

E
/

NO. 87424-7

RECEIVED BY E-MAIL

SUPREME COURT OF THE STATE OF WASHINGTON

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

Respondents/Cross-Appellants,

v.

STATE OF WASHINGTON and DEPARTMENT OF RETIREMENT SYSTEMS,

Appellants/Cross-Respondents.

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

Respondents,

v.

STATE OF WASHINGTON and DEPARTMENT OF RETIREMENT SYSTEMS,

Appellants.

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

Respondents/Cross-Appellants,

v.

STATE OF WASHINGTON and DEPARTMENT OF RETIREMENT SYSTEMS,

Appellants/Cross-Respondents.

CROSS-APPELLANTS' REPLY

Edward Earl Younglove III, WSBA #5873
Younglove & Coker, PLLC
Westhills II Office Park
1800 Cooper Point Road SW, Bldg. 16
P.O. Box 7846
Olympia, Washington 98507-7846
(360) 357-7791

Harriet Strasberg, WSBA #15890
Law Office of Harriet Strasberg
203 Fourth Avenue E., Suite 520
Olympia, Washington 98501

Don Clocksin, WSBA #4370
Law Office of Don Clocksin
203 Fourth Avenue E., Suite 405
Olympia, Washington 98501

TABLE OF CONTENTS

I. INTRODUCTION..... 1

II. ARGUMENT..... 3

A. THE CONCEPT OF DEFERRED COMPENSATION DOES NOT PERMIT CONDITIONING A PENSION BENEFIT ON THE RESTORATION OF ANOTHER'S PENSION RIGHTS. 3

1. Pension Benefits are not Solely Determined by Statute. 4

2. An Automatic Repealer is a Qualitatively Different Condition Subsequent than are Service Requirements for Vesting..... 8

3. Pension Benefits Cannot Be Eliminated After Work has Been Performed..... 11

4. The Automatic Repeal Provision is Ineffective Because There Was No Agreement of the Parties. ... 15

B. THE SCHEME IS ATTRIBUTABLE TO THE ACT OF THE LEGISLATURE BECAUSE THE CONDITION WAS DRAFTED BY THE LEGISLATURE..... 19

C. THE REPEAL OF THE IMPROVED ERRFS FOR PLAN 2 MEMBERS VIOLATES *BAKENHUS* BECAUSE THERE IS NO FISCAL NECESSITY AND THESE EMPLOYEES RECEIVE NO REPLACEMENT FOR THE LOST ERRFS..... 22

III. CONCLUSION 25

TABLE OF AUTHORITIES

Cases

<i>Bainbridge Island Police Guild v. City of Puyallup</i> , 172 Wn.2d 398, 259 P.3d 190 (2011)	19
<i>Bakenhus v. City of Seattle</i> , 48 Wn. 695, 296 P.2d 536 (1956).....	passim
<i>Bates v. City of Richland</i> , 112 Wn. App. 919, 51 P.3d 816 (2002)	3
<i>Bowles v. Department of Retirement Systems</i> , 121 Wn.2d 52, 847 P.2d 440 (1993)	3, 5
<i>Bowman v. Webster</i> , 44 Wn.2d 667, 269 P.2d 960 (1954)	19
<i>Buchholz v. Storsve</i> , 740 N.W. 2d 107 (S.D. 2007).....	9
<i>City of Nat'l Bank of Anchorage v. Molitor</i> , 63 Wn.2d 737, 388 P.2d 936 (1964)	13
<i>Colorado Structures, Inc. v. Insurance Co. of the West</i> , 161 Wn.2d 577, 167 P.3d 1125 (2007)	17
<i>Dorward v. ILWU-PMA Pension Plan</i> , 75 Wn.2d 478, 452 P.2d 258 (1969)	6
<i>Eagan v. Spellman</i> , 90 Wn.2d 248, 581 P.2d 1038 (1978).....	2, 6, 8
<i>Feifer v. Prudential Ins. Co. of America</i> , 306 F.3d 1202 (2 nd Cir. 2002)...	7
<i>Halver v. Welle</i> , 44 Wn.2d 288, 266 P.2d 1053 (1954).....	16
<i>Int'l Ass'n of Firefighters, Local 1789 v. Spokane Airports</i> , 146 Wn.2d 207, 45 P.3d 186 (2002)	6
<i>Leonard v. City of Seattle</i> , 81 Wn.2d 479, 503 P.2d 741 (1972)..	5, 6, 7, 10
<i>Letterman v. City of Tacoma</i> , 53 Wn.2d 294, 333 P.2d 650 (1959).....	3, 11
<i>Ludwig v. Washington State Dept. of Retirement Systems</i> , 131 Wn. App. 379, 127 P.3d 781 (2006)	9, 10

<i>Marr v. Fisher</i> , 182 Or. 383, 187 P.2d 966 (1947).....	12
<i>McAllister v. City of Bellevue Firemen's Pension Board</i> , 166 Wn.2d 623, 210 P.3d 1002 (2009)	23
<i>McCall v. State of New York</i> , 219 A.D.2d 136, 640 N.Y.S. 347 (1996) .	12, 13
<i>Minish v. Hanson</i> , 64 Wn.2d 113, 390 P.2d 704 (1964).....	20
<i>Muckle v. Hoffman</i> , 119 Wash. 519, 205 P. 1048 (1922).....	22
<i>Navlet v. Port of Seattle</i> , 164 Wn.2d 818, 194 P.3d 221 (2008).....	2, 7, 21
<i>Oregon-Washington, R. & Nav. Co. v. Seattle Grain Co.</i> , 106 Wash. 1, 8, 178 P. 648 (1919)	17
<i>Pabst v. Fischer</i> , 13 Ohio App. 302 (1920).....	19
<i>Robertson v. Kulongoski</i>	7
<i>State v. Duren</i> , 547 S.W.2d 476 (Mo. 1977)	12
<i>Strunk v. Public Employees Retirement Board</i> , 338 Or. 145, 108 P.3d 1058 (2005)	7
<i>Tatum v. Wheelless</i> , 180 Miss. 800, 178 So. 95 (1935).....	12
<i>Vallet v. City of Seattle</i> , 77 Wn.2d 12, 459 P.2d 407 (1969).....	3, 23
<i>Washington Association of County Officials v. Washington Public Employee Retirement Board</i> , 89 Wn.2d 729, 575 P.2d 230 (1978) ..	5, 23
<i>Washington Federation of State Employees v. State</i> , 98 Wn.2d 677, 658 P.2d 634 (1993)	5, 18, 20, 23
<i>Webb v. Whitley</i> , 114 Ga. App. 153, 150 S.E.2d. 261 (1966).....	9

Constitutional Provisions

Wash. Cont. art. I, § 23	19
--------------------------------	----

Other Authorities

17A C.J.S. Contracts § 451 16

25 Wash. Prac. Contract Law and Practice § 8.5..... 15

5 Williston on Contracts (3d ed.) § 667 15

Black’s Law Dictionary, 7th Ed. (1999)..... 16

Restatement Second, Contracts § 224..... 15

I. INTRODUCTION

Since the enactment of EHB 2391 in 2007 adding the “improved” Early Retirement Reduction Factors (ERRFs) as a benefit for Plan 2 members of the state’s retirement systems, numerous Plan 2 members have benefited by retiring early without a reduction in retirement benefits. Many more Plan 2 employees have worked since that time with the expectation of taking advantage of the benefit to retire early with a reduced penalty when they become eligible.¹ Correspondingly, the contributions of all Plan 2 members have been increased to pay for the cost of the improved ERRFs.

Nevertheless, the State argues, albeit erroneously, that because the Plan 2 employees’ contract right to continuation of the ERRFs was contingent, the State has no obligation to provide these improved ERRFs to other Plan 2 members as they become eligible and that there is no impairment if the court gives effect to the automatic repeal provision triggered by the re-instatement of gain-sharing.

This Court should not give effect to the condition automatically repealing the improved ERRFs should the repeal of gain-sharing be held

¹ Plan 2 employees with 30 years of service can retire prior to age 65 with more favorable benefit reductions. Those 62 or older can retire with no reduction in their monthly retirement allowance. Those ages 55-62 can retire with a lesser reduction in their benefits than under earlier ERRFs. *See* EHB 2391 Fiscal Note, at CP 6932-33. *See also* State’s Cross-Resp., at 41 and Cross-Appellants’ Brief in Support of Cross-Appeal, at 62.

to be unconstitutional. This contingency is not enforceable for many of the same reasons that the Reservation of Rights (ROR) in the statute enacting gain-sharing is unenforceable. Members have provided service with the expectation of receiving the benefit, and have made higher contributions to pay for it. The condition repealing the improved ERRFs was imposed by law, not by agreement of Plan 2 members. Additionally, giving effect to the automatic repeal provision causes the pension benefits to be unconstitutionally unpredictable and arbitrary.

The Court should also reject the State's argument that because the court, not the legislature, is the "actor" triggering the automatic repeal of the ERRFs, the constitutional prohibition against the passage of laws that impair contracts is not violated.² The legislature designed and implemented the scheme through its enactment of the law granting the ERRFs. Thus, the legislation's consequences are as attributable to the legislature as they would be if it had acted directly.

Bakenhus, Navlet,³ and other previous decisions invalidating laws that impair public pensions⁴ are applicable to this case despite the State's

² "No bill of attainder, ex post facto law, or law impairing the obligations of contracts shall ever be passed." Const. art. I, § 23.

³ *Bakenhus v. City of Seattle*, 48 Wn. 695, 296 P.2d 536 (1956) and *Navlet v. Port of Seattle*, 164 Wn.2d 818, 194 P.3d 221 (2008).

⁴ See e.g. *Eagan v. Spellman*, 90 Wn.2d 248, 581 P.2d 1038 (1978) (reduction in mandatory retirement age reducing employee's pension impaired employee's pension contract),

contention that none concerned a conditional benefit. The improved ERRFs were provided to Plan 2 employees who were not eligible for gain-sharing. For in excess of six years now, these members have provided service and made contributions with the expectation of receiving the benefit.⁵ This Court should reject the State's arguments and protect a valuable pension benefit of Plan 2 employees from unconstitutional infringement.

This appeal is filed on behalf of only Plan 2 members. If this Court affirms the trial court's Phase 1 ruling, these employees will otherwise not receive any benefit from the invalidation of the repeal of gain-sharing in contrast to Plan 3 members who will receive gain-sharing.

II. ARGUMENT

A. THE CONCEPT OF DEFERRED COMPENSATION DOES NOT PERMIT CONDITIONING A PENSION BENEFIT ON THE RESTORATION OF ANOTHER'S PENSION RIGHTS.

A condition subsequent which acts to arbitrarily divest employees' vested pension rights is a non sequitur. Whether the automatic repeal lan-

Letterman v. City of Tacoma, 53 Wn.2d 294, 333 P.2d 650 (1959) (employee entitled to benefit of plan in effect when employment commenced rather than those of later plan that did not provide benefits of comparable value); *Vallet v. City of Seattle*, 77 Wn.2d 12, 459 P.2d 407 (1969) (modification of pension after commencement of employment valid as it offered corresponding benefit for loss of pension rights); and *Bates v. City of Richland*, 112 Wn. App. 919, 51 P.3d 816 (2002) (City's new pay plan impaired employee's pension contract).

⁵ In *Bowles v. Department of Retirement Systems*, 121 Wn.2d 52, 68, 847 P.2d 440 (1993) the court found that a DRS practice had become an "established [pension] policy" after 4 to 10 years. Plan 2 members have worked with the ERRFs in place for approximately 7 years now.

guage is a condition subsequent to the State's contractual obligation to provide Plan 2 employees' improved ERRFs is immaterial because this condition subsequent is ineffective as part of a deferred compensation package.

The Court should reject the State's view that a Plan 2 member's right to benefit from the improved ERRFs is subject to the operation of a condition subsequent that could divest them of the benefit as it is not supported by the law. Giving effect to the divestiture eliminates a significant pension benefit that for more than six years the employees rendered services expecting to receive and, in addition, that they paid for in the form of increased pension contributions.⁶

1. Pension Benefits are not Solely Determined by Statute.

In Washington State, pension benefits are not solely determined by the pension statutes, despite the State's characterization. (State's Cross-Resp., at 43). Service provided while the contract terms are in place give rise to the contractual obligation to provide Plan 2 members with the opportunity to take advantage of the new ERRFs once they have met the eligibility requirements. It is well-recognized that pension benefits are more than contract rights. See *Leonard v. City of Seattle*, 81 Wn.2d 479, 486,

⁶The State admits that Plan 2 members paid for the improved ERRFs for both Plans 2 and 3 in the form of higher contribution rates. Defendant's Cross Motion on Summary Judgment on Phase 2, at 11, fn 45 (CP 5998).

503 P.2d 741 (1972) (describing the employees' pension as "more than an expectancy and more than an enforceable promise or a contract").

In addressing the issue of what constitutes a public employee's pension contract, Washington courts have given paramount importance to the employee's "reasonable expectations" regarding their pension benefits. In several cases, employee expectations based on DRS administrative practices—even though not authorized by the express terms of the pension statutes—have been held to be vested contractual pension rights. See *Bowles v. Washington Dep't of Retirement Systems*, 121 Wn.2d 52, 67-8, 847 P.2d 440 (1993); *Washington Federation of State Employees v. State*, 98 Wn.2d 677, 658 P.2d 634 (1993) (DRS administrative practice of including vacation pay in pension calculations could only be changed as to new employees.); and *Washington Association of County Officials v. Washington Public Employee Retirement Board*, 89 Wn.2d 729, 575 P.2d 230 (1978). (The same 25 year practice of retirement board regarding vacation pay led to "legitimate contractual expectations" upon which members were entitled to rely and which State was bound to honor.)

The State's "statute centric" view of public employees' pension contracts is not only contrary to the case law in Washington State, it is inconsistent with this Court's previous focus on the pension expectations for

which employees work. A pension benefit “flows from the compensatory nature of the [benefit conferred] in the employment relationship’ . . . independent of any required showing of the employer’s express intent to provide retirement benefits.” *Eagan v. Spellman*, 90 Wn.2d 248, 257, 581 P.2d 1038 (1978), quoting in part from *Int’l Ass’n of Firefighters, Local 1789 v. Spokane Airports*, 146 Wn.2d 207, 221, 45 P.3d 186 (2002).

The contract pension obligation “will arise...even though the pensioner does not know the precise terms of the pension agreement.” *Dorward v. ILWU-PMA Pension Plan*, 75 Wn.2d 478, 483, 452 P.2d 258 (1969). Significantly, an employee’s pension rights develop “in a continuing process of vesting through a continuing contract of employment in the public service.” *Leonard v. City of Seattle*, 81 Wn.2d 479, 490, 503 P.2d 741 (1972). (Statute that purported to forfeit an employee’s pension for conviction of a felony ruled as ineffective).

That the retirement pension arises out of a contract of employment does not deprive it of the characteristics of property, but rather imparts to it that very characteristic by removing it from the status of a gratuity, mere expectancy, or simply a promise enforceable ultimately by no more than a judgment for damages.

...

Even before ripening finally, and during the years of its accrual, it was more than expectancy and more than enforceable promise or a contract, it gave [the employee] **steadily accruing rights** in and to the pension fund itself. As fully

ripened, plaintiff's pension contributed property – the present right to payment of his deferred compensation. When his rights to the pension fully vested, he acquired enforceable rights to funds under the control of the trustees according to his contract, and these rights thus finally vested constituted property not to be divested or defeated by means or for other reasons or on different grounds than those upon which any other kind of property could be alienated or defeated.

Leonard, 81 Wn.2d at 486. (Emphasis added).

Pension rights in Washington State are more broadly defined than they are in Oregon and some other states. In *Robertson v. Kulongoski*, 466 F.3d 1114 (9th Cir. 2006),⁷ that court, relying on *Strunk v. Public Employees Retirement Board*, 338 Or. 145, 108 P.3d 1058 (2005), noted that Oregon had adopted the view that employees' pension rights were limited to those expressed in the pension statutes. On that basis, the court held that the state was not obligated to continue a benefit that was not created by statute. This view, of course, is contrary to Washington's more expansive view of employees' pension benefits noted previously as including, for example, DRS practices, and was specifically rejected in *Navlet*.⁸

The *Bakenhus* court acknowledged that the application of contract theories to pension benefits “may not be flawless in a purely legalistic

⁷ See State's Reply, at 10.

⁸ Washington's approach is also more consistent with the federal court's approach in ERISA cases. In *Feifer v. Prudential Ins. Co. of America*, 306 F.3d 1202 (2nd Cir. 2002) a program summary—only material made available at the time—was held to constitute “the plan” and established the rights of participating employees.

sense” and that the object was to give “effect to the reasonable expectations of the employee.” *Bakenhus*, 48 Wn.2d at 701; See also *Eagan v. Spellman*, 90 Wn.2d 248, 257, 581 P.2d 1038 (1978).

Consequently, a condition in a statute that makes a pension benefit potentially revocable at some future date is ineffective to deprive a Plan 2 member of a property right they have already acquired by working.

2. An Automatic Repealer is a Qualitatively Different Condition Subsequent than are Service Requirements for Vesting.

The State admits that Plan 2 employees have a contract right to the improved ERRFs, albeit one it contends is contingent, and that these benefits have a “significant monetary value” to employees. (State’s Cross-Resp., at 41). The State argues, however, that the continuation of the benefit can be, and in this case was, made contingent upon the condition that there is no restoration of the gain-sharing benefit for the members of Plans 1 and 3. (State’s Cross-Resp., at 43). This argument hinges on its contention that the contingency is effective because it is similar to a condition such as the requirement for vesting. Yet, the automatic repeal provision is qualitatively different from the requirements for the vesting of pension benefits.

The State’s reliance on several cases concerning the rights of spouses or third party beneficiaries to support its argument is misplaced

since the rights at issue here concern the vested rights of the Plaintiff employees themselves. The State cites *Webb v. Whitley*, 114 Ga. App. 153, 150 S.E.2d, 261 (1966) for the proposition that “a contract within the meaning of the constitution” cannot be a contingent one. (State’s Cross-Resp., at 43-4). *Webb* held that the rights were not vested in the employee’s surviving spouse but were dependent entirely upon the employee’s rights. *Buchholz v. Storsve*, 740 N.W. 2d 107 (S.D. 2007) similar to *Webb* also concerned the right of a beneficiary, an expectancy interest.

The State also relies on *Ludwig v. Washington State Dept. of Retirement Systems*, 131 Wn. App. 379, 127 P.3d 781 (2006) (State’s Cross-Resp., at 45) for the proposition that because the exercise of pension rights is subject to a condition precedent – the number of years of service before a public employee’s pension rights are vested, a condition subsequent in the form of an automatic repeal provision is also effective.⁹ Like the above-referenced cases, *Ludwig* involved the issue of standing and the rights of a third party beneficiary.

A designated condition precedent, such as a requisite period of service prior to vesting, is very different from the condition presented here. The *Ludwig* court’s full statement was:

⁹ State’s Cross-Resp., at 45.

A public employee's vested pension rights are limited in two respects: first, they are subject to any designated condition precedent, such as a requisite period of service, and second, they are subject to reasonable modifications aimed at keeping the pension system secure and flexible in the face of changing economic conditions. [Citing *Bakenhus*]

Ludwig, 131 Wn. App., at 383.

Vesting is a condition that is predictable, certain, and announced at the beginning of employment. RCW 41.32.765(1); RCW 41.35.420(1); RCW 41.40.630(1). For the most part, an employee can choose to stay employed in order to meet the years of service required to become fully vested. If not, their monetary contributions are returned to them with interest.

Plaintiffs have not contested that Plan 2 employees would need to have the requisite years of service and meet the age requirements to “qualify” for the benefits afforded by the improved ERRFs. Assuredly, an employee must meet these qualifications to receive the promised pension. He or she may have to work for a certain minimum period of time or reach a certain age, for example. These prerequisites are far different than a condition that purports to operate by divesting an employer of a promised benefit for which the employee is qualified and has worked.

The automatic repeal provision is not predictable and it is arbitrary. And, it is certainly not equitable. *Leonard v. City of Seattle*, 81 Wn.2d

479, 487, 503 P.2d 741 (1972) citing *Letterman v. Tacoma*, 53 Wn. 2d 294, 333 P.2d 650 (1958). (Employee's pension cannot be detrimentally modified if the modifications are inequitable.) There is an inequitable and disparate effect on employees if the provision is implemented. Some Plan 2 employees will pay for the improved ERRFs through increased contributions and have been or will be able to take advantage of the benefit based on their age and years of service. Others who are newer to service may in the future have their contributions decreased, as the State argues, so that their contributions for the improved ERRFs will have been inconsequential. But, there are many others who are on the cusp, either due to their age or because they do not yet have the requisite years of service, who are paying for the improved ERRFs through increased contributions but for whom the date of the court decision will come just a little too soon to enable them to either take advantage of the new benefit of retiring earlier than they were hoping and expecting to receive, or to benefit substantially from reduced future contributions during their few remaining years of service.

3. Pension Benefits Cannot Be Eliminated After Work has Been Performed.

The State mistakenly relies on a number of cases for the proposition that a statute's provisions can be made effective on the condition that a later event occur. (State's Cross-Resp., at 44). The statute granting the

improved ERRFs became effective in 2007. Since that date, Plan 2 members have worked for and paid for this benefit. A statute effective upon the occurrence of a later event where service has not been induced or where the benefit has not become vested is not comparable. EHB 2391 created a new retirement benefit for Plan 2 members to induce their performance and then will eliminate the benefit upon the occurrence of a later event after the employees have performed. These situations are, to coin a phrase used by the State, qualitatively distinct.

The cases cited by the State for the proposition that certain benefits (not pension benefits) have been allowed to terminate if a statute granting them is found unconstitutional do not concern a situation where service has been provided and as a result, the deferred compensation has been, in a sense, earned. Moreover, unemployment benefits (*Tatum v. Wheelless*, 180 Miss. 800, 178 So. 95 (1935)); a lesser criminal penalty (*State v. Duren*, 547 S.W.2d 476 (Mo. 1977)); and increased income tax benefits (*Marr v. Fisher*, 182 Or. 383, 187 P.2d 966 (1947)) are not contractual, do not involve rights that have already begun vesting, and do not implicate impairment of contract issues.

Neither does *McCall v. State of New York*, 219 A.D.2d 136, 640 N.Y.S. 347 (1996) support the State's position that a contingent contract

cannot be impaired. (State's Cross-Resp., at 45). In that case, the court first held that Section 13 of the law changing the funding method for the retirement fund at issue was unconstitutional because it impaired the employees' pension contracts. Another section, Section 16, which made the timing of a payment to employees' contingent on the commencement of litigation regarding the constitutionality of Section 13, was not analyzed under a contract impairment analysis, but rather whether it denied employees the right of access to the courts. The court analyzed whether Section 16 "intolerably conditions a benefit on the waiver of a constitutional right, namely, the right to seek a judicial determination of the constitutionality of the credit provision." *Id.*, at 140-1. Further, unlike the automatic provision at issue here, the challenge to Section 16 did not concern a condition that completely eliminated a benefit, but one which merely delayed it to a date certain.

City of Nat'l Bank of Anchorage v. Molitor, 63 Wn.2d 737, 388 P.2d 936 (1964) does not stand for the proposition attributed to it by the State. (State's Cross-Resp., at 46). The actual holding in that case was that parol evidence is not admissible to prove a condition subsequent that contradicts the terms of an oral contract. That the outcome of pending litigation can be an effective condition subsequent excusing performance of

a contract obligation was *dicta* in that case and was not actually determined.

The court should reject the State's suggestion that it construe the statute (EHB 2391) as conditioning Plan 2 employees' rights to the continuation of the improved ERRFs, that they have worked and paid for since 2007, on the condition of the gain-sharing benefit not being restored as a pension benefit for Plan 1 and 3 members. The State cannot effectively disclaim the contractual nature of a promised pension benefit after an employer has enjoyed the benefit of the employee's service. The service was elicited with the promise of the benefit and so created the expectation of receiving the benefit.

Such a "bait and switch" is surely contrary to the characterization of pension benefits as deferred compensation for work already performed. The effect is similar to the ineffective ROR in the statute enacting gain-sharing since the legislature reserved the potential elimination of the benefit, albeit through the judicial process, after the employee provided the service the benefit was intended to produce. An employee's right to a pension cannot be a gamble that the benefit will still be there when the time comes for the employee to retire.

4. The Automatic Repeal Provision is Ineffective Because There Was No Agreement of the Parties.

The State argues that a decision restoring gain-sharing for Plan 1 and 3 employees is a condition subsequent and operates to divest Plan 2 employees of the improved ERFFs after they worked and paid for them.

The term 'condition subsequent' as normally used in contracts in contrast to 'condition precedent' should mean subsequent to a duty of immediate performance, that is, a condition which divests a duty of immediate performance of a contract after it has once accrued. Such conditions are very rare.

5 Williston on Contracts (3d ed.) § 667.¹⁰

Such a condition is ineffective in pension legislation because it is contrary to the concept of deferred compensation just as is a ROR, it has an arbitrary and inequitable effect and it was not agreed to by the parties.

A condition subsequent is any event the existence of which, *by agreement of the parties*, operates to discharge a duty of performance that has arisen.

25 Wash. Prac. Contract Law and Practice § 8.5 [Emphasis supplied].

As noted in another treatise:

A condition subsequent presumes a valid contract and refers to a future event, which divests a preexisting contractual liability. Thus, a contract that is conditioned to become void on a specified event is one subject to a condition subsequent. The fact that a promise is made depending on

¹⁰ The Restatement of Contracts no longer uses the term "condition subsequent" and instead, simply refers to "conditions." Restatement Second, Contracts § 224.

a condition subsequent does not affect its validity. A condition subsequent does not delay the enforceability of a contract, as it only preserves the possibility that contract can be set aside later in time if a condition is not fulfilled. A condition subsequent, upon its happening, provides a party the option to either to terminate the contract or not to terminate it. The termination of a contract by a condition subsequent has the effect of a **mutual rescission, because it is a term agreed to by the parties to bring the contract to an end upon the occurrence of the condition.**

Conditions subsequent are not favored by the law, and are construed strictly. The intent to create a condition subsequent must appear expressly or by clear implication, although no precise technical words are required to create a condition subsequent in a contract. If doubt exists, a clause will be construed to create a covenant and not a condition subsequent. A contract, however, does not have to expressly provide that if performance subsequently becomes impossible or impracticable, then the parties are excused from their obligations, as the law implies that as a condition subsequent.

17A C.J.S. Contracts § 451. [Citations omitted] [Emphasis supplied].

An essential element of a condition subsequent is missing here. As stated, *a condition subsequent is only effective if it has been agreed to by the parties.*¹¹ But here, there was no agreement. It has long been the rule that “[a] liability created by statute is one in which no element of agreement enters. It is an obligation which the law creates in the absence of an agreement.” *Halver v. Welle*, 44 Wn.2d 288, 291, 266 P.2d 1053 (1954),

¹¹ “A condition that, if it occurs, will bring something else to an end; an event the existence of which, *by agreement of the parties*, discharges a duty of performance that has arisen.” Black’s Law Dictionary, 7th Ed., at 289 (1999) (emphasis added).

quoting *Oregon-Washington, R. & Nav. Co. v. Seattle Grain Co.*, 106 Wash. 1, 8, 178 P. 648 (1919).

Plan 2 members who were never entitled to gain-sharing received a new benefit in the form of the improved ERRFs in 2007. Those benefits were provided by law and not by agreement. Any agreement implied by their service is legally distinct from the types of agreement inherent in the cases involving effective conditions cited by the State.

Specifically, *Colorado Structures, Inc. v. Insurance Co. of the West*, 161 Wn.2d 577, 167 P.3d 1125 (2007) is inapposite. That case involved an action to recover on a subcontractor's performance bond. The court held that the general contractor's right to sue the surety on the bond was not conditioned on the contractor's formal declaration that the subcontractor was in default. The decision reflected an interpretation of the expressly agreed upon terms of the bond and has no application to the facts here which do not involve an express agreement between the parties.

The State's suggestion that the union plaintiffs agreed to the condition because representatives testified in support of the legislation has no support in contract law. Plan 2 members never agreed to repeal of the ERRFs in the event gain-sharing is re-instated. Nor is there any evidence to support that the unions agreed to the automatic repeal provision.

Working while the statute was in effect does not amount to an implied agreement to the conditional nature of the benefit. Such an implication is contrary to the concept of pension benefits as deferred compensation for services and contributions provided to the State for at least the past six years. Nor can an agreement can be implied, since employees' pension benefits are determined by the employees' expectations based on practice as well as statute, even if not authorized by the express terms of the statute, and even if many employees were not aware of the specifics regarding their benefits. *Washington Federation of State Employees*, 98 Wn.2d, at 635-636. Our courts have presumed employees work for and expect to receive the benefits in effect while they work. The improved ERRFs have been in effect for more than six years. The expectation of unconditionally receiving the improved ERRFs is certainly reasonable since Plan 2 employees are also paying for them.

Plan 2 employees are not party to an agreement that would make the automatic repeal provision an effective condition subsequent to their right to the improved ERRFs. Rather, a pension is a unilateral contract where an offer is accepted by working. Once the offer is accepted through work, the State cannot retroactively enforce a condition as that would be contrary to the principles of deferred compensation. Where a promise is

intended to induce performance and performance is indeed induced, the court should not give effect to a condition subsequent that would eliminate the consideration promised in exchange for the performance, particularly in the complete absence of the performing party's agreement.¹²

B. THE SCHEME IS ATTRIBUTABLE TO THE ACT OF THE LEGISLATURE BECAUSE THE CONDITION WAS DRAFTED BY THE LEGISLATURE.

The State argues because it is the act of the court that will invalidate the repeal of gain-sharing, and result in the repeal of the improved ERRFs, that consequently, there was no law passed impairing contract as prohibited by the provisions of Wash. Cont. art. I, §23. (State's Cross-Resp., at 47-8). However, the State ignores that the condition was drafted by the legislature. The court is an actor in the legislative scheme that was envisioned to eliminate benefits after service has been rendered. It is the

¹²The State's acceptance of performance by employees in the form of their services and their payment for the cost of the improved ERRFs also waives the condition subsequent.

A waiver is the intentional and voluntary relinquishment of a known right, or such conduct as warrants an inference of the relinquishment of such right.

Bainbridge Island Police Guild v. City of Puyallup, 172 Wn.2d 398, 409, 259 P.3d 190, 195 (2011) citing *Bowman v. Webster*, 44 Wn.2d 667, 669, 269 P.2d 960 (1954). See also *Pabst v. Fischer*, 13 Ohio App. 302 (1920) (landlord's acceptance of tenant's rent constituted waiver of condition subsequent requiring tenant to give ten days' notice to continue tenancy). By accepting the employees' service, the State should be held to have waived the condition that might then divest the employees of the benefit.

implementation of the condition, as enacted by the legislature, that is a legislative act impairing contracts.¹³

Minish v. Hanson, 64 Wn.2d 113, 390 P.2d 704 (1964), relied on by the trial court and cited by the State, does not support its argument for two reasons. (State's Cross-Resp., at 47). First, *Minish* is neither a pension case nor a unilateral contract case. The case involved a contractor's claim that its executory agreement with the water district would be impaired if the water district was dissolved in accordance with a statutory provision that pre-dated the agreement. The court did not decide whether the proposed dissolution was a legislative act, but assumed that it was and held that the suit was premature because the dissolution had not yet occurred. If it was not a legislative act, then the contract, which had not been performed, was deemed to have been made in contemplation of the law permitting the dissolution of the water district. In either case, the court said it did not reach the impairment issue.

While *Minish* and the cases cited in the State's Cross-Resp., at 47, correctly state the rule that generally contracts are not impaired by statutes existing at the time the contract was entered into, the provisions in the

¹³ *Washington Federation of State Employees, supra*. (The Legislature could not indirectly impair employees' pension right to include vacation pay in pension calculations through legislation requiring employees to take their leave, because it could not have done so by directly prohibiting the inclusion of leave cashout payments.)

statutes discussed in each of those cases were already “in effect” when the contracts were entered. In contrast, the vast majority of Plan 2 employees, and particularly those “on the cusp” of eligibility for the improved ERRFs, have been rendering services (and continue to render services) prior to the effectiveness of the conditional provision purporting to repeal the improved ERRFs.

The State cannot have it both ways: offer a benefit to induce employees to enter or remain in employment and at the same time create a condition that will eliminate the benefit after the employees’ performance. That is the holding of *Navlet v. Port of Seattle, supra*. The cases cited by the State do not involve the concept of deferred compensation and do not involve the situation where performance has at least been partially rendered by the other party.

The impact on employee’s pensions is exactly the same whether the repeal of the ERRFs is the result of a legislative act or a court striking down an unconstitutional act. In the latter situation, the court has become the actor implementing a scheme drafted and enacted by the Legislature. As a party to a contract, the State should not be permitted to benefit from its wrongful or illegal act (the repeal of gain-sharing) when the other party (Plan 2 members) have performed in good faith by providing services and

where an injustice would otherwise result. *Muckle v. Hoffman*, 119 Wash. 519, 205 P. 1048 (1922). (Defendant refused to execute the contract after the plaintiff had performed.)

Ultimately, there is no sound basis for this Court to hold the “reservation” in the gain-sharing statute is ineffective in a pension statute, thus protecting a vested contract right from impairment, but give effect to a “condition” in EHB 2391 denying that protection to another vested contract right, the improved ERRFs for Plan 2 employees.

C. THE REPEAL OF THE IMPROVED ERRFS FOR PLAN 2 MEMBERS VIOLATES *BAKENHUS* BECAUSE THERE IS NO FISCAL NECESSITY AND THESE EMPLOYEES RECEIVE NO REPLACEMENT FOR THE LOST ERRFS.

The State admits that the 2007 benefits that it refers to as “replacement benefits,” specifically including the ERRFs, “had significant monetary value, as well as other advantages to plan members.” (State’s Cross-Resp., at 41). However, it persists in the erroneous and unsupported contention that the improved ERRFs for Plan 2 members were replacements for gain-sharing. Members of Plan 2 never had gain-sharing and will not get it even if this Court affirms the trial court’s restoration of gain-sharing. Under no definition of “replacement” are the ERRFs a replacement benefit for members of Plan 2. The improved ERRFs are a new contractual benefit for Plan 2 members and must be analyzed as such.

Plan 2 employees receive no comparable “replacement benefit” for the loss of the improved ERRFs. Plan 3 members who also lost the ERRFs will receive gain-sharing if this Court affirms the trial court’s decision in Phase 1 and for that reason are not a party to this cross-appeal. However, the State is attempting to divest Plan 2 members of the improved ERRFs and give them nothing in return. Plaintiffs are not attempting to “cherry pick” the best benefits from various statutory provisions which this court disapproved of in *McAllister v. City of Bellevue Firemen’s Pension Board*, 166 Wn.2d 623, 632, 210 P.3d 1002 (2009) and *Vallet v. City of Seattle*, 77 Wn.2d 12, 21, 459 P.2d 407 (1969). If the State prevails in Phase 2 and the automatic repeal provision is implemented, Plan 2 employees will not receive the improved ERRFs or a substitute benefit from their years of service or contributions.¹⁴

The concept of a “replacement package” referenced by the State (State’s Cross- Resp., at 49) has no support in case law. Our court has consistently recognized the various retirement system plans as separate plans. In both *County Officials*, 89 Wn.2d at 732 and *Wash. Fed. State Employees*, 98 Wn.2d, at 677, the court specifically noted that the legislature had created a new plan (Plan 2) to provide different (reduced) benefits

¹⁴ Plaintiffs did not further pursue Plan 3 members claim for continuation of the improved ERRFs since they will receive the benefit of gain-sharing reinstatement.

for new employees. The State must not be permitted to now lump all the plans together for the purpose of offsetting benefits from one plan to another. Such a practice ignores the critical expectations of the various plan members to the benefits of “their” plan, the one for which they have worked. That has been the guiding principle in the Washington court’s analysis of pension benefits.

In *Bakenhus*, the court held that a corresponding benefit must be provided to the employee whose benefit was eliminated or modified. *Bakenhus*, 48 Wn.2d, at 702-703. Giving effect to the automatic repeal provision does not comply with *Bakenhus* because Plan 2 employees who will lose the improved ERRFs will receive absolutely no benefit to replace the lost benefit.

Additionally, the State cannot show that repeal of the improved ERRFs is necessary to maintain either the flexibility or the financial integrity of the pension system. The State gave short shift to Plaintiffs’ claims that the State could not meet the flexibility and integrity prongs of the *Bakenhus* analysis. (State’s Cross-Resp., at 49). Its argument that because the State could not afford gain-sharing, it cannot afford the improved ERRFs is disingenuous and lacking in factual support. The record is clear, based on the admission of the State Actuary there was no fiscal

need to repeal gain-sharing.¹⁵ The financial health of all Plans 2 did not support the need for the automatic provision for the ERRFs in 2007 and does not do so today.¹⁶

III. CONCLUSION

Giving effect to the provisions automatically repealing the improved ERRFs would result in an unconstitutional impairment of Plan 2 employees' pension contracts.

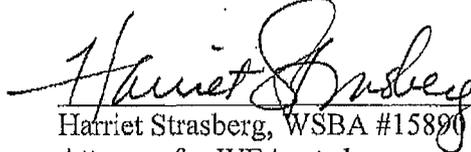
RESPECTUFLY SUBMITTED this 31st day of May, 2013.

YOUNGLOVE & COKER, PLLC



Edward Earl Younglove III, WSBA #5873
Attorney for WFSE, et al.

LAW OFFICE OF HARRIET STRASBERG



Harriet Strasberg, WSBA #15890
Attorney for WEA, et al.

LAW OFFICE OF DON CLOCKSIN



Don Clocksin, WSBA #4370
Attorney for WEA, et al.

¹⁵ CP 1767 (Smith Dep.166:16-167:14). See also Respondent's Brief, at 15-16, 35.

¹⁶ Cross-Appellants' Opening Brief, § III B.4, at 63, showing the health of Plans 2/3 with the new ERRFs.

DECLARATION OF SERVICE

I certify that on the date below I served a true and correct copy of the Cross-Appellants' Reply to which this Declaration of Service is attached by email and U.S. mail, postage prepaid to:

Anne Hall
Spencer Daniels
Sarah Blocki
Office of the Attorney General
7141 Cleanwater Drive SW
PO Box 40108
Olympia, WA 98504-0108
anneh@atg.wa.gov
spencerd@atg.wa.gov
sarahb@atg.wa.gov

Noah Guzzo Purcell
Solicitor General
PO Box 40100
Olympia, WA 98504-0100
npurcell@perkinscoie.com

James D. Oswald
Schwerin Campbell Barnard
Iglitzin & Lavitt, LLP
18 West Mercer Street, Suite 400
Seattle, WA 98119-3971
oswald@workerlaw.com

Steven B. Frank
Frank Freed Subit & Thomas, LLP
705 - 2nd Avenue, Suite 1200
Seattle, WA 98104
sfrank@frankfreed.com

I declare under penalty of perjury under the laws of the state of Washington that the foregoing is true and correct.

DATED this 31st day of May, 2013 at Olympia, WA.



Leah Pagel, Legal Assistant
Younglove & Coker, P.L.L.C.

OFFICE RECEPTIONIST, CLERK

To: Leah Pagel
Cc: anneh@atg.wa.gov; spencerd@atg.wa.gov; sarahb@atg.wa.gov; npurcell@perkinscoie.com; James D. Oswald; Steve Frank; Harriet Strasberg; Don Clocksin (clocksinlaw@qwestoffice.net); Ed Younglove; WFSE/Anita Hunter (AnitaH@wfse.org)
Subject: RE: WEA, et al. v. DRS, Supreme Court No. 87424-7

Rec'd 5-31-13

Please note that any pleading filed as an attachment to e-mail will be treated as the original. Therefore, if a filing is by e-mail attachment, it is not necessary to mail to the court the original of the document.

From: Leah Pagel [<mailto:Leah@ylclaw.com>]
Sent: Friday, May 31, 2013 11:04 AM
To: OFFICE RECEPTIONIST, CLERK
Cc: anneh@atg.wa.gov; spencerd@atg.wa.gov; sarahb@atg.wa.gov; npurcell@perkinscoie.com; James D. Oswald; Steve Frank; Harriet Strasberg; Don Clocksin (clocksinlaw@qwestoffice.net); Ed Younglove; WFSE/Anita Hunter (AnitaH@wfse.org)
Subject: WEA, et al. v. DRS, Supreme Court No. 87424-7

Dear Supreme Court Clerk:

Attached for filing is the Cross-Appellants' Reply in the above matter.

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

Leah Pagel, Legal Assistant
YOUNGLOVE & COKER, PLLC
1800 Cooper Point Road SW, Bldg. 16
PO Box 7846
Olympia, WA 98507-7846
leah@ylclaw.com
360.357.7791 Ext. 101
360.754.9268 (fax)

CONFIDENTIALITY NOTICE: *The information contained in this ELECTRONIC MAIL transmission is confidential. It may also be subject to the attorney-client privilege or be privileged work product or proprietary information. This information is intended for the exclusive use of the addressee(s). If you are not the intended recipient, you are hereby notified that any use, disclosure, dissemination, distribution (other than to the addressee(s)), copying or taking of any action because of this information is strictly prohibited.*