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SUPREME COURT OF THE STATE OF WASHINGTON

WASHINGTON EDUCATION ASSOCIATION, et al., and all others
similarly situated,

Respondents/Cross-Appellants,
v.

WASHINGTON STATE DEPARTMENT OF RETIREMENT SYSTEMS
and the STATE OF WASHINGTON,

Appellants/Cross-Respondents.

CHERYL COSTELLO, STEPHEN GORE, RICHARD MORVAN,
JERALD NEWELL, DAVID RENO, and FINN LIVINGSTON, on behalf
of themselves and a class of persons similarly situated,

Respondents,
v.

WASHINGTON STATE DEPARTMENT OF RETIREMENT SYSTEMS
and the STATE OF WASHINGTON,

Appellants.
v.

WASHINGTON FEDERATION OF STATE EMPLOYEES, PAULETTE
THOMPSON, DANA HUFFORD, and DON HEWITT,

Respondents/Cross-Appellants,
v.

WASHINGTON STATE DEPARTMENT OF RETIREMENT SYSTEMS
and the STATE OF WASHINGTON,

Appellants/Cross-Respondents.

 ORIGINAL

RESPONDENTS'/CROSS-APPELLANTS'
RESPONSE TO BRIEFS OF *AMICI*

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“Pension and other retirement plans are unique property rights ... in the nature of deferred compensation, as such they are not mere expectancies, but are vested rights possessed by employees.” *Farver v. Dept. of Retirement Systems*, 97 Wn.2d 344, 346, 644 P.2d 1149, 1150 (1982). Pension benefits are “not subject to full legislative control.” *Noah v. State*, 112 Wn.2d 841, 844, 774 P.2d 516, 517 (1989). *Amici* argue to the contrary that a right to withdraw pension benefits, even after work has been performed, may be reserved and exercised without complying with *Bakenhus v. Seattle*, 48 Wn.2d 695, 296 P.2d 536 (1956). But, as this Court recognized in *Navlet v. Port of Seattle*, 64 Wn.2d 818, 194 P.3d 221 (2008), “we cannot give effect to such an attempted reservation of rights by an employer” because Reservation Clauses are inconsistent with the nature of deferred compensation.

The Legislature repealed gain-sharing at a time when Washington’s pension system was one of the best funded in the country. Gain-sharing was not repealed in response to an economic crisis as amici argue. Its repeal was in response to a different funding policy promoted by a new State Actuary. Even if the repeal had been prompted by an economic crisis, Washington’s constitutional provision prohibiting impairment of contracts does not permit

the Legislature's exercise of plenary power to repeal a pension benefit compensating employees for work previously performed.

Two amici claim that this Court, even if it affirms the trial court, should void the gain-sharing benefits based on a severability argument never advanced by any party to this litigation and not properly raised now. RAP 9.12; *Long v. Odell*, 60 Wn.2d 151, 154, 372 P.2d 548, 550 (1962). The trial court held unconstitutional the 2007 law repealing gain-sharing and not the law amici ask this Court to find severable. The legal underpinnings of amici's argument – that the subjective intent of the Legislature in enacting pension legislation controls – do not apply under the now well-settled *Bakenhus* principle that employees' pension contracts are determined by the employees' expectations, not the Legislature's intent in granting them. *Navlet*, 164 Wn.2d at 834-35. ("The obligation arises independent of any required showing of the employer's express intent to provide retirement benefits....") As a vested property right, the class cannot be deprived of deferred compensation under the Contracts Clause.

The Legislature's separation of powers argument should also not be considered, as it too was not raised below. Moreover, the Final Judgment entered by the trial court does not interfere with the Legislature's plenary power to repeal gain-sharing prospectively for new hires.

Thousands of working employees made an irrevocable decision to transfer from a more generous defined benefit plan (Plan 2) to a partial defined contribution plan (Plan 3) relying on the State's communications promising gain-sharing as a new benefit in Plan 3. This Court has a longstanding history of enforcing employees' expectations in the context of pension benefits and should continue to follow that precedent here. *Washington Ass'n of Cy Officials v. Public Employees Retirement Sys. Board*, 89 Wn.2d 729, 733, 575 P.2d 230 (1978). (DRS practice gave rise to enforceable contract expectation.)

ARGUMENT

1. **The repeal of gain-sharing was not due to a fiscal crisis. And, fiscal necessity alone cannot justify impairment of a pension contract.**

- 1.1 **Financial considerations alone are insufficient justification to impair employees' pension contracts.**

Amici rely upon new evidence, not presented to the trial court, to argue that current economic data justifies the Legislature's repeal of gain-sharing. The new evidence is not properly before the Court and should be stricken pursuant to Respondents' Motion to Strike.

On review of an order granting or denying a motion for summary judgment, the appellate court *will consider only evidence and issues called to the attention of the trial court.*

RAP 9.12 (emphasis added).

Regardless, as in *Carlstrom v. State*, 103 Wn.2d 391, 694 P.2d 1 (1985) this Court should reject cost arguments as the sole justification for the State's impairment of its own contracts.

Financial necessity, though superficially compelling, has never been sufficient of itself to permit states to abrogate contracts. "[A] State is not completely free to consider impairing the obligations of its own contracts on a par with other policy alternatives." *United States Trust*, 431 U.S. at 30–31, 97 S.Ct. at 1522. If governments could reduce their financial obligations whenever an important public purpose could be conceived for repudiating a contract "the Contract Clause would provide no protection at all." *United States Trust*, 431 U.S. at 26, 97 S.Ct. at 1519.

103 Wn.2d at 396.

Fiscal necessity is only one of three required elements that must be met before the Court will find modification of pension benefits to be constitutional. *Bakenhus*. Respondent's Brief (Resp'ts' Br.) at 21.

1.2 Gain-sharing was not repealed in response to an economic crisis.

With no basis in the record, amici suggest that the Legislature repealed gain-sharing to respond to the State's worsening fiscal crisis. Yet, when EHB 2391 (the act repealing gain-sharing in 2007) was under consideration, the State Actuary [Smith] "did not raise [gain-sharing] as a fiscal integrity issue." Smith admitted that he was not aware of any allegation or

data that indicated repeal of gain-sharing was necessary to preserve the fiscal integrity of the pension plans. CP 1767. In fact, there was no fiscal crisis at that time.¹ Resp'ts' Br. at 15-16.

Although amici argue otherwise,² Respondents submitted competent evidence rebutting the State's allegations of fiscal necessity. Respondents demonstrated that the State would have saved more money had the Legislature merely ended the benefit for new hires, legislation which Respondents agree would have been constitutional. Resp'ts' Br. at 16-17.³

EHB 2391 repealed gain-sharing for those employees hired after July 2007. CP 238. Had the State only eliminated gain-sharing for new entrants employer contribution costs would have been reduced by \$3,220.1 million. CP 2636. The total net reduction in employer costs from all provisions of EHB 2391: the savings attributable to the repeal of gain-sharing for new entrants, savings attributable to the repeal of gain-sharing for existing members and the cost of new (replacement) benefits provided to existing members of all Plans and to new entrants to Plans 2 and 3 and Plan Choice,

¹Amici's submissions concede this fact, e.g. the "Report on Financial Condition (August 30, 2013)" references the "recession of 2009." Brief of the Washington State Legislature (Leg. Br.) App. at 3. This "recession" occurred two years after the Legislature repealed gain-sharing.

² See Association of Municipal Attorneys and Association of Cities ("Cities") Br. at 4.

³ The repeal was an unconstitutional impairment because simply ending the benefit for new hires was a less restrictive and constitutional alternative. See *Caritas v. Dept. of Social and Health Services*, 123 Wn.2d 391, 411, 869 P.2d 28 (1994), citing *Carlstrom*, 103 Wn.2d at 396.

was \$2,265.5 million. CP 2641. As Actuary Smith acknowledged, the Legislature would have saved *an additional \$954.6 million* if it had added no new benefits, but “simply eliminated gain-sharing for future new members” and left gain-sharing in place for existing members. CP 1771.

The argument that gain-sharing was repealed due to an economic crisis has no support in the record. Consequently, amici attempt to introduce new evidence in violation of RAP 9.12. Specifically, the State Actuary Report on Financial Condition, August 30, 2013 (Leg. Br., App. to Errata (“Report”)), is new evidence, and should not be considered pursuant to RAP 9.12, *supra*. See also Respondents’ Motion to Strike.

Furthermore, the Report does not support amici’s argument that dire consequences will flow from the invalidation of the repeal of gain-sharing. The Report is generally bullish on the status of the retirement plans. Focusing on the estimated “funded status” of the retirement plans “as a measure of the plans’ health and financial condition,” the Report explains:

[A] plan with a funded status of at least 100 percent is on target with its financing plan; whereas a plan with a funded status below 100 percent is off target... However, it’s important to note that “a plan with less than a 100 percent funded status is not automatically ‘at risk’ of not being able to meet future benefit obligations.”

Report at 2. The Funded Status of PERS, TRS and SERS 3 in 2012 were well above 100% while the Funded Status of PERS and TRS 1 were below

100% in 2012. Report at 5.⁴ Absolutely no evidence, including the Report, indicates that any Plan will change from “not at risk” to “at risk” if gain-sharing is reinstated. The Funded Status of PERS, TRS and SERS Plans 3 will remain above 100% while the Funded Status of PERS and TRS Plans 1 will drop by only 3%. Report at 6.

The Actuary Report described the decline in funded status to be “less than we expected in our last report due to higher than expected returns over the past few years. We also expect to see the funded status begin to improve for all plans.” *Id.* at 3, 7 (emphasis added). It also projected that “[plans] will be in a better financial position over the longer-term due to the lower investment return assumption.” *Id.* at 4.

1.3 Gain-sharing is a flexible benefit.

Amici rely on *SEIU Healthcare 775 NW v. Gregoire*, 168 Wn.2d 593, 601, 229 P.3d 774 (2010) in arguing that the repeal of gain-sharing is justified by the “public good.” Washington State Association of Counties (“Counties”) Br. at 20. This same argument, that the “public good” compels the impairment, was specifically rejected as a justification for the State’s impairment of its own contracts by this Court in *Caritas*.

⁴ The Report figures assume the impact of the reinstatement of *both* gain-sharing and the UCOLA. The Table reports the funded status of PERS, TRS and SERS 2/3. It does not segregate the Plans 2 from the Plans 3.

[A] state cannot refuse to meet its legitimate financial obligations simply because it would prefer to spend the money to promote the *public good* rather than the private welfare of its creditors. (Emphasis Supplied.)

123 Wn.2d 391 at 406 (quoting *United States Trust Co. v. New Jersey*, 431 U.S. 1, 29, 97 S. Ct. 1505, 1521 (1977) (“A state is not free to consider impairing its obligations on a par with other policy alternatives.” *U.S. Trust* at 1522.)

In *SEIU*, this Court did recognize the Legislature’s need for flexibility to meet public needs over private interests in times of crises. But, as the trial court here observed: “gain-sharing was designed as a flexible tool to recognize and equitably share extraordinary returns on the system’s investments.” CP 5109. Furthermore, *SEIU* concerned an application for a writ of mandamus seeking to compel the Governor, as a matter of equity, to revise her budget to fund an arbitration award. It has no application to a case sounding in contract law and certainly does not trump the well-established law of this State concerning the application of the Contracts Clause to pension benefits. Nor does it justify having public employees foot the bill for other public services.

The Legislature designed gain-sharing as a flexible benefit to be paid when there were *sustained extraordinary gains* on pension fund investments. When gain-sharing was enacted, the Legislature was well aware of

the funded nature of the pension system: Plans 1 were underfunded as they had been at least since they closed in 1977; Plans 2 & 3 were funded well over 100%. Resp'ts' Br. at 15. Both situations continue to be true today.⁵ Any change in their condition today is simply one of "degree rather than in kind," the type of change this Court has expressly disallowed as a justification for impairment of a state contract obligation. *Carlstrom*, 103 Wn.2d, 397 (relying on *United States Trust*, 431 U.S. at 30-31).

The Legislature did not repeal gain-sharing in response to a fiscal crisis and even if it had, that does not provide a sufficient justification for the Legislature to impair employees' pension contracts. As recognized by the trial court, gain-sharing is a benefit that is designed to be flexible to accommodate changes in the economy.

2. The exercise of the reservation to repeal gain-sharing impaired employees' pension contracts.

2.1 The gain-sharing benefit is a contractual benefit.

"[I]f the challenged legislation can properly be characterized as pension legislation, the principles of *Bakenhus* ... will govern its constitutionality." *Washington Fed'n of State Employees v. State*, 98 Wn.2d 677, 683,

⁵ In 2001, the Legislature repealed the portion of the 1998 gain-sharing statute that had committed one-half of extraordinary investment gains to paying down the historic underfunding of Plan 1. Laws of 2001, 2d Spec. Sess., ch. 11 § 10; Laws of 2001, ch. 329, § 10. Resp'ts. Br. at 40.

658 P.2d 634, 637 (1983). Pension benefits are scrutinized because “[t]his Court has recognized that state employees’ pension rights are of a contractual nature....” *Fed’n of Employees v. State*, 127 Wn.2d 544, 561-62, 901 P.2d 1028, 1037 (1995). Beyond a doubt, the legislation at issue is “pension legislation.”

But amici nevertheless claim that *Bakenhus* does not apply because the Legislature has “deemed” the gain-sharing pension benefit to be non-contractual. Under amici’s approach, the Legislature could statutorily disclaim all vested pension rights by simply passing legislation stating that its employees have no vested pension rights. Of course, *Bakenhus* and its progeny prevent this type of legislative re-characterization because:

construing the clause in the manner ... would allow [the State] unilaterally and retroactively to modify its contracts at will and without prior explicit notice. This result is antithetical to the intent of the contract clause. A promise in a contract that gives one party the power “to deny or change the effect of the promise is an absurdity.” *United States Trust Co.*, 431 U.S. at 25, n. 23.

Caritas Services, 123 Wn.2d at 407.

Agreements become contracts entitled to protection under the Contracts Clause not because of the term that the Legislature assigns to the relationship, but as a result of the nature of the arrangement itself:

[A] legislative enactment may contain provisions which, *when accepted as the basis of action by individuals*, become contracts between them and the State...

Gruen v. Tax Commission, 35 Wn.2d 1, 54, 211 P.2d 651, 681 (1949) (*quoting Indiana ex rel. Anderson v. Brand*, 303 U.S. 95, 58 S. Ct. 443 (1938)).

A contractual relationship may exist even when the State did not intend to make a contract: “The obligation [to provide a retirement benefit] *arises independent of any required showing of the employer’s express intent* to provide retirement benefits....” *Navlet*, 164 Wn.2d at 834-35 (emphasis added).⁶ In fact, a contractual relationship may arise even when the intent was to *not* create a contractual right.

Even assuming that the reservation of rights language in the trust agreement and the SPD *indicated the Port’s intent not to provide a vested right* to retirement welfare benefits in

⁶ The Legislature’s argument concerning the “unmistakability doctrine” – that there must be a clear statutory intent to create a contract right – is unavailing. Leg. Br. at 7. As noted in *United States v. Winstar Corp.*, 518 U.S. 839, 880, 116 S. Ct. 2432, 2457 (1996), the “application of the doctrine will ... differ according to the different kinds of obligations the Government may assume and the consequences of enforcing them.” In the context of pension rights, *Bakenhus* and its progeny specifically hold that the State may bind itself to pay pension benefits *even if it did not subjectively intend to do so*. See e.g. *Navlet*, 164 Wn.2d at 834-35. By entering into an employment relationship with its employees, of which their pension benefits are a part, the State has waived claims of sovereign immunity related to pension liability claims arising from that contractual relationship, the same as any other employer.

[B]y the act of entering into an authorized contract with a private party, the State, absent a contractual provision to the contrary, thereby waives its sovereign immunity in regard to the transaction and impliedly consents to the same responsibilities and liabilities as the private party... *Architectural Woods, Inc. v. State*, 92 Wn. 2d 521, 526-27, 598 P.2d 1372, 1375 (1979). (State was liable for interest on contract damages.)

the CBA, *we cannot give effect to such an attempt at reservation of rights by an employer.*

Id. at 848 (emphasis added). It is the “[c]ompensatory nature of the employment relationship” rather than intent that determines whether a contract subject to the Contracts Clause limitations exists. *Id.* at 834-35.

As this Court has consistently held, pension rights *are* by their very nature contractual benefits for work already performed.

[U]nder *Bakenhus* and its progeny the pension statutes are, at the least, contractual in nature – they are not subject to full legislative control. But this court in *Bakenhus* never held that a public retirement statute in and of itself constitutes a complete contract. In fact, there is no statutory analysis in *Bakenhus*. Further, as the court recognized in *Bakenhus*, the contract analysis might not be flawless in a purely legalistic sense, [but it] *gives effect to the reasonable expectations of the employee* and at the same time allows the legislature the freedom necessary to improve the pension system and adapt it to changing economic conditions.

Noah, 112 Wn.2d at 844-45 (emphasis added) (*quoting Bakenhus*, 48 Wn.2d at 701). The State cannot overrule *Bakenhus* by simply saying that pension rights are not contractual in order to avoid constitutional limits on its power.

Employees, working while gain-sharing was in effect, reasonably expected that gain-sharing would continue as long as they worked and thereafter as long as they were members of the retirement system, as found by

the trial court. The State communicated that gain-sharing was a unique feature of Plan 3⁷ in its materials enticing members to irrevocably transfer from Plan 2 (a pure defined benefit plan) to Plan 3 (a hybrid plan and cheaper for the employer) in order to be eligible for the new gain-sharing benefit in Plan 3. Many employees exercised this option. For example, 17,135 TRS 2 members transferred to TRS Plan 3 shortly after a legislator, chairing the Joint Committee on Pension Policy mailed a letter on State Legislature letterhead to every Plan 2 member highlighting gain-sharing as a Plan 3 benefit and making no mention of any reservation. CP 640 ¶ 12 and CP 1149.

DRS booklets distributed to employees described “*ongoing gain sharing*” (CP 3866, 3890, 4048, 4152) and stated that during periods of strong investment performance, “the gain sharing feature... *will* provide extra savings for the Defined Contribution component.” CP 3834, 4022, 4048, 4152 (emphasis added).⁸ As the State stipulated, no booklets referred to the Reservation Clause on which the State now relies. CP 898 (“Stipulation”).

Amici argue that DRS did not have authority to issue these materials to plan members because they exceeded the statutory language and as a re-

⁷ Gain-sharing is a benefit in Plan 3, but not in Plan 2.

⁸ See also Resp’ts’ Br. at 9-12 & nn.50-51 and Resp’ts’ Br. at 6 & n.22).

sult, DRS' promises cannot be enforced. Washington State School Director's Association (School Dir.) Br. at 17. However, under principles of equitable estoppel, a claim held applicable to the facts of this case by the trial court, the interests of justice do not permit the State to repeal the benefit after it communicated to members that gain-sharing was a plan benefit. *See Silverstreak v. Dept. of L&I*, 159 Wn.2d 868, 154 P.3d 891 (2007) (applying estoppel based on agency memo regarding requirements of prevailing wage law and estopping agency from applying new interpretation retroactively).

School Directors rely on *Ass'n of Capitol Powerhouse Eng'rs v. Div. of Bldg. and Grounds*, 89 Wn.2d 177, 570 P.2d 1042 (1977) to mistakenly argue that pensions are like other terms of employment for civil service employment and are controlled by statute. School Dir. Br. at 17. This Court has plainly distinguished pension benefits from other terms of employment. *Washington Fed'n of State Employees, AFL-CIO, Council 28 AFSCME v. State*, 101 Wn.2d 536, 541, 682 P.2d 869, 872 (1984). (Law requiring employees to exhaust vacation prior to retirement impaired employees' pension contract.) *See Washington Ass'n of Cy. Officials v. Washington Pub. Employees' Retirement Sys. Bd.*, 89 Wn.2d 729, 575 P.2d 230 (1978). (The practice of including vacation cash-out in pension calculation was part of employees' pension contract.)

Amici also argue that there can be no contract because the originating statute expressly stated that no contract was created. Yet, *Bakenhus* and its progeny are clear: a public employee's pension is "not a gratuity but is deferred compensation for services rendered." *McAllister v. City of Bellevue*, 166 Wn.2d 623, 628, 210 P.3d 1002 (2009) (citing *Bakenhus*, 48 Wn.2d at 698). Respondents were granted gain-sharing in 1998 (Plan 1) and 2000 (Plan 3) and worked while the benefit was in effect.

An overriding rule of construction in this area is that contracts must be construed to avoid rendering contractual obligations illusory. *Quadrant Corp. v. American States Ins. Co.*, 154 Wn.2d 165, 110 P.3d 733 (2005).⁹ If the State's promise of gain-sharing given in exchange for employees' work were subject to the Legislature's whim to repeal it, it would be illusory. Such a construction is not permitted.

2.2 Even with the Reservation Clause, gain-sharing became a part of employees' pension contracts.

Counties argues that no contract right was created based on the inclusion of the reservation in the originating statute. Counties Br. at 12-17. In doing so, Counties attempts to distinguish *Bakenhus* because there was

⁹ See also *Taylor v. Shigaki*, 84 Wn. App. 723, 730, 930 P.2d 340 (1997) and *St. John Med. Ctr. v. Dep't of Soc. & Health Serv's*, 110 Wn. App. 51, 68, 38 P.3d 383 (2002) ("An illusory contract is unenforceable because there is no consideration").

no reservation contained in the statute at issue and *Navlet* because the reservation was not contained in the collective bargaining agreement. These attempts fail for several reasons, many of which were fully briefed by Respondents. Resp'ts' Br. at 21-33.

Navlet confirms the then-longstanding and still applicable basis for the rule of *Bakenhus*. Retirement benefits are deferred compensation and are earned when the services are provided. “[R]etirement benefits vest at the time they are created if they are properly considered compensatory.” *Navlet*, 164 Wn.2d at 834.

[Courts] cannot give effect to such an attempted reservation of rights by an employer . . . [because] ‘[o]nce the employee fulfills the service requirements . . . the employee *acquires a contractual right* to those benefits, and the employer cannot abridge that right *despite an aboriginal reservation* of a power to effect unilateral amendments or to terminate the plan outright.’

Id. at 848 (emphasis added) (citations omitted).

The contractual obligation:

flows from the compensatory nature of the [benefit conferred] in the employment relationship, and does not necessarily flow from the collective bargaining relationship. The obligation arises independent of any required showing of the employer’s express intent to provide the retirement benefits.

Id. at 834-5.

The Legislature argues that “California – the source of the rule adopted in *Bakenhus* – refused to apply the California Rule in precisely the

circumstances presented here ...” Leg. Br. at 9. Its reliance on a lower court decision, *Walsh v. Board of Administration*, 6 Cal. Rptr. 2d 118, 4 Cal. App. 4th 682 (1992), to support the Legislature’s exercise of the reservation to repeal gain-sharing is misplaced as the case actually underscores the protected nature of the rights at issue here.

In *Walsh*, the issue was whether a former legislator’s pension benefits could be modified. The case turned on a specific provision of *the California Constitution* that at the time of the decision, expressly reserved the power of the Legislature to limit the retirement benefits of members of the Legislature before their retirement. *See former* Cal. Const., Art. IV, § 4, para. 3. Because modification of Walsh’s retirement benefits was consistent with this *constitutional reservation* (and the specific constitutional provisions concerning legislators’ retirement benefits took precedence over the more general contracts clause), the court approved the modification. In doing so, however, the court indicated that absent the specific constitutional provision applicable to legislators, the modification would have violated the Contracts Clause. *Walsh*, 4 Cal.App.4th at 698. It discussed *Legislature v. Eu*, 54 Cal.3d 492, 529-533, 816 P.2d 1309, 1331-1335 (1991) which held that pension rights are not subject to a take-away:

Pension rights, unlike tenure of civil service employment, are deferred compensation earned immediately upon the

performance of services for a public employer ‘[and] cannot be destroyed ... without impairing a contractual obligation....’

Id. at 533 (cited in *Walsh*, 4 Cal. App. 4th at 704). *Walsh* has no relevance because the Washington Constitution has no provision similar to that relied on by the California court.

2.3 Gain-sharing is not simply a legislative policy.

The Legislature argues that gain-sharing is simply a matter of policy that the Legislature can change at its whim. Leg. Br. at 13. The Honorable Richard Eadie, in his letter opinion correctly rejected this argument determining that gain-sharing is not a policy falling within the Legislature’s plenary power to unilaterally alter:

Defendants [State] argue that legislation, including the gain-sharing legislation at issue here, is a declaration of policy by the legislature and that the legislature inherently retains plenary power to change state policy. A standard dictionary definition of “policy” is “... a plan or course of action adopted by a government... designed to influence decisions, action and other matters: *American foreign policy*... [a] course of action, guiding principle, or procedure considered to be expedient, prudent, or advantageous: *honesty is the best policy*. *American Heritage Dictionary, New College Edition, 1980*. The adoption of a pension benefit such as gain-sharing does not express a guiding principle intended to influence decisions in a general sense. **Gain-sharing is a benefit (a retirement benefit)** or it may be thought of as a program, or an act or action to provide a benefit, **but does not fall within the legislature’s unchallenged power to direct changes in state “policy.”**

CP 5111 (emphasis added).

2.4 Gain-sharing is not a benefit granted “in perpetuity.”

Contrary to the Legislature’s argument, an affirmance of the trial court’s decision will not require that gain-sharing be paid “in perpetuity.” The trial court’s Final Judgment benefits the class, but does not award gain-sharing to employees hired after July 1, 2007. CP 6492-99.

Plans 1 are closed and the number of members in the class will diminish to zero as time passes. As to Plans 3, § 1(2) of EHB 2391 amended RCW 41.31A.020 to limit gain-sharing benefits to persons hired prior to July 1, 2007 and their number will eventually also diminish to zero. Employees hired after July 1, 2007 will not receive gain-sharing even under the trial court’s judgment. If the Court affirms the reinstatement of gain-sharing, it will not be in perpetuity.

2.4 Pension rights must be determined by the law in effect prior to the repeal of gain-sharing.

Respondents agree that pension rights should be determined by *the latest act that can constitutionally be applied*. Cities Br. at 15-20.¹⁰ The trial

¹⁰ See *McAllister v. City of Bellevue*, at 628-29, citing *Vallet v. City of Seattle*, 77 Wn.2d 12, 21, 459 P.2d 407 (1969). See also *Dailey v. City of Seattle*, 54 Wn.2d 733, 739, 344 P.2d 718 (1959) citing *Eisenbacher v. City of Tacoma*, 53 Wn.2d 280, 333 P.2d 642, 645 (1958) and *Letterman v. City of Tacoma*, 53 Wn.2d 294, 333P.2d 650 (1958).

court correctly invalidated the *2007 repeal* of gain-sharing.¹¹ Thus, the existing law prior to the repeal of gain-sharing – the 1998 and 2000 laws enacting gain-sharing – is the latest act that can constitutionally be applied.

3. The Legislature’s plenary power to create laws does not require reversal of the trial court’s reinstatement of gain-sharing.

The parties agree the 2007 Legislature was not bound in that it was free to repeal the benefits for new plan entrants after July 1, 2007, as it did. The real issues here are whether Art. I, § 23 of the Constitution, the “Contracts Clause,” insulates gain-sharing from repeal as to employees who worked prior to July 1, 2007; and whether the reservations are unenforceable as to those employees.

The Legislature argues that its “plenary authority” to make laws requires reversal of the trial court’s affirmative response to these disputed issues. Leg. Br. at 1. It then argues that this Court should avoid “constitutionalizing” “ordinary statutes” to avoid elevating the gain-sharing legislation to the status of a constitutional amendment. Leg. Br. at 3. However, the Legislature recognizes that its law-making power is “limited...by the state and federal constitutions.” Leg. Br. at 1. *Accord, Wash. State Farm Bureau Federation v. Gregoire*, 162 Wn. 2d 284, 290, 174 P.3d 1142 (2007).¹² (The

¹¹ Laws of 2007, ch. 491, § 13.

¹² The Legislature cites *Washington Farm Bureau* in support of its argument that the plenary power of the 2007 Legislature authorized it to repeal gain-sharing, *Washington Farm*

plenary power of the legislature is “limited by our state and federal constitutions.”)

The Legislature’s argument denigrates this Court’s constitutional authority where, as here, the Contracts Clause is implicated. Where the issue is whether the State has impaired its own contract (as opposed to a private contract), the Washington courts apply a heightened standard of review and independently analyze the case “to determine if the impairment was ‘reasonable and necessary.’” *Carlstrom*, 103 Wn. 2d at 394.

The Legislature’s plenary authority to enact legislation does not insulate a law from constitutional scrutiny. *Cf. Carlstrom*, 103 Wn. 2d at 396-97. (The fact that legislation was based on police power was “not sufficient to shield it from scrutiny when constitutional considerations are at stake.”)

The Legislature’s argument also misses the point that the trial court’s injunction did not interfere with the Legislature’s authority. The trial court did not declare EHB 2391 ineffective as to plan members who were

Bureau is distinguishable. There, the Court held that the Legislature’s plenary power enabled it to modify the expenditure limit enacted by a previous Legislature. Nothing in the Constitution insulated the expenditure limit from modification by a subsequent Legislature. *Farm Bureau*, 162 Wn.2d at 290 (no Contracts Clause violation), *id.* at 304 (no violation of separation of powers doctrine). Here, the 1998 and 2000 Legislatures enacted gain-sharing, a pension benefit. Under *Bakenhus* and its progeny, pension benefits cannot be diminished or repealed by subsequent Legislatures after the benefit is enacted and the employee works or continues to work.

first hired after its effective date. All the trial court held was that the Contracts Clause prohibited enforcement of EHB 2391 with respect to employees who became Plan members on or before its effective date.

The Court's application of the Contracts Clause in *Bakenhus* does not eliminate the Legislature's power to act. *Bakenhus* "allows the legislature the freedom necessary to improve the pension system and adapt it to changing economic conditions." The pension rights of employees "may be modified prior to retirement ... for the purpose of keeping the pension system flexible and maintaining its integrity" but in doing so, the Legislature must provide new benefits offsetting the loss from the benefits that are modified or repealed. *Bakenhus*, 48 Wn. 2d at 701

4. Severability principles cannot constitutionally be applied in this case.

The Legislature and Cities argue extensively that the Reservation Clause is non-severable from the 1998 and 2000 legislation that enacted gain-sharing, and any decision holding the Reservation Clause ineffective must also void the benefit itself. Leg. Br. at 15-19, Cities Br. at 11-20. For a variety of reasons, set out below, the Court should reject this argument.

4.1 Amici cannot raise new arguments on appeal.

The State did not make a severability argument in the trial court or in this Court. CP 1522-2674, 4879-4915. Amici are not permitted to raise

new arguments: “It is further well established that appellate courts will not enter into the discussion of points raised only by *amici curiae*.” *Long v. Odell*, 60 Wn.2d 151, 154, 372 P.2d 548, 550 (1962).

‘[T]he case must be made by the parties litigant, and its course and the issues involved cannot be changed or added to by friends of the court.’ This is a long established practice of Washington courts....

Bldg. Indus. Ass'n of Washington v. McCarthy, 152 Wn. App. 720, 749 n.12, 218 P.3d 196, 210 n.12 (2009) (citations omitted). This rule flows directly from RAP 9.12, *supra*.¹³

4.2 Under *Bakenhus*, the subjective intent of the Legislature is irrelevant.

Amici’s severability argument is premised upon the legal principle that the Court’s “primary duty in interpreting any statute is to discern and implement the intent of the legislature.” Leg. Br. at 18 (*quoting Washington Farm Bureau*, 162 Wn.2d at 300). Amici fail to acknowledge that pensions are subject to a different statutory analysis. The whole point of *Bakenhus* is that the Legislature, *notwithstanding its own intent*, is bound to provide pension benefits because it reflects compensation that has already been earned by the employee. *Navlet*, 164 Wn.2d at 834-35.

¹³ See also *Sourakli v. Kyriakos, Inc.*, 144 Wn. App. 501, 509, 182 P.2d 985 (2008) (citing RAP 9.12 as basis for declining to consider argument not made to the trial court); *Coronado v. Orona*, 137 Wn. App. 308, 318, 153 P.3d 217 (2007) (RAP 9.12 limits our review to issues brought to the trial court’s attention).

Precedent illustrates the flaw in amici's position. In *Leonard*, for example, the Legislature intended to strip retirees of pension benefits if they committed a felony. *Leonard v. City of Seattle*, 81 Wn.2d 479, 484, 503 P.2d 741, 745 (1972). Therefore, the City argued that under then-existing RCW 41.20.110, Mr. Leonard was not entitled to any pension benefit due to his felony conviction. *Id.* at 484. Legislative intent, however, did not prevail. Instead, relying upon *Bakenhus*, this Court held that despite the forfeiture requirement, Mr. Leonard had vested property rights in his pension benefit that could not be forfeited. *Leonard* at 485-86. This Court rejected the City's argument – the same arguments made by amici here – that his property right was “no greater than the contractual rights which created it, and plaintiff's pension vested conditionally only, to be canceled upon occurrence of the very condition upon which he had agreed it should be discontinued.” *Id.* at 485. Nor did this Court void his pension under a severability analysis because it was the Legislature's intent to only pay pensions to non-felons. The result is no different here.¹⁴

¹⁴ See also *Washington Federation of State Employees v. State*, 98 Wn.2d 677, 658 P.2d 634 (1983) striking down a provision requiring employees to exhaust vacation leave, disregarding legislative intent because its effect was to repeal employees' expected pension benefits.

4.3 It is the legislative repeal in EHB 2391, not the reservation itself that is unconstitutional.

In arguing that the gain-sharing benefit is not severable from the Reservation Clause, amici fail to understand which statute was declared unconstitutional. Cities Br. at 10 (stating that the “Plaintiffs’ argument hinges on whether this Court will strike down Section 3 of ESHB 2491 [former RCW 41.31.30 and Section 312(4) [former RCW 41.31A.020(4)]. Yet, the trial court did not invalidate any part of the 1998 or 2000 gain-sharing statute, nor did it invalidate the Reservation Clause itself. Rather, the trial court invalidated § 13 of EHB 2391, the **2007 legislation** which attempted to repeal gain-sharing, because the Legislature invoked the Reservation Clause to repeal gain-sharing in an unconstitutional way. CP 6492-6499.

4.4 The Reservation Clauses are severable in any event.

The general rule is that when part of an enactment is unconstitutional, only that section will be invalidated.

As a general rule “only the part of an enactment that is constitutionally infirm will be invalidated, leaving the rest intact.”¹⁵

To overcome this rule, amici must prove that “it is evident” that the constitutional parts would never have been enacted:

¹⁵ *Collier v. City of Tacoma*, 121 Wn.2d 737, 761, 854 P.2d 1046, 1058 (1993) (quoting *National Advertising Co. v. Orange*, 861 F.2d 246, 249 (9th Cir. 1988)).

Unless it is evident that the Legislature would not have enacted those provisions which are within its power, independently of that which is not, the invalid part may be dropped if what is left is fully operative as law.

Buckley v. Valeo, 424 U.S. 1, 108, 96 S.Ct. 612, 677 (1976).¹⁶

Here, the Reservation Clause in the 1998 and 2000 gain-sharing statutes is inherently separate from the grant of the gain-sharing benefit. As the Supreme Court held in finding that an unconstitutional legislative veto provision was severable, a veto (like a reservation) is inherently separate from the substantive provisions of a law:

Congress could not have intended a constitutionally flawed provision to be severed from the remainder of the statute if the balance of the legislation is incapable of functioning independently. See, e. g., *Hill v. Wallace*, 259 U.S. 44, 70-72 (1922) (Future Trading Act held nonseverable because valid and invalid provisions so intertwined that the Court would have to rewrite the law to allow it to stand). ***This is not a concern, however, when the invalid provision is a legislative veto, which by its very nature is separate from the operation of the substantive provisions of a statute.*** Indeed, when Congress enacted legislative-veto provisions, it contemplated that activity under the legislation would take place so long as Congress ***refrained*** from exercising that power.

Alaska Airlines, Inc. v. Brock, 480 U.S. 678, 684-685, 107 S. Ct. 1476, 1479 (1987) (emphasis added). The Reservation Clause, like a legislative veto, “contemplate that activity under the legislation would take place so long as

¹⁶ Accord, *State v. Abrams*, 163 Wn.2d 277, 285-86, 178 P.3d 1021, 1025 (2008).

[the legislature] *refrained* from exercising that power.” *Id.* Here the statutes that provide gain-sharing can function without the reservation clause.

It is not Respondents’ position that the Reservation Clause could never be exercised in a constitutional manner, only that EHB 2391 was not a constitutional exercise of that power. There is simply no basis for the astonishing suggestion of the Legislature that this Court invalidate the 1998 and 2000 gain-sharing laws because those laws include Reservation Clauses that are unenforceable in this case, but remain part of the statutes. Leg. Br. at 18-19. Non-severability cannot be a basis for such an outlandish suggestion since the Reservation Clauses were not struck down by the trial court and this Court should reject the invitation to reverse the trial court on a ruling it did not make.

CONCLUSION

The trial court’s judgment re-instating gain-sharing should be affirmed.

DATED this 14th day of October, 2013.

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CERTIFICATE OF SERVICE

I certify under penalty of perjury in accordance with the laws of the State of Washington that the original of the preceding Respondents'/Cross-Appellants' Response to Briefs of *Amici* was filed by email with the Washington State Supreme Court at *supreme@courts.wa.gov*. I also certify that a copy of the same was served on the following in the manner indicated below:

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Dear Supreme Court Clerk:

Attached for filing in the above matter are the Respondents'/Cross-Appellants' Motion to Permit Single Over Length Brief in Response to Multiple Briefs of *Amici* and Response to Briefs of *Amici*.

If you have any difficulty with the attached or have questions, please feel free to contact this office.

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