■	■	■
Deferred or Post Employment Benefit	■	■	■	■	■	■	■	■
Employer Contributions	■	■	■		■	■	■	■
Trust Fund	■	■	■		■			
Actuarial Valuation	■	■	■		■			
Chapter 135	■		■	■	■			
Monetary Employee Contributions	■							

As can be seen from the chart above, there are three foundational elements that all these cases share in common: (1) the existence of an employer-employee relationship; (2) that an employee works for a set period of time to fulfill an eligibility requirement; and, (3) the benefit is to be provided at some point in the future. Many of the cases share additional but not required elements such as the existence of employer contributions, the use of a trust fund, the utilization of actuarial valuations in the administration and valuation of the benefit, and codification in Chapter 135 of the General

Statutes. As will be discussed in § III infra, the facts in this case share far more of these elements than many of the other cases where courts have held that there were contractual benefits. As stated in the next section below, the Court of Appeal's decision ignored these foundational attributes and instead created a new standard to justify reversing the trial court's order.

c. The Court of Appeals' Decision Disregarded and Misapplied this Court's Binding Precedent

In erroneously holding that there is no contractual obligation in this case, the Court of Appeals misapplied the law, culminating in what can only be described as an altogether new test or framework that is not consistent with or supported by the prior case law in this State, including this Court's binding precedent. Perhaps most glaring, the Court of Appeals failed to sufficiently analyze whether the benefits at issue here met the standards for contractual obligations under North Carolina jurisprudence and failed to evaluate *any* of the abundant record evidence. Instead, the Court of Appeals entirely based its holding, first, on its (misguided) determination of purported factual distinctions between pension and the Retirement Health Benefit, including relying on two non-binding, inapposite cases from other jurisdictions, and

then, second, the standard from federal case law (i.e., the express language of the statute). That was in error as described below.

i. Failure to Apply Deferred Compensation Principles

In lieu of actually applying the Bailey and Faulkenbury deferred compensation standards, the Court of Appeals proceeded to make arbitrary distinctions between pension benefits and the Retirement Health Benefit in an apparent attempt to distinguish those cases.[4] See Lake, 825 S.E.2d at 651–52. The result by implication of the Court of Appeals' new analysis is that the deferred compensation principles in Bailey and Faulkenbury have been relegated to the pension context. In other words, under the Court of Appeals' view, if the benefit at issue is different from pensions, then it cannot be deferred compensation and Bailey and Faulkenbury are meaningless and simply do not apply at all.

As a threshold matter, the Court of Appeals' analysis on this front is flawed because the deferred compensation principles in Bailey/Faulkenbury have never been held to be limited to the pension context. First, in looking to those specific decisions, Faulkenbury, for example, used expansive terms like

[4] The Court of Appeals' decision describes Bailey and Faulkenbury as "pertaining to and interpreting pension and disability retirement benefits". Lake, 825 S.E.2d at 651.

"certain benefits" and "certain conditions" rather than the exact benefits and conditions in that case when explaining its holding. Faulkenbury, 345 N.C. at 691, 483 S.E.2d at 427. Further, in Bailey, the Court went through an exhaustive recitation of the historic application of contractual and deferred compensation principles in a number of contexts, not limited to pension. Bailey, 348 N.C. at 142–46, 500 S.E.2d at 60–63. The Court of Appeals' analysis is also in conflict with NCAE, which evaluated a *teacher tenure* benefit under the Bailey/Faulkenbury principles. There, this Court did not seek to distinguish Bailey and Faulkenbury as dealing with pension. See NCAE, 368 N.C. at 788, 786 S.E.2d at 263–64. Rather, this Court applied those principles and ultimately determined that career status did not meet the standard because it was dependent on a future discretionary action.[5] See id.

The errors in the Court of Appeals' new standard are further demonstrated in looking at the specific purported distinctions it found and elevated. For example, the Court of Appeals apparently found it most significant that a mandatory portion of salary is deducted to be deposited toward future pension benefits whereas the Retirement Health Benefit is "not

[5] In the present case, such a future discretionary action is not present and the Court of Appeals did not identify one.

mandatory," with employees becoming "eligible" and having the option (but not requirement) for payroll deduction to pay for the benefits. Lake, 825 S.E.2d at 652. The significance that the Court of Appeals ascribed to this issue is not supported by this Court's prior precedent. Specifically, while Bailey mentioned "mandatory participation" as one of a host of factors considered, that factor did not even apply to all of the tax exemptions at issue and which were held to be contractual. Bailey, 348 N.C. at 136–38, 146, 500 S.E.2d at 57–58, 63. Bailey involved tax exemptions related to thirteen separate retirement systems and plans, and only a subset of those were mandatory. See id. at 136–37, 500 S.E.2d at 57–58. Other plans at issue in the case were "optional defined contribution or defined benefit plans" and "noncontributory defined benefit plans." Id. at 137–38, 500 S.E.2d at 58. The more important point in Bailey was that under each of the systems, 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'". Id. at 138, 500 S.E.2d at 58 (emphasis added). In fact, the Simpson decision, affirmed *per curiam* by this Court, stated that "[c]ourts have generally been more likely to find vested contractual rights arising out of voluntary plans than out of

mandatory ones." Simpson, 88 N.C. App. at 222, 363 S.E.2d at 93. This is in direct contradiction to the Court of Appeals' opinion in this case.

Other of the Court of Appeals' distinctions suffer similar problems. For instance, the Court of Appeals relies on the notion that the Retirement Health Benefit, unlike pensions, "is not dependent upon an employee's position, retirement plan, salary, or length of service." Lake, 825 S.E.2d at 652. However, there is no basis in the prior case law for this having any significance, let alone being dispositive in any way. Furthermore, it is in conflict with the facts from prior cases. See, e.g., Bailey, 348 N.C. at 138, 146, 500 S.E.2d at 58 (tax exemption did not vary based on position, salary, or length of service – if employees met the minimum required number of years employed, then those employees were all entitled to the same blanket tax exemption). At other points, the Court of Appeals ignored the statutory language in favor of substituted language to make its distinctions work. See Lake, 825 S.E.2d at 652 (arguing that the State "endeavors" to provide the State Health Plan, ignoring the actual language in the "undertaking" clause of the statute).

Doubling down on its "distinction" analysis, the Court of Appeals centrally relied on two out-of-state cases,[6] Studier v. Michigan Public School Employees' Retirement Board, 698 N.W.2d 350 (Mich. 2005), and Davis v. Wilson County., 70 S.W.3d 724 (Tenn. 2002). However, those cases are completely inapposite. In Studier, the Supreme Court of Michigan was tasked with determining whether healthcare benefits fit within a very specific state constitutional provision and the specific terminology used therein, including the term "accrued financial benefits." Studier, 698 N.W.2d at 355–60. The court held that the constitutional provision "only protects those financial benefits that increase or grow over time," and the court's analysis regarding years of service and salary was for the specific purpose of evaluating whether a health care benefit was "accrued", and increased or grew over time. Id. at 358. In this State, there is no similar constitutional provision governing either pensions or retirement health care benefits, as the Court of Appeals acknowledged, and the terminology as used in Studier is simply irrelevant under our North Carolina precedent.

[6] Those cases had been cited, but with little to no discussion, by Defendants in a footnote in their appellate brief.

In Davis, the Supreme Court of Tennessee relied heavily on prior precedent in that state where health care had been established as a "welfare benefit" under an adoption of an ERISA-styled analysis. Davis, 70 S.W.3d at 727 (citing Hamilton v. Gibson County Utility District, 845 S.W.2d 218 (Tenn. Ct. App. 1992). Such an analysis is not found in our State's legal precedent, and regardless, the Court of Appeals did not even attempt to apply it.

ii. Failure to Consider Abundant Record Evidence of Contract

In Bailey, NCAE, Stone, Bolick, and Pritchard, this Court and the Court of Appeals looked to evidence of contract outside of the particular statute at issue. However, after reviewing the statute here under the federal standard (e.g., looking to whether the statute literally contained the word "contract"), the Court of Appeals declined to even consider the abundant record evidence, including the representations and promises made to the Plaintiffs. See Lake, 825 S.E.2d at 653–54. The Court of Appeals attempted to justify this refusal in a cursory fashion by falling back to its erroneous distinctions between the Retirement Health Benefit and pensions:

> We have already distinguished the differences between the mandatory and contributory retirement benefits and the State's policy to offer optional health care benefits. *Stone* has no application to the case at bar.

> The other cases Plaintiffs cite for support, *Bailey*, 348 N.C. at 146, 500 S.E.2d at 63; *Bolick*, 182 N.C. App. at 100-01, 641 S.E.2d at 390; and *Pritchard*, 81 N.C. App. at 552-53, 344 S.E.2d at 826-27, fail to support their arguments for similar reasons.

Id. at 654. The consideration of competent evidence does not turn on a supposed distinction between pension and other retirement benefits. This Court has routinely examined a totality of the circumstances surrounding offers to retirees and employees, whether it be oral and written communications, pamphlets, or testimony from the parties. See, e.g., Bailey, 348 N.C. 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);[7] NCAE, 368 N.C. at 789, 786 S.E.2d at 264 (considering record evidence that showed that teachers were promised and relied upon the career status rights in making employment decisions and that such rights have value and "make[] up for not having better monetary compensation"). The Court of Appeals clearly should

[7] It additionally bears noting that the Court of Appeals did not address numerous other factors mentioned as competent evidence of contract in Bailey and which are present in this case. See Bailey, 348 N.C. at 146, 500 S.E.2d at 63 (noting additional factors such as "use of the [benefit] as inducement for employment," the "establishment of a set time period for vesting, and the reliance of employees upon retirement compensation in exchange for their services.").

have followed this Court's binding precedent and evaluated the abundant, competent evidence in the record.

The Court of Appeals' decision thus failed to apply the standards and principles of contract and deferred compensation in Bailey and Faulkenbury and failed to evaluate the abundant record evidence that was found in prior cases to evidence a contract. In sum, the Court of Appeals' decision – while applying federal law and inapposite cases from other states – altogether fails to sufficiently apply the law of *this State* under the precedent established by *this Court*. As explained further infra, if the Court of Appeals had correctly applied the law, it should have concluded that the Retirement Health Benefit is a contractual obligation and affirmed the decision of the trial court.

III. The Evidence in this Case Is Uncontroverted and Establishes a Contractual Obligation as a Matter of Law

Applying the ample precedent of this Court, it is clearly apparent that the Retirement Health Benefit must be contractual, as it constitutes deferred compensation, is vested, is part of the overall retirement package, and is premised on numerous admissions by the Defendants that there is a contractual obligation. When the actual record of evidence used by the trial court is examined (as it must be according to Bailey, Stone, etc. and which the

Court of Appeals refused to do), there is uncontroverted evidence for a contractual obligation to provide the Retirement Health Benefit.

a. The Defendants Used Words of Contract in Their Representations and Descriptions of the RHB

i. Words Such as "Earned", "Contract" "Liability", and "Compensation" Were Used by Defendants in Representations to Plaintiffs

Ample support for the contractual nature of the RHB can be found in the State's own representations to the Plaintiff Class Members over the years. Repeatedly, the State described the RHB as it would a contract, using the language of contract. As a threshold matter, the Court of Appeals failed to consider the voluminous extra-statutory materials in support of the RHB being a contract. Neither did the Court of Appeals directly hold why these materials should not be considered.

It is settled law in this State that benefit handbooks, pamphlets, written correspondence and even oral representations to public employees can serve to create or evidence a contract between the employee and the State. See Stone, 191 N.C. App. at 414, 664 S.E.2d at 40 (considering "Your Retirement Benefits" booklets); Bailey, 348 N.C. at 138–39, 146, 500 S.E.2d at 58–59, 63 (considering oral and written representations, including official publications

and employee handbooks); Bolick, 182 N.C. App. at 96, 100–01, 641 S.E.2d at 388, 390 (holding that a personnel policy could supply the terms of a contractual right to a severance package that had been offered to employees); Pritchard, 81 N.C. App. at 551–53, 344 S.E.2d at 826–27 (oral representations were sufficient to express contract for a vacation policy that was mentioned in an ordinance). In NCAE, this Court considered affidavits from the plaintiffs stating that they relied upon representations about career status in accepting their employment. See NCAE, 368 N.C. at 789, 786 S.E.2d at 264. In fact, some of the very same handbooks and benefit pamphlets relied upon in Bailey and Stone refer to the RHB using words of contract.

Since 1982, the Retirement System has published a series of "Your Retirement Benefits" booklets, all of which included reference to the RHB. Each handbook contains an opening letter from the North Carolina State Treasurer explaining that the benefits described therein were a part of the retirement benefit that employees would receive at retirement. (See, e.g., Doc. Ex. 3849; Doc. Ex. 3950; Doc. Ex. 4094; Doc. Ex. 4336). Each handbook also included a statement that the benefits were a part of the employees' total compensation package deferred until retirement. See id.

For example, Treasurer Richard Moore's opening letter in the 2002 "Your Retirement Benefits" handbook explained that the booklet "describes the retirement benefits you can expect to receive as a member of the Teachers' and State Employees' Retirement System." (Doc. Ex. 4094). The letter further explains: "Your retirement benefit is a ***part of your compensation earned*** during your active working career ***that has been deferred*** until the time you stop working." (Id. (emphasis added); see also Doc. Ex. 4336 [opening letter from the 2008 Your Retirement Benefits] (stating same)). As another example, Treasurer Harlan Boyles' opening letter in the 1988 Your Retirement Benefits Handbook similarly states: "This booklet describes your benefits as a member of the Teacher's and State Employees' Retirement System. The benefits provided by the State Retirement System ***are part of your total package of compensation which is deferred until you retire***." (Doc. Ex. 3849 (emphasis added)).

The handbooks and other documents also include contractual language linking the receipt of the premium-free health benefit to the five year vesting requirement. The 1988 booklet, for example, specifically states: "When you retire, if you have at least 5 years of service as a contributing teacher or State employee, you are eligible for coverage under the State's Comprehensive

Major Medical Plan with the State contributing toward the cost of your coverage." (Doc. Ex. 3862; see also Doc. Ex. 3950 [Your Retirement Benefits, March 1, 1995]). Similarly, the 1988 Plan Booklet promulgated by the State Health Plan stated that the State would pay for "noncontributory (no cost to you)" coverage to "[r]etired North Carolina public school teachers and State employees," but that "[i]n order to qualify for benefits under the Plan, an employee who retires on or after January 1, 1988 must have completed at least 5 years of contributory service prior to retirement." (R pp 67-68 at ¶ 48 [Defendants' Answer]; see also Doc. Ex. 1329 [Summary Plan Description, Nov. 1989] ("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.")). The inclusion of the RHB and the contractual language surrounding it, which offers a benefit and describes the consideration in order to receive that benefit is the language of contract and is consistently expressed in the Your Retirement Benefits handbooks and the State Health Plan booklets from 1988 to 2011.

Other State publications describe the RHB as "vested" and use the word "contract". For example, the 2008 "Your Retirement Benefits" Booklet, under

the heading "How to Qualify For Benefits" and the subheading "Becoming Vested" states:

> You become ***vested*** in the Retirement System once you have completed a minimum of five years of membership service. This means that you are eligible to apply for lifetime monthly retirement benefits based on a formula, and the age and service requirements described in this handbook, provided you do not withdraw your contributions. You may also be eligible for retiree health coverage as described on page 20.

(Doc. Ex. 4340 (emphasis added); see also Doc. Ex. 4380 [Your Retirement Benefits, 2009]). The 2004 Summary Plan Description from the State Health Plan goes so far as to directly refer to coverage provided by the Plan as contracts: "The Plan offers the following ***contracts***: 1. Employee Only- covers only the employee or retiree." (Doc. Ex 1663 (emphasis added)).

Treasurer Cowell's first introduction letter to the 2009 "Your Retirement Benefits" Booklet specifically refers to the duration of the RHB as "***life long***" and represents that those "life long benefits are ***guaranteed*** and ***protected*** by the Constitution of the State of North Carolina." (Doc. Ex. 4376 (emphasis added)). The RHB was described as being "for life" or of a "lifetime" duration in other publications promulgated by Defendants. (See, e.g., Doc. Ex. 12925 [University of North Carolina at Chapel Hill Personal Benefits Statements]

(health plan "continues for life" if vested); Doc. Ex. 1042 [Summary of NC Obligations to Provide other Postemployment Benefits ("OPEB") Valuation as of December 31, 2012] (specifying "Coverage duration: Lifetime" as the relevant duration of the RHB).

Other times the RHB was referred to as being "***already earned*** by current retired employees" and a "liability" and "obligation" of the State. (See, e.g., Doc. Ex. 777 [Fiscal Research Division Presentation, Feb. 2007] (emphasis added) (describing the RHB as a "liability"; "obligation"; "already earned"); Doc. Ex. 732–766 [Report of the Actuary on Post Employment Medical Benefits Valuation, December 2005] ("liability")). The Defendants also admitted that there was an "obligation" to provide the RHB. (See Doc. Ex. 10585-86, 10588–89 [Cowell Dep. at 86:5–87:10; 89:20–90:10] (conceding that the RHB is an "obligation" by the State); Doc. Ex. 10697 [Cowell Dep. at 198:12-200:5] (conceding that the State is obligated to provide at least some form of health insurance to already vested retirees)).

The Court of Appeals also failed to consider evidence that the Plaintiffs themselves relied upon the promise of the RHB in deciding to work for the State. (See Doc Ex. 626-630 [Kursh Report]; Doc Ex. 7023 [Cooper Dep. at 27:17-28:5]; Doc Ex. 6574 [Blanton Dep. at 196:7-197:14]; Doc Ex. 6806

[Buchanan Dep. at 131:21-133:24]; Doc Ex. 6864-72 [Carpenter Dep. at 9:18-24, 15:2-15, 15:15-17, 17:10-21]; Doc Ex. 7527-31 [Evans Dep. at 15:3-18, 17:7-10, 19:23-20:3]; Doc. Ex. 12694 [Wall Dep. at 35:17-36:17]). This Court in numerous cases, including NCAE considered and gave weight to such evidence. See NCAE, 368 N.C. at 789, 786 S.E.2d at 264 (discussing record evidence that " '[t]eachers rely upon their career status rights in making employment decisions').

The Court of Appeals' holding that there was no intent to contract failed to consider any of these numerous admissions and representations – evidence that the trial court properly relied upon in making its ruling. This alone was a substantial error of law under this Court's binding precedents as described in § II supra. The mountain of evidence in this case demonstrates that the State had the requisite intent to make an offer of contract and understood the RHB – once accepted by performance – is a contractual obligation.

ii. The RHB Statutes Included Vesting – Indicating a Contractual Obligation

The concept of "vesting" has had a prominent role in the jurisprudence of State benefits at least since Simpson, Faulkenbury and Bailey. As this Court has perennially held, when a benefit is offered in exchange for a set period of service to the state, those benefits become vested when the employee reaches

the service requirement. See Bailey, 348 N.C. at 142–46, 500 S.E.2d at 60–63; Faulkenbury, 345 N.C. at 691–92, 483 S.E.2d at 427–28; see also Milam v. Milam, 92 N.C. App. 105, 106–07, 373 S.E.2d 459, 460 (1988) (for purposes of defining "vested" for equitable distribution purposes, adopting definition that "'[v]esting' occurs when an employee has completed the minimum terms of employment necessary to be entitled to receive retirement pay at some point in the future. . . ."). Once vested, the benefits cannot be reduced. See Faulkenbury, 345 N.C. at 692, 483 S.E.2d at 428. In the form of publications to the Plaintiffs and even in the course of this litigation, Defendants have admitted that the Plaintiffs vested into the RHB. These admissions took numerous and various forms over a breadth of years, including in:

1. Legislative History and Statutes (e.g., Short Bill Titles for Session Laws amending the vesting requirements (Session Law 2006-174 (S.B. 837) (Short Bill Title "State Health Plan / 20 Year ***Vesting***") (emphasis added)).

2. Press Releases pertaining to the State Health Plan (e.g., Doc. Ex. 723 ("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.") (emphasis added)).

3. Training manuals used by retirement division customer service personnel to advise retirees and current employees (e.g., Doc. Ex. 899 [Introduction to Retirement, Vol. II, First Contact Training] ("In order for the retiree to have paid health insurance, he must

have 5 years of contributing membership in the State System, and be in receipt of a monthly retirement benefit with the State….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.") (emphasis added)).

4. Actuarial Reports (e.g., Doc. Ex. 935–36 [State of N.C. OPEB Strategy Study, March 21, 2011] ("Elimination of 5 YOS ***vested*** eligibility" and "Elimination of all ***vested*** elig., must retire from Act. Svc") (emphasis added); Doc. Ex. 939 (chart showing "Elimination of 5 YOS ***vested*** eligibility" would yield $4 billion in "Liability Savings") (emphasis added); Doc. Ex. 967–68 ("Currently, individuals who leave State employment after becoming ***vested***, may work elsewhere and then enroll in health benefits at retirement.") (emphasis added)).

5. PowerPoint Presentations (e.g., Doc. Ex. 719 [State Health Plan Update by Mona Moon, Dec. 12, 2012] (stating that "the State's unfunded liability associated with retiree health benefits earned by: current retirees, active employees, and former employees with a ***vested*** retiree health benefit" and listing 30,241 "Inactive ***Vested*** Participants" along with retirees, etc.) (emphasis added)).

6. Defendants and former agents of Defendants in depositions (e.g., 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*** – I came into the – in '05, so I am eligible at a certain age to receive some retiree health benefits.") (emphasis added); Doc. Ex. 11593, 11597, 11688 [Moon Dep. at 212:9–16, 216:9–18, 307:25–308:6] ("Q: Do you acknowledge that there have been ***vesting*** requirements for certain years of contributing membership in order for someone to be eligible for state paid individual health insurance coverage at retirement? A: ***I do***") (emphasis added); Doc. Ex. 11780 [Trogdon Dep. at 69:9–16] ("Q: [D]oes that mean you are also ***vested*** in the

> retirement health benefits? A: ***That is correct***.") (emphasis added)).[8]

A more exhaustive list of examples of admissions of vesting with regard to the RHB can be found in the Appendix (App. 1-6) to this brief.

The Defendants' own admissions of vesting eliminate their ability to escape any obligation to now provide the RHB. The inclusion of the term "Vesting,"—a term understood to mean that contractual rights were conferred since at least Simpson in 1988—is compelling evidence that the RHB was intended to be contractual. There is no genuine issue of material fact that the Defendants themselves considered the Plaintiffs vested into the RHB. The case law (Faulkenbury, Bailey, and Simpson) is clear that a benefit once vested cannot be reduced. Therefore, the RHB is a contractual obligation that the Defendants could not reduce after the Plaintiffs vested.

b. The Enabling Statutes Alone Evidence the State's Intent to Contract with Plaintiffs

[8] Janet Cowell was the Treasurer of the State of North Carolina; Mona Moon was the Executive Director and 30(b)(6) deponent for the Defendant State Health Plan; and Mark Trogdon was Director of the Fiscal Research Division of the N.C. General Assembly.

Even though this Court has held in the past that it is not necessary to meet the "unequivocal intent" standard solely relied upon by the Court of Appeals, the statutes that authorize the RHB do demonstrate an unequivocal intent by the General Assembly to create a contract with its employees and retirees. The Court of Appeals erred in holding the opposite.

i. The Relationship Between the State and its Employees Itself Evidences the Intent to Contract

When the General Assembly passed the statutory scheme that authorized the RHB, it evidenced an intent to offer a contract by providing a benefit in exchange for a set period of service to the State. As this Court held in Faulkenbury, "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." Faulkenbury, 345 N.C. at 691, 483 S.E.2d at 427. All that is needed to evidence the contract is that the State offered a deferred benefit in exchange for service. The federal cases relied upon by the Court of Appeals are not cases where the State is an employer offering retirement benefits to employees in exchange for work

performed. See e.g. Nat'l R.R. Passenger Corp. v. Atchison, T & S. F. R. Co., 470 U.S. 451, 454, 466 (1985) (determining whether statute that established the nongovernmental entity, Amtrak, created a contractual relationship directly between the United States and private railroads).

In contrast to those cases which do not have a deferred compensation statutory scheme, Simpson, Bailey, and Faulkenbury never required the exacting language in the statute that the Court of Appeals held in this case was required to form a contract. "In [Bailey and Faulkenbury], this Court held that vested contractual rights were created by the statutes at issue because, at the moment the plaintiffs fulfilled the conditions set out in the two benefits programs, the plaintiffs earned those benefits." NCAE, 368 N.C. at 788, 786 S.E.2d at 263. The fact that the Plaintiffs and the State were already in a contractual employee-employer relationship and the statute required performing years of a service for a benefit is itself proof of an "unequivocal intent" to contract.

ii. The RHB is a Part of the Overall Retirement Package of Class Members and Intertwined with the Pension Statutes which have been held to be Contractual

Further support of the statutory intent to create a contract for retirement benefits lies in the RHB's statutory and practical context. The

RHB's authorizing statute is inextricably interwoven and integrated per statute with the larger Retirement System and with the pension benefits paid to state retirees through that system.

By statute, eligibility to receive the RHB is based upon participation in the State's overall pension retirement plan. Under N.C.G.S. § 135-48.1(18) (2011), a person must be receiving pension payments from the State Retirement System in order to be eligible to receive the RHB. This requirement has existed since the initial codification of the RHB. See N.C.G.S. § 135-40.1(17) (1982); N.C.G.S. §135-40.2(a)(2) (1982). If an employee or retiree receives a refund of their contributions to the pension plan, they actually forfeit their right to the RHB. (See, e.g., Doc. Ex. 4113). The RHB and the retirement system rely on shared definitions in the statutes. See N.C.G.S. § 135-48.1 (2011) (same definition of "retiree"); N.C.G.S. § 135-1(8) and § 135-4 (2011) (shared definition of "Creditable service" used to define eligibility for benefits for RHB, pension, and retirement disability). In fact, the definition of the term "Retirement System" itself is inclusive of non-pension benefits such as the RHB. See N.C.G.S. § 135-2 (2011) ("A Retirement System is hereby established … for the purpose of providing retirement allowances *and other benefits* under the provisions of this Chapter.") (emphasis added). The State

itself legislated that the RHB was "a part of the total compensation package for employees and retired employees" and the RHB has always been codified in Chapter 135 of the General Statutes alongside the other pension and retirement related benefits. See Session Law 1987-857 § 23(b); see generally N.C.G.S. § 135-1, et. seq.[9]

Like pension, the RHB is merely another form of deferred compensation. The benefits provided under Chapter 135 have consistently been held to be deferred compensation. See, e.g., Faulkenbury, 345 N.C. at 692, 483 S.E.2d at 428; Bailey, 348 N.C. at 141–42, 500 S.E.2d at 60. The treatment of the Retirement Health Benefits as "deferred compensation" is mandated by N.C.G.S. § 135-48.12, which has required that the State account for the benefits annually by way of actuarial valuation using "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

[9] Other indicia of similarities to pension and the contractual nature of the RHB can be found in the statutes that require a trust fund be created to hold funding for the RHB. See N.C.G.S. § 135-7(f) ("Retiree Health Benefit Fund"); § 135-48.5 ("Health benefit trust funds created"). Similar trust funds are also used in the context of other contractual retirement benefits, such as pensions. See e.g., N.C.G.S. § 135-7(g).

treated as deferred compensation and classified as a liability. (See Doc. Ex. 785–87). The General Assembly was correct in mandating this treatment of the RHB because the RHB is provided as compensation in exchange for services rendered to the government-employer. It is also provided after said work ceases – when one retires. This acknowledgement was ignored by the Court of Appeals.

The fact that the RHB is insurance as opposed to a check (whether paid monthly or otherwise), makes it no less of a form of compensation. In fact, this Court has previously noted that insurance provided to a public employee is compensation for work performed. Leete v. County of Warren, 341 N.C. 116, 121, 462 S.E.2d 476, 479 (1995) ("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***.") (emphasis added). The Court of Appeals' drawing of a 'red-line' between pension benefits and the Retirement Health Benefits is counter to this Court's prior holding in Bailey that the "respect for individual rights has manifested itself through the ***expansion of situations*** in which courts have held contractual relationships to exist." Id. at 143, 500 S.E.2d at 61 (emphasis added). There is neither legal nor factual

foundation for the Court of Appeals' dispositive distinction between pension and retirement health benefits.

iii. The Undertaking Clause in the RHB Statutes Shows an Intent to Contract

Further support that the statute contained the intent to create a contract is found in its undertaking clause. Since 1982, the RHB statute has contained an undertaking clause, using the language of contract, and evidencing the State's intent to obligate itself. See N.C.G.S. § 135-40 (1982) ("Undertaking"). The original undertaking clause states: "The State of North Carolina undertakes to make available a Comprehensive Major Medical Plan . . . to employees, retired employees, and certain of their dependents which will pay benefits in accordance with the terms hereof." Id. "Undertaking" means "[a] promise, pledge, or engagement." Black's Law Dictionary (9th Ed. 2009), UNDERTAKING. The word "undertake" similarly means "[t]o take on an obligation or task" and "[t]o give a formal promise; guarantee." Black's Law Dictionary (9th Ed. 2009), UNDERTAKE. The General Assembly purposefully chose these words and in doing so demonstrated an intent to take on an obligation and give a formal promise and guarantee. See Dickson v. Rucho, 366 N.C. 332, 344, 737 S.E.2d 362, 371 (2013) (quoting N.C. Dep't of Corr. v. N.C.

Med. Bd., 363 N.C. 189, 201, 675 S.E.2d 641, 649 (2009)) ("We presume that the General Assembly 'carefully chose each word used' in drafting the legislation.").

iv. Subsequent Amendments to the RHB Statutes Evidence the Existence of a Contractual Obligation

The Legislature's own understanding of the RHB, as expressed through legislative history, demonstrates an intent to create an obligation to the Plaintiffs. "Courts may use subsequent enactments or amendments as an aid in arriving at the correct meaning of a prior statute by utilizing the natural inferences arising out of the legislative history as it continues to evolve." Burgess v. Your House of Raleigh, Inc., 326 N.C. 205, 216, 388 S.E.2d 134, 141 (1990). In 2006, the General Assembly enacted a prospective change to the RHB statute that increased the eligibility requirements for new hires from 5 years to 20 years. See Session Law 2006-174. The short title for the session law was "State Health Plan / 20 Year ***Vesting***." Senate Bill 837, Session Law 2006-174 (emphasis added). (See Doc Ex. 725). The title of an act is an indication of legislative intent. See Dickson, 366 N.C. at 342, 737 S.E.2d at 370. The Legislative Actuarial Note, forming the basis for Session Law 2006-174, notes that "***the bill requires its application to be prospective***" and

acknowledges that the payment of premiums for current and future retirees meeting the five-year service requirements "***will continue to be a State obligation for some time until these retirees exit the Plan.***"[10] (Doc. Ex. 727 (emphasis added); see also Doc. Ex. 4768 (emphasis added) (earlier edition of Actuarial Note based on 10-year vesting which included identical "obligation" language and noting short title of the proposed Session Law as "State Health Plan/10-Year ***Vesting***.")). In addition to the unmistakable language of contract used by the Legislature, Session Law 2006-174's *prospective* application (applying solely to newly hired employees), is an acknowledgement of the vested and unalterable status of the RHB for those who met the previous service requirements.

v. The 'Right to Amend' Clause Does not Impact Already Vested Benefits

The enabling statute contains a right to amend provision which was referenced by the Court of Appeals and has been argued throughout this litigation by the Defendants to defeat any claim of a contract between the State and its employees. See Lake, 825 S.E.2d at 654. While Plaintiffs agree that the right to amend does confer to the General Assembly the right to

[10] This Actuarial Note also uses the words "earn" and "earned" to describe what employees would be doing to be eligible for the Retirement Health Benefit.

change the statutes underlying the RHB, ample North Carolina precedent puts a limit on that right. Any such changes are permitted only as to non-vested employees. In other words, the State may rescind the offer, but not after it has been accepted and the benefit earned. As in Simpson, Faulkenbury, and Bailey, the State offered a retirement benefit as deferred compensation in exchange for five years of service. Once those service requirements were performed by Plaintiffs, their rights were vested and could not be taken away. See, e.g., Faulkenbury, 345 N.C. at 690, 483 S.E.2d at 427 (citing Simpson) (rights to pensions based on five years of service were "earned and may not be taken from them by legislative action"); Wiggs, 361 N.C. at 324, 643 S.E.2d at 908 (holding that a county could "pass a resolution which would apply prospectively to those whose rights to the special separation allowance had not yet vested," but it could not retroactively apply such a resolution "to [the] plaintiff's vested contractual right" to receive employment benefits).

Simpson and Faulkenbury – the only two North Carolina cases to consider right-to-amend clauses in the context of state retirement benefits – both summarily rejected the Defendants' current position, holding that a reservation of the right to amend did not prevent a contract from being formed. See Faulkenbury, 345 N.C. at 691, 483 S.E.2d at 427; Simpson, 88 N.C.

App. at 221, 363 S.E.2d at 92. In Simpson, the Court considered a similar right to amend clause to the one in the present case, and after consideration, held that "the relationship between plaintiffs and the Retirement System is one of contract." Simpson, 88 N.C. App. at 221, 223, 363 S.E.2d at 92, 93.[11]

Similarly, in the non-retirement context, North Carolina Courts have held that there are limitations on a right to amend in the context of vested rights. In Elizabeth City Water & Power Co. v. Elizabeth City, 188 N.C. 278, 124 S.E. 611 (1924), 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. The Plaintiffs in this case have vested rights that they earned through contributory service to the State of North Carolina. As demonstrated in Elizabeth City, the existence of a right to amend clause can neither deprive them of those rights already earned, nor prevent them being earned in the first place.

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[11] While the statute at issue limited the right to amend, the Court in Simpson did not consider the limiting language and characterized the right to amend as "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." Simpson, 88 N.C. App. at 221, 363 S.E.2d at 92 (quoting N.C.G.S. § 128-38)

IV. The Trial Court Properly Held that the Terms of the Contract with the Plaintiffs were Established by Uncontroverted Evidence in the Statutes and in Documents Provided to the Plaintiffs

The trial court properly held that there was no genuine issue of material fact as to the terms of the contract between the State and the Plaintiff Class and that the State had breached those terms. The trial court correctly held that the RHB consists of "a non-contributory (premium-free) health plan equivalent to the 80/20 regular state health plan that had been long offered and provided to Class Members." (R p 615 ¶¶ 25, 28). The Court of Appeals' opinion substantively misunderstood and misapplied the ruling of the trial court regarding both the terms of the contract and the history of its provenance[12].

There can be little dispute that the RHB was intended to be provided premium-free to vested participants. From the passage of the authorizing

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[12] One general problem with the Court of Appeals' decision is that it repeatedly relies on a mischaracterization of the trial court's (and the Plaintiffs') position as to the Retirement Health Benefit, continually referring to "static" or "unalterable" health insurance benefits. See Lake, 825 S.E.2d at 648 ("static health benefits"); 652 ("static and non-contributory health care insurance benefits under the State Health Plan"); 653 (same); 655 ("unalterable and static"). Neither Plaintiffs' arguments nor the trial court's order have ever made such a characterization.

statutes in 1982 to the present day, the statutes themselves stated that eligible retirees were entitled to receive a "non-contributory"[13] health plan. Compare § 135-40.2(a)(1982) with N.C.G.S. § 135-48.40(a)(2020) ("The following persons are eligible for coverage . . . on a noncontributory basis . . . ."). Documents provided by the State to the Plaintiff Class confirmed this point. See § III, supra. Even in this litigation, the State has admitted that a premium-free RHB must be provided to eligible retirees. (See, e.g. Doc. Ex. 11144 [Moon Dep. 81:18–20] ("From my perspective, there is a statutory requirement that directs the Plan to offer a premium-free option to retirees.")). The trial court appropriately relied on this undisputed evidence, while the Court of Appeals altogether ignored it.

The premium-free plan offered as the RHB has always referred to a single *regular* or *standard* plan. This health plan was referred to by the Defendants as the "Regular State Health Plan" (or "regular State insured health plan") or the "Standard" plan. (Doc. Ex. 12910–16 (citing SHP enrollment forms from 1988 to 2011 referring to the primary health benefit plan as the "Regular State Health Plan" and "Standard" plan); Doc. Ex. 4496 [Highlights of Your

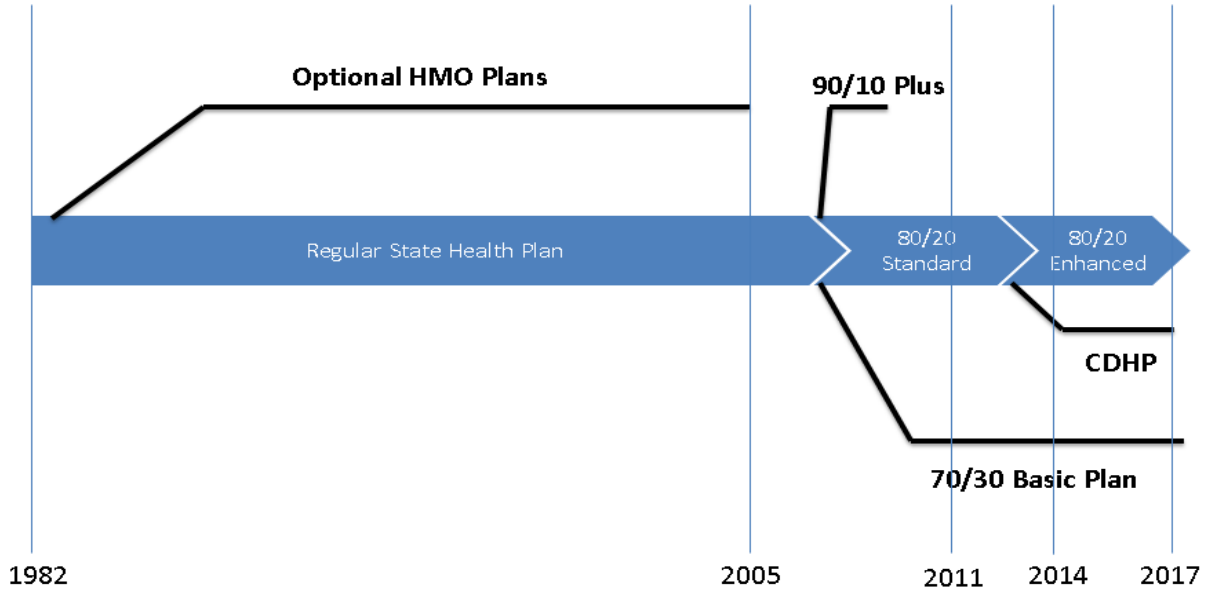
[13] Noncontributory means the plan is provided without the payment of a premium from the employee or retiree.

Retirement Benefits, July 2004] ("When you retire . . . provided you have at least 5 years of retirement membership service earned as a teacher or State employee. . . . the State pays the full cost of your individual coverage under *the regular State insured plan*.") (emphasis added); Doc. Ex. 4240 [Your Retirement Benefits, January 2005] ("regular State insured plan"); Doc. Ex. 4079 [Your Retirement Benefits, March 2001] (same); Doc. Ex. 4278 [Your Retirement Benefits, January 2006] (same)).

The Legislature allowed the SHP to create and offer optional plans that differed in benefits and structure from the regular plan. See N.C.G.S. § 135-39.5B (1982–2005) (allowing the State Health Plan to provide "optional" plans to retirees and employees); N.C.G.S. § 135-39.5B (1994) ("The amounts of State funds contributed for such ***optional plans*** shall not be more than the amounts contributed for each person eligible under G.S. 135-40.2 on a noncontributory Employee Only basis, with the person selecting an ***optional plan*** paying any excess, if necessary.") (emphasis added). These optional plans took several different forms – such as HMO's, PPO's, and a CDHP – offering benefits greater, lesser, or just different than what was offered by the regular state health plan. (Doc. Ex. 12910–16). Pursuant to the enacting

legislation, premiums could be assessed on these optional plans. See e.g. N.C.G.S. § 135-39.5B(1994).

In contrast, the Regular State Health Plan was the default and primary plan that was required to be offered premium-free. The Legislature made this clear in 2007 and 2008 when the Regular State Health Plan was converted from an indemnity to a PPO offering. See Session Law 2007-323 § 28.22A.(n)(retirees in the regular state health plan who had not "elected one of the optional PPO benefit plans" must be enrolled "in the Standard PPO Option, or its equivalent."). This fact was communicated directly to employees and retirees by the Defendants in the 2008 Annual Enrollment Forms. (See Doc. Ex. 12863 ("Members who don't switch will be automatically moved to the PPO Standard Plan.")). A timeline illustrating the various plan offerings of the SHP follows:



Based on the legislative and documentary history of the RHB, the trial court properly held that the Plaintiff Class had all vested into the premium-free Regular State Health Plan. The record is clear that all Plaintiffs attained the minimum eligibility requirements and vested in the RHB at a time when the Regular State Health Plan was offered premium-free. (See R pp 38–56).

The trial court also properly noted that the uncontroverted evidence in the record shows that the State's decision to charge a premium for the regular state health plan violated the contractual and constitutional rights of the Plaintiff Class. The evidence in the record is undisputed that starting in 2011, the State began charging a premium for the Regular State Health Plan (at that

time called the "Standard Plan").[14] (See Doc. Ex. 11104 [Moon Dep. [09/14/15] at 41:7–41:24]). Instead, the State substituted one of the optional plans – the 70/30 Basic Plan – as the only premium-free option. The Defendants conceded and the trial court properly noted that this optional plan was 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). Based on the admissions of the Defendants and the uncontroverted evidence in the record, the trial court held that the Defendants had breached and impaired the contract with the Plaintiff Class.

a. Changes Made to the Health Plan Over Time Do Not Diminish the Contractual Nature of the Benefit

[14] Said plan was later called the "Enhanced Plan" – a name change that occurred after this lawsuit was filed.

Despite the undisputed evidence in the record, the Court of Appeals reversed the trial court's ruling – at least ostensibly in part on the basis that changes made in the health plans over time obviated the existence of an obligation to provide any plan at all. By throwing the baby out with the bath water, the Court of Appeals ignored the core statutory history and documentary evidence of the RHB and refused to acknowledge persuasive authority from other jurisdictions that have dealt with this very issue.

There is little doubt that both health care and health insurance have changed since the 1980's. New procedures and medicines are introduced, while older procedures and medications are discontinued. However, the core promise to provide retirement health insurance is neither dependent upon nor diminished by these natural changes. While North Carolina courts do not appear to have taken up this precise issue, sister states have acknowledged that retirement health insurance can change and at the same time maintain a core contractual benefit of the bargain to the recipients. In Duncan v. Retired Pub. Emples. of Alaska, Inc., 71 P.3d 882 (Alaska 2003), the Alaska Supreme Court held "that health insurance benefits must be allowed to change as health care evolves," but went on to hold that the need for this type of change does not destroy the protected nature of the retirement benefit. See Duncan, 71 P.3d

at 891–92. In adopting an actuarial equivalency approach for measuring that benefit of the bargain (an approach adopted by the trial court in this case),[15] the court in Duncan held that "disadvantageous changes must be offset by comparable new beneficial changes." See id. at 889.

Many of the historical changes mentioned by the Court of Appeals reflect both additions and deletions to the benefits.[16] Changes to the vesting period were only made prospectively and existing employees were exempted from such changes. See e.g., Session Law 1987-857, codified at N.C.G.S. § 135-40.1(17) (1987); Session Law 2006-174 (S.B. 837). There is no evidence in the record that such historical changes reduced the value of the RHB for Plaintiffs.[17] Nor were they previously challenged, likely because most of them expanded health coverage rather than restricting it.

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[15] The trial court adopted a narrowly tailored remedy to ensure that the RHB may naturally evolve as needed, but that it would maintain the benefit of the bargain to the Plaintiff Class by requiring that the Retirement Health Benefit be equivalent – not identical. (R p 618 (ordering the state to provide the Plan "or its Equivalent")); see also Session Law 2007-323, § 28.22(n)(Legislature requiring new plan to be ***equivalent*** to the Regular State Health Plan).

[17] While conceding that certain changes were purely for clarification and some changes actually added benefits, the Court of Appeals also stated that certain changes "arguably reduced the type and level of benefits" without any reference to any specific record evidence that the overall value of the offering had been reduced. See Lake, 825 S.E.2d at 655.

Most pertinently, none of the historical changes argued by the Defendants and mentioned by the Court of Appeals ever added a premium to the regular state health plan. The first time such a change was enacted was in 2011 – the change being adjudicated in this very litigation.

V. Defendants' Actions Constituted an Impairment of Contract and Impermissible Taking of Property in Violation of the North Carolina and United States Constitutions

a. Impairment of Contract

Defendants' actions in reducing the Retirement Health Benefits constituted an impairment of Plaintiffs' contracts in violation of Article I, Section 10 of the United States Constitution and Article I, Section 19 of the North Carolina Constitution. Having shown that the Retirement Health Benefit is a contractual obligation, it is also clear that the State impaired that contract and that such impairment was not reasonable and necessary to serve an important public purpose. See Bailey, 348 N.C. at 141, 500 S.E.2d at 60 ("The U.S. Trust test requires a court to ascertain: (1) whether a contractual obligation is present, (2) whether the state's actions impaired that contract, and (3) whether the impairment was reasonable and necessary to serve an important public purpose.").

The contract at issue here was impaired when the Defendants unilaterally reduced the value of the contractual benefits without compensation. "When examining whether a contract has been unconstitutionally impaired, the 'inquiry must be whether the state law has . . . operated as a substantial impairment of a contractual relationship.'" Id. at 151, 500 S.E.2d at 66 (quoting Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 244–45 (1978)). "Total destruction of contractual expectations is not necessary for a finding of substantial impairment." NCAE, 368 N.C. at 790, 786 S.E.2d at 265 (quoting Energy Reserves Grp. v. Kan. Power & Light Co., 459 U.S. 400, 411 (1983)). In Faulkenbury, for example, the Court held that "[t]he contract was substantially impaired when the promise was taken from them." Faulkenbury, 345 N.C. at 693, 483 S.E.2d at 428. The broken promise there was the *reduction* of benefits. See id.

In the present case, it is uncontroverted that the Retirement Health Benefit was reduced. Both parties' experts noted that there was a drop in value between the 70/30 and 80/20 plans for both Medicare and non-Medicare retirees. (See Doc. Ex. 1098–99; Doc. Ex. 4605, 4624). The State Health Plan's own actuaries also calculated in 2011 (after the challenged legislation) that the new premium-free option (the 70/30 Plan) that year had a relative value eight

percent (8%) less than the Regular State Health Plan (the 80/20 Plan). (See Doc. Ex. 12237 [Vieira Dep. 135:7–15]; Doc. Ex. 1032 [N.C. OPEB Valuation Report, 2011]). Individually, the average non-Medicare participant would experience a difference in lost value per year in the range of $434.04 – $497.16. (See Doc. Ex 1097 [McCarthy Aff. Ex. B]; Doc. Ex. 4605, 4624 [Fuhrer Aff.]). For non-Medicare retirees paying a premium for the Regular State Health Plan, the base monthly premium rose from $21.62/month in 2011 to $104.20/month in 2016, or a total of $1,250.40/year. (See R p 617; Doc Ex. 3061 [Monthly Contribution Rates for 2011]; Doc Ex. 3515 [Enhanced 80/20 Plan Monthly Premium Rates] (showing a base premium of $104.20)). Even further, in the aggregate, the State acknowledges that the breach is substantial, possibly exceeding $100 million in back premiums. (See Doc. Ex. 3673). The Court in Bailey used a similar aggregate number to hold that the impairment in that case was substantial. See Bailey, 348 N.C. at 151, 500 S.E.2d at 66 (noting that "losses to retirees in expected income will be in excess of $100 million" and concluding "it is clear [the law] substantially impairs the employees' contractual right.").

The record is also clear here that the impairment was neither reasonable nor necessary to serve an important public purpose. The State has indicated

its action in reducing the Retirement Health Benefit was motivated by the desire of the State to alleviate the financial obligations of the State Health Plan. Specifically, in response to the question, "Was there anything that you're aware of . . . that compelled the change in treatment of premiums from a noncontributory basis to a partially contributory basis for the 80/20 plan?," Ms. Moon stated in her deposition that "the [State Health] Plan was experiencing increases in cost that traditionally the State had had to cover through increases in the employer contribution", that "[t]he State was experiencing budget issues", and that "[t]he General Assembly wanted the [State Health] Plan to determine other ways to raise funds than just the employer contribution." (Doc. Ex. 11178-79 [Moon Dep. 115:19-116:9]).

Here, like Bailey, the impairment was unnecessary because there were "numerous ways that the State could have achieved [its purpose] without impairing the contractual obligations of [P]laintiffs." Bailey, 348 N.C. at 152, 500 S.E.2d at 67. This fact was also admitted by Ms. Moon. (See Doc. Ex. 11178 [Moon Dep. (9-14-15) 115:8–12]) (Question: "There were other ways to balance things out… without necessarily charging a premium to the employee, active or retired, in 2011, isn't that right?" Answer: "Yes")). In fact, fifteen alternative options were presented in a March 2011 study prior to the changes, and a

further 2015 legislative report offered options including: (1) the General Assembly increasing appropriation, (2) increasing service time requirements for the non-contributory health benefit, (3) requiring active employees to contribute to the Retiree Health Benefit Fund, and (4) eliminating benefits for new hires and non-vested employees. (See Doc. Ex. 3634–75; Doc. Ex. 3663–72 [General Assembly Program Evaluation Division, June 14, 2007]). In Bailey, because there was another way to achieve the purpose there without affecting vested rights, the Court held that the impairment was unnecessary. See Bailey, 348 N.C. at 152, 500 S.E.2d at 67 (discussing two alternatives). Here, there were a multitude of methods to stabilize the State Health Plan without impairing vested rights. (See Doc. Ex. 3634–75; Doc. Ex. 3663–72). The State's impairment was therefore not necessary.

Moreover, in Bailey, this Court specifically rejected the reasonableness of the State's actions when centered around financial concerns, noting, "[t]he legislature sought a 'revenue neutral' approach to complying with the *Davis* decision, meaning that legislators would be faced with neither raising taxes nor cutting other programs in order to comply. However, this convenient approach impaired vested rights . . . ." Bailey, 348 N.C. at 152, 500 S.E.2d at 67. Importantly, mere "[l]egislative convenience is not synonymous with

reasonableness." Id. When the State chose to impair Plaintiffs' vested rights, rather than pursue the multitude of alternatives, it took the convenient path, not the necessary or reasonable one.

b. Impermissible Taking of Private Property

Session Law 2011-96, and its application, also constituted an impermissible taking of private property contrary to the 14th Amendment of the US Constitution and the North Carolina Constitution's Law of the Land Clause, Article I, Section 19. Deprivation of private property without compensation is an impermissible taking and "valid contracts are property, whether the obligor be a private individual, a municipality, a *State* or the United States." Bailey, 348 N.C. at 154, 500 S.E.2d at 68 (quoting Lynch v. United States, 292 U.S. 571, 579 (1934)) (emphasis added). The contracts for the State to provide the Retirement Health Benefit are property earned and obtained by Plaintiffs through many years of service with the State. Session Law 2011-96 impermissibly deprived Plaintiffs of those property rights without compensation.

VI. The Court of Appeals' Opinion, if Allowed to Stand, Will Have a Detrimental Effect on Both Public Employees and Public Employers

The Court of Appeals opinion, if left undisturbed, will have a vast negative impact on not only the 222,000 members of the Plaintiff Class, but also on the over 265,000 additional current state employees who are entitled to receive retirement health insurance after their retirement. (R pp 375–80). In addition, the contrarian and conflicting nature of the lower court opinion leaves both employees and government entities in a legal quagmire as to the true nature and validity of all retirement benefits.

Public employees have long relied upon the full faith and credit of the State to fulfill its promises for retirement benefits. Despite several instances when current political expediency attempted to undermine such contractual benefits, this Court has always protected such contractual obligations owed to retired employees. It has been a long-accepted presumption that the lesser salaries earned by public employees are off-set by the retirement and other non-monetary benefits provided to induce public employment. (Doc Ex. 626-630 [Kursh Report]); see also NCAE, 368 N.C. at 789, 786 S.E.2d at 264 (citing record evidence that the benefit at issue induced employment and "makes up for not having better monetary compensation"); Bailey, 348 N.C. at 146, 147, 500 S.E.2d at 63, 64 (stating that benefit was used to induce employment). When the State is allowed to unilaterally renege on a considerable part of the

compensation package of public employees (as has happened in this case), this dampens the prospect for public employment for both current and future employees. Is it not difficult enough to attract talented teachers to our most needy classrooms without the specter of a significant portion of their hard earned compensation being retroactively eliminated? Attracting talented employees to public service is a core concern for everyone in the State, but the Court of Appeals' opinion may leave many seeking other opportunities outside state employment amid increased uncertainty about the safety of their retirement benefits.

The Court of Appeals' opinion also creates a great deal of legal uncertainty in the realm of public retirement benefits. Because the Court of Appeals impliedly endorsed the elimination of all Retirement Health Benefits by failing to acknowledge any obligation to current retirees and employees, other similarly situated employers – such as those in cities and counties who offer similar benefits – may question the pertinence of this case to their own benefits. This could lead to a cascade effect, where additional litigation of these local benefits follows as localities with similar benefit structures attempt to reduce or eliminate such benefits.

The increasing premiums for the RHB demonstrate another reality about the nature of the impairment of the Plaintiffs' contracts: it grows year over year. The premium charged for the Regular State Health Plan increased by a factor of five between 2011 and 2016. In fact, the State admits that the impairment will likely further increase going forward. The Executive Director of the State Health Plan opined that virtually any type of plan (even a 60/40, 50/50 or 40/60) would satisfy the State's admitted statutory requirement to provide a non-contributory plan to retirees. (See Doc. Ex. 11148 [Moon Dep. [9-14-15] 85:6–86:2]). Former Treasurer Janet Cowell also indicated that the State Health Plan may be converted to a defined contribution plan, rather than its current status as a defined benefit plan. (See Doc. Ex. 10567 [Cowell Dep. 68:11–20]).

For a certain subset of retired employees, the reduction of the RHB and the threat of total elimination of the Retirement Health Benefits are especially problematic. Many retirees are years away from becoming eligible for Medicare. This is especially true for many State law enforcement officers. See e.g. N.C.G.S. § 135-5(a)(4) (2010) (allowing full-service retirement for law enforcement officers at age 50 with 15 years of creditable service). During the period of years between the onset of their public retirement and Medicare

eligibility, these retirees are left with the prospect of limited and increasingly expensive health insurance options. For those retirees – such as retired state troopers, teachers, or DOT workers – their financial future was premised on the promise of RHB. (See Doc. Ex. 4601 [Collins 3rd Aff.] (stating that, as of January 2016, over 46,000 retirees enrolled in the State Health Plan were not eligible for Medicare)). These fixed income retirees have little recourse to avoid the consequences of the State's abdication of its obligation. The termination of health insurance for such a large population could trigger a crisis within our State that could lead to numerous unintended and negative consequences, including increased enrollments in other State-funded programs, with the consequent costs and burdens that may place on the State, on other program participants, and on the citizenry in general.

Both the Defendants and Plaintiffs agree that the outcome of this case will materially affect all of our state's public-employee benefits and government spending. See Bypass Petition, Lake v. State Health Plan for Teachers & State Emp., No. 436P13-3, at 13 ("Although the parties disagree on the legal issues in this case, they agree that the outcome of this case will materially affect our state's public-employee benefits and government spending."). While the purely legal merits of this case weigh overwhelmingly

towards upholding the trial court's ruling and reversing the Court of Appeals, these various policy implications should be considered by this Court and also weigh heavily towards protecting the vested and contractual benefits promised to both the Plaintiff Class and to hundreds of thousands of other public servants.

CONCLUSION

The Retirement Health Benefits are substantively no different than the retirement benefits held contractual in this Court's cases in Bailey, Faulkenbury, Simpson, etc. and therefore should be treated no differently. The Retirement Health Benefits are deferred compensation, are vested, and are part of the Plaintiffs' overall retirement benefit package. This Court should follow its long history of precedent on this issue and find that the Retirement Health Benefits are contractual and cannot be unilaterally reduced. 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 28th day of June 2020.

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