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MORO CASE SUPREME COURT DECISION SUMMARY

On April 30, 2015, the Oregon Supreme Court issued its decision in *Moro v. State of Oregon*, 357 Or 167 (2015), regarding the constitutionality of the changes made in 2013 to the PERS Cost of Living Adjustments (COLAs) and to the 1991 (SB 656) and 1995 (HB 3349) income tax offsets for out-of-state retirees when the legislature passed SB 822 (effective May 6, 2013) and SB 861 (effective October 8, 2013).

COLA Changes

Before the 2013 legislative changes, Tier 1, Tier 2, and OPSRP retirees received a COLA based on CPI up to a maximum of 2 percent under ORS 238.360 (Tier 1 and Tier 2) and ORS 238A.210 (OPSRP). SB 822 reduced the 2 percent COLA for all Tier 1, Tier 2, and OPSRP retirees and active members to 1.5 percent for 2013 and SB 861 reduced the COLA further in years after that to a fixed 1.25 percent on the first \$60,000 and 0.15 percent on all benefits above \$60,000. The PERS Actuary estimated that the changes made by SB 822 and SB 861 reduced COLA liability by over \$4.9 billion.

The *Moro* petitioners challenged the reductions to the COLA benefits as an impairment of contract under the Oregon and US Constitutions, a taking of property without just compensation under the Oregon Constitution, and a breach of the PERS Contract.

The Oregon Supreme Court held that the 2 percent COLA statutes were terms of the PERS contract for Tier 1, Tier 2, and OPSRP members because they relate to a financial benefit and use language which is mandatory. Tier 1, Tier 2, and OPSRP members “accrue” COLA benefits on an on-going basis by providing service to their PERS covered employers. The 2013 changes to COLA are permissible to the extent they are “prospective” and apply only to service provided after the effective dates of SB 822 and SB 861 because that part of the COLA benefit was not yet “accrued” when the changes went into effect, and the COLA statutes did not contain express language or an implied promise regarding future changes. However, the 2013 changes are unconstitutional under the State Contracts Clause to the extent they apply “retroactively” to reduce COLA benefits Tier 1, Tier 2, and OPSRP members have already accrued through the service they provided their employers before the effective dates of SB 822 and SB 861.

The Supreme Court's decision finding the SB 822 and SB 861 reductions to COLA unconstitutional for benefits earned before the effective dates of SB 822 and SB 861 means that over \$4 billion in "accrued" benefits have been protected. In other words, members who retired before the effective dates of SB 822 (May 6, 2013) and SB 861 (October 8, 2013) will receive payments from PERS to make-up for the reduced COLAs they received in 2013 and 2014 and will continue to receive the 2 percent COLA for the remainder of their retirement.

Those who retire after the effective dates of SB 822 (May 6, 2013) and SB 861 (October 8, 2013) and active Tier 1, Tier 2, and OPSRP members will receive what the court referred to as a "blended" COLA to reflect their different periods of service. The court did not decide how the "blended" COLA should operate, but explained that one constitutionally permissible way would be the approach previously used for the 1995 (HB 3349) tax-offset payments, which looks to the percentage of total service provided before and after the effective dates of the change. Under this approach, Tier 1, Tier 2, and OPSRP members would be entitled to receive the 2 percent COLA for that part of their total years of service provided before May and October of 2013, and the SB 822 and SB 861 COLAs for that part of their total years of service provided after those dates.

Out-of-State Retiree Income Tax Offset Changes

Before the 2013 legislative changes, Tier 1 PERS members who established membership in PERS before July 14, 1995, were eligible for the higher of the 1991 (SB 656) or 1995 (HB 3349) income tax offset benefits. The 1991 (SB 656) benefits were calculated based on years of service, ranging from 1 percent for members with more than 10 years of service to 4 percent for more than 25 or 30 years, depending on whether they were general service or police and fire members. The 1995 (HB 3349) benefits were 9% of that part of a member's benefit attributable to service rendered before October 1, 1991. SB 822 prohibited paying either the 1991 or the 1995 tax offset payments to any PERS retiree who is not subject to Oregon income tax assessments. The PERS Actuary estimated that this change made by SB 822 reduced liability for such payments by \$0.39 billion.

Moro petitioners challenged the denial of the 1991 (SB 656) payments to out-of-state retirees on the same grounds as the COLA changes. Other individual petitioners also challenged the denial of 1995 (HB 3349) benefits as a denial of equal protection, a violation of federal tax law, and a breach of the *Chess/Stovall* settlement agreement resolving the original breach of contract claim for removal of the tax exemption.

The Oregon Supreme Court held that the 1995 income tax offsets were not contractual because HB 3349 expressly provided that no member would acquire a right "contractual or otherwise, to the increased benefits." In addition, the 1991 benefits were not contractual because they did not accrue while the members were providing service, but rather were passed after the fact to compensate PERS members for a breach of contract and not for their years of service, even though calculated based on service.

The court also rejected the additional arguments raised by the other petitioners. However, the court left open the possibility that out-of-state retirees might be able to re-open the Stovall/Chess class action, an issue that the court indicated it did not have jurisdiction to decide. In addition, the court left intact the right of such retirees to seek reinstatement of the benefits if they move back to Oregon and become subject to Oregon tax again.

PERS Employer Defenses

Finally, the court rejected the defenses raised by participating employers that the changes made by SB 822 and SB 861 were not “substantial” and were “necessary to support an important public purpose.” The court found that the combined effect of SB 822 and SB 861 on COLA benefits was substantial, noting that with compounding, by the 10th year after retirement, the COLA can make up about 20 percent of the retirement benefit and by the 14th year of retirement about 30 percent of the retirement benefit. A State is not free to consider impairing the obligations of its own contracts on par with other policy alternatives, especially when it has not considered any alternative means for achieving the very loosely defined policy goals put forward. Even if participating employers had identified specific public service deficiencies resulting from the current level of funding, according to the court, they did not demonstrate that those deficiencies could not be remedied through funding from other sources. Respondents never compared Oregon’s tax burden to other states, noting that, in Oregon, state taxes per capita are 11.8 percent below the national average and as a percent of gross state product, Oregon taxes are 14.8 percent below the national average.

In conclusion, as a result of the Supreme Court’s decision in *Moro*, over \$4 billion of the \$5.3 billion in benefits at issue have been protected. This represents a significant victory for PERS retirees and members. A complete copy of the decision can be found on the Supreme Court’s website at:

<http://www.publications.ojd.state.or.us/docs/S061452A.pdf>.

The Supreme Court’s press-release regarding the decision can be found at:

[http://www.ojd.state.or.us/SCA/WebMediaRel.nsf/Files/2015-04-30-Media_Release.pdf/\\$File/2015-04-30-Media_Release.pdf](http://www.ojd.state.or.us/SCA/WebMediaRel.nsf/Files/2015-04-30-Media_Release.pdf/$File/2015-04-30-Media_Release.pdf)