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State Capitol, Room 115
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Mr. Michael Nehf
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RE: Request for advice regarding proposed Employees' Retirement System changes

Dear Ms. Osborn and Mr. Nehf:

This letter is in response to your request for advice regarding proposed changes to the Employees' Retirement System of Georgia ("ERS"). You have asked whether ERS or the General Assembly may legally increase the employee contribution levels for current members; implement a lower cost-of-living adjustment ("COLA") for current retirees than ERS has previously implemented or decline to implement a COLA; and/or lower the percentage multiplier for the calculation of "new plan" retirees' benefits.

As explained herein, it is my advice that: (1) ERS has existing statutory authority to adopt a method for awarding COLA's that increases the employee contribution rate up to a total of an additional ¼ % in order to fund COLA's for those who retire after the adoption of such a new method, but courts would likely disfavor any further mandatory increase for existing members in the employee contribution rates set by law for COLA's or annuities. Under existing case law, if a statutory increase is accompanied by comparable new advantages in exchange, ERS could be authorized by the General Assembly to further raise employee contribution rates for members who voluntarily agree to participate in exchange for new advantageous provisions. A unilateral, involuntary increase, however, even with comparable new advantages would require very strong justification and even then would require Georgia courts to change their long-standing interpretation of the constitutional prohibition against impairment of contracts in public pension cases; (2)

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Consistent with long-standing administrative interpretation and practice and advice, ERS has statutory discretion to determine whether to award a COLA and its amount, but any such award must be consistent with the statutory authority, with the method adopted under the statute, and with the actuarial soundness of the system; and (3) ERS cannot, under existing law, lower the benefits to be paid to "new plan" retirees by reducing the percentage multiplier for benefit calculations.

Mr. Nehf has informed me that ERS is currently considering these potential changes to the system in light of calculations by ERS's actuary indicating that, although the system's unfunded liabilities are relatively low for the short term, those unfunded liabilities could increase dramatically over the long term if the system's revenue and expenditure projections remain unchanged.

I will address each of the proposed changes in turn following a brief discussion of the history of ERS employee contribution rates and COLA's and the legal context in which these issues arise.

History of ERS employee contributions and COLA's [1]

The ERS was created by an act of the General Assembly in 1949. *See* 1949 Ga. Laws 138. Members were originally required to contribute 5% of their earnable compensation to the system. The employees' contributions were to be "credited by the Board to the individual accounts in the annuity savings fund of the member from whose compensation the deductions were made." 1949 Ga. Laws 138, § 7.[2] In return, the members were entitled to receive upon retirement an annuity that would be "the actuarial equivalent of [their] accumulated contributions at the time of [their] retirement" and a pension that would be "equal to the annuity allowable at the age of retirement, but not to exceed" that to which they would have been entitled at the age of 65. 1949 Ga. Laws 138, § 5.[3] Retirees were also entitled to choose from other optional retirement allowances. 1949 Ga. Laws 138, § 5.[4] The original ERS Act did not provide for the possibility of COLA's for retirees.

In 1967, the General Assembly added a provision for retiree COLA's. 1967 Ga. Laws 751, § 3.[5] The amendment authorized the ERS Board of Trustees "to adopt a method for providing for postretirement benefit adjustments for the purpose of maintaining essentially no less purchasing power for a beneficiary in his postretirement years." It

[1] I include this chronology of the evolution of the ERS plan in order to provide context for my analysis of the changes that are currently being contemplated.
[2] The current version of this provision is now codified at O.C.G.A. § 47-2-51.
[3] The current version of this provision is now codified at O.C.G.A. § 47-2-120.
[4] The current version of this provision is now codified at O.C.G.A. § 47-2-121.
[5] The current version of this provision is now codified at O.C.G.A. § 47-2-29.

further provided that a method for providing COLA's would be based upon a recommendation from the Board's actuary; the actuarial soundness of the system; its application to the income of those retiring on or after the date of the adoption of a method for COLA's; and "[a]ny additional contribution by the member to be in an amount not to exceed one-fourth of one percent of his monthly earnable compensation." The 1967 amendment originally provided that any such plan for COLA's adopted by the Board would require the prior approval of the General Assembly, but that requirement was removed the next year. 1967 Ga. Laws 751, § 3; 1968 Ga. Laws 1356, § 3.

Following the 1967 amendment to the ERS statutes, the ERS Board of Trustees directed its actuary to study the problem of erosion of post-retirement benefits and make proposals to remedy the problem. According to excerpts of Board meeting minutes provided by ERS staff, in November 1968, the Board adopted "Guidelines for Implementing the Post-Retirement Adjustment of Benefits," which were "designed to provide [the Board and the Executive Secretary] with the necessary operating procedures for implementing the post-retirement adjustment of benefits." These guidelines provided that a COLA "will be granted two times a year on January 1 and July 1 to be determined" by the calculation of a ratio between the current Consumer Price Index ("CPI") average and a base index. The COLA was not to exceed 1½ % every six months, and if the retiree's calculated ratio resulted in a number less than 1.000, the retiree's COLA could be reduced. It appears that the first COLA's were paid in January 1969.[6]

In 1980, the General Assembly amended the ERS Act to require the members' employers to pay the employees' 5% contribution for them but then required the members themselves to contribute an additional ½ % of their earnable compensation. 1980 Ga. Laws 925, § 3.[7] Although this change technically raised the employee contribution rate from 5% to 5½ %, as a practical matter it actually reduced the rate members paid out of their pockets from 5% to ½ %. "The 1980 Act was enacted, in part, to provide state employees with increases in disposable income through the employer's payment of most of the employee contributions to the ERS." 1980 Op. Att'y Gen. 80-91, p. 192.

It became necessary shortly thereafter to make further refinements in the system. After finding that "an adjustment in the compensation of state employees is necessary to assure the future actuarial soundness of the [ERS], and to protect the fiscal integrity of the [ERS] so as to insure the future payment of retirement benefits and allowances to those entitled to same," in 1982 the legislature increased the employee contribution for those members hired before July 1, 1982 by an additional 1% of their earnable compensation.

[6] The 1968 guidelines also provided for Supplemental Adjustments to be based on "the excess yield earned by the Trust Fund." It appears that the first Supplemental Adjustments were paid in January 1970 but were discontinued after January 1981.
[7] The current version of this provision is now codified at O.C.G.A. § 47-2-54(b).

1982 Ga. Laws 1163, § 3.[8] This change brought the employees' total contribution rate to 6½ %, though employers continued to pay 5% of the employees' contribution for them. *See* O.C.G.A. §§ 47-2-51(a)(1), 47-2-54(b), 47-2-54(i). In addition, concurrently with the statutory increase in the rate of member contributions, the General Assembly awarded a general salary increase for Fiscal Year 1983, which appears to approximate or exceed the amount of the increase in required contributions, although that would be a matter of proof and further investigation. 1982 Ga. Laws 1876, 2069.

In the same legislation that increased member contributions, the General Assembly also created a "new plan" for ERS members hired on or after July 1, 1982. (Members hired before that date accordingly became known as members of the "old plan," which became a "closed system." "Old plan" members were also given the option to join the "new plan." O.C.G.A. § 47-2-334(e).) "New plan" members were required to contribute ½ % of their earnable compensation to the system, and those contributions were to be "credited to the individual accounts of the members in the annuity savings fund." 1982 Ga. Laws 1163, § 2.[9] In return, they were entitled to receive an annuity "which shall be the actuarial equivalent of the member's accumulated contributions at the time of retirement" and an annual pension "which, together with the annuity, shall provide a total retirement allowance equal to 1.5 percent of the member's average final compensation over the eight consecutive calendar quarters of creditable service producing the highest such average, multiplied by the number of years of creditable service." 1982 Ga. Laws 1163, § 2.[10]

In its Supplemental Appropriations Act for Fiscal Year 1983-84 and its General Appropriations Act for Fiscal Year 1984-85, the General Assembly included language indicating its intent to limit COLA's for ERS (and TRS) retirees to $25 per month. The Attorney General opined, however, that "the General Assembly cannot, solely through language in an Appropriations Act, place a ceiling or limit on the amount of a cost-of-living increase granted to a retiree of the ERS or TRS. . . ." 1984 Op. Att'y Gen. 84-19, p. 42-43. The Attorney General explained:

> . . . With respect to both retirement systems, cost-of-living increases (postretirement benefit adjustments) can be granted by the respective boards of trustees based upon actuarial recommendations and the primary concern of

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[8] The current version of this provision is now codified at O.C.G.A. § 47-2-54(i).
[9] *See* note 12 *infra* (explaining that ¼ % goes to the annuity and ¼ % to group term life insurance).
[10] The current version of this provision is now codified at O.C.G.A. § 47-2-334.

> maintenance of the actuarial soundness of the systems. See O.C.G.A. § 47-2-29 (ERS) and O.C.G.A. § 47-3-126 (TRS). Neither the ERS Act nor the TRS Act sets any ceiling or limit on the amount or percentage of granted cost-of-living increases. In both cases, the decision as to the amount or the percentage is left to the discretion of the governing board of trustees based on the actuary's recommendation and subject to the fundamental concern for the maintenance of the actuarial soundness of the system. . . . [A]ppropriations Acts cannot constitutionally alter a discretionary authority for the expenditure of that money which the General Assembly has granted an agency by general law.

Id. at p. 43-44.

In 1987, pursuant to a legislative requirement, ERS published its COLA methodology with the Secretary of State. It provided that "[e]ach January 1 and July 1, a [COLA] will be granted to each beneficiary who has attained age 45 and has been retired at least seven months" based on the CPI, up to a maximum of 1½ %. The rule then expressly provided: "Any such increase in benefit shall become effective only if the necessary appropriations/funds are available to maintain the actuarial soundness of the System."[11]

In 1990, the legislature increased the employee contribution rate for members of the "new plan" to 1½ % of their earnable compensation. 1990 Ga. Laws 532, § 1. At the same time, the legislature also increased the ceiling on the multiplier used to calculate "new plan" pensions such that "together with the annuity" the "new plan" would:

> provide a total retirement allowance equal to more than 1.5 percent, but not greater than 2 percent, the actual percent to be set by the board of trustees in direct relation to the amount of increased appropriations provided by the General Assembly to fund the provisions of this paragraph, of the member's average monthly compensation over the eight consecutive calendar quarters of creditable service producing the highest such average, multiplied by the number of years of creditable service.

1990 Ga. Laws 1163, § 1.

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[11] The current version of this rule can be found at Ga. Comp. R. & Regs. r. 513-1-1-.05.

In 1992, ERS amended its officially promulgated COLA rule by eliminating reference to the CPI and providing that COLA's "may be granted" in an amount not to exceed 1½ % "and shall apply to the current retirement allowance not in excess of the Social Security wage base as established for that calendar year." The amended rule continued to provide that "[a]ny increase in benefit shall become effective only if the necessary appropriations/ funds are available to maintain the actuarial soundness of the System."

In 1993, the legislature enacted O.C.G.A. § 47-1-31, which provides:

> Any other provision of this title to the contrary notwithstanding, any discretionary postretirement benefit increase granted on or after July 1, 1993, by the board of trustees of any public retirement system pursuant to the authority to grant such increases within the limits of actuarial soundness granted by general law shall be subject to reduction by subsequent legislation and shall not be considered an element of any contract of employment.

Finally, in 2002, the General Assembly lowered the floor for the employee contribution rate for "new plan" members to "an amount not less than 1 percent nor greater than 1½ % of earnable compensation. . . ." 2002 Ga. Laws 1288, § 2.

Today, therefore, the employee contribution rate for "old plan" members stands at 6½ % (with 5% actually being paid by their employers for them). O.C.G.A. §§ 47-2-51(a)(1), 47-2-54(b), 47-2-54(i).[12] An "old plan" member is entitled to an annuity that would be "the actuarial equivalent of his accumulated contributions at the time of his retirement" and a pension that would be "equal to the annuity allowable at the age of retirement, but not to exceed" that to which he would have been entitled at the age of 65. O.C.G.A. § 47-2-120(a). The employee contribution rate for "new plan" members, on the other hand, is now set by the ERS Board of Trustees at 1½ %, which is at the top of the statutorily allowed range of 1% to 1½ %. ERS Explanation of Benefits 2007, p. 3; O.C.G.A. § 47-2-334(c).[13] "New plan" members are entitled to an annuity "which shall

[12] "Of the one-half of 1 percent deducted from the earnable compensation of members, one-quarter of 1 percent shall be credited to each member's account in the annuity savings fund, and the remaining one-quarter of 1 percent shall be credited to the group term life insurance fund in lieu of the deduction required under Code Section 47-2-128." O.C.G.A. § 47-2-54(c). If a member is not participating in GTLI, the contribution is entirely credited to the annuity fund. *Id.*

[13] "Of the percentage deducted from the earnable compensation of members, one-fourth of 1 percent shall be credited to the group term life insurance fund in lieu of any other deduction therefor and the remaining portion shall be credited to the individual accounts of the members in the annuity savings fund." O.C.G.A. § 47-2-334(c).

be the actuarial equivalent of the member's accumulated contribution at the time of retirement" and an annual pension that, together with the annuity, provide a total retirement allowance equal to 2% "of the member's average monthly compensation over the eight consecutive calendar quarters of creditable service producing the highest such average, multiplied by the number of years of creditable service" – a percentage set by the ERS Board of Trustees at the top of the statutorily allowed range of 1½% to 2%. ERS Explanation of Benefits 2007, p. 15; O.C.G.A. § 47-2-334(b). Members of both plans may also choose other optional retirement allowances. *See* O.C.G.A. § 47-2-121. In addition, the ERS Board of Trustees has generally granted COLA's to retirees twice per year, most often in the amount of 1½ % semi-annually, but on occasion either less or more.

The information presented to me by ERS also indicates that the rate for employer contributions provided to the system by the state has declined from a high of approximately 18% of employees' compensation in 1990 to a current level of approximately 10%.

<u>Legal context of ERS employee contribution and COLA issues</u>

The United States Constitution prohibits states from passing any "Law impairing the Obligation of Contracts." U.S. CONST. art. I, § 10. The Georgia Constitution similarly prohibits "laws impairing the obligation of contract." GA. CONST. of 1983, art. I, § I, ¶ X.

Applying both the state and federal constitutional prohibition on impairment of contractual obligations in the context of public pensions, the appellate courts in Georgia have consistently held that:

> . . . a statute or ordinance establishing a retirement plan for government employees becomes a part of an employee's contract of employment if the employee contributes at any time any amount toward the benefits he is to receive, and if the employee performs services while the law is in effect; and that the impairment clause of our constitution . . . precludes the application of an amendatory statute or ordinance in the calculation of the employee's retirement benefits if the effect of the amendment is to reduce rather than increase the benefits payable. It is not necessary for an application of this rule that the rights of the employee shall have become vested under the terms of the retirement plan while the amendment is in effect. Rather, if the employee performs services during the effective dates of the legislation, the benefits are constitutionally vested,

> precluding their legislative repeal as to the employee, regardless of whether or not the employee would be able to retire on any basis under the plan.

Withers v. Register, 246 Ga. 158, 159 (1980) (citing *Burks v. Bd. of Trustees of the Fireman's Pension Fund*, 214 Ga. 251 (1958); *Bender v. Anglin*, 207 Ga. 108 (1950); and *Trotzier v. McElroy*, 182 Ga. 719 (1936)). *See also Alverson v. Employees' Retirement Sys.*, 272 Ga. App. 389, 391-92 (2005); *Malcom v. Newton County*, 244 Ga. App. 464, 467-68 (2000); *Parrish v. Employees' Retirement Sys.*, 260 Ga. 613, 613 (1990); *Swann v. Bd. of Trustees of Joint Municipal Employees' Benefit Sys.*, 257 Ga. 450, 454 (1987); *City of Athens v. McGahee*, 178 Ga. App. 76, 77-78 (1986); and *Webb v. Whitley*, 114 Ga. App. 153, 156-57 (1966) (holding the same).

The Georgia Supreme Court's decision in *Bender v. Anglin*, 207 Ga. 108 (1950), serves as a simple illustration of this doctrine. The plaintiff in that case had been a firefighter employed by the City of Atlanta. At the time of his employment in 1915, the rules of the Firemen's Pension Fund of the City of Atlanta required him to pay a percentage of his monthly salary into the fund and, in return, entitled him to retire after 25 years of service and receive thereafter a monthly pension of $100 for the rest of his life. In 1935, however, the rules were amended to lower the monthly pension payment amount to $75 per month. When he retired in 1942 and was only paid $75 per month, he sued, seeking the $100 monthly payments that the rules had provided for when he began his employment with the city. The Supreme Court ruled in his favor, holding that a binding contract was formed between the firefighter and the city when he began working and contributing to the fund in 1915 and that the terms of that contract were dictated by the fund's rules as of the beginning date of his employment. As a result, the city's attempt to lower the monthly pension payments unconstitutionally changed the terms of – and impaired the obligations of – the contract.

The Georgia Supreme Court has more than once rejected arguments that economic duress justified an impairment of the compensation agreement with public employees. In a series of pension cases going back to the Depression era, the City of Atlanta unsuccessfully argued that the General Assembly was free under its general police power to change pension policy because of the state of the economy, saying: "If the legislature has imposed impossible burdens upon [Atlanta] which can not be supported by the taxpayers, due to changed economic conditions, the legislature can remove those burdens by subsequent legislation." *Trotzier v. McElroy*, 182 Ga. 719, 722 (1936); *see also Atlanta v. Anglin*, 209 Ga. 170, 172 (1952); *Bender v. Anglin*, 207 Ga. 108, 110 (1950); *West v. Trotzier*, 185 Ga. 794, 798 (1938). More recently, the Board of Regents of the University System made such an argument in the case of *Busbee v. Ga. Conference, American Assoc. of Univ. Professors*, 235 Ga. 752 (1975). There, after the general appropriations act had become law, the Board of Regents entered into individual contracts with its faculty members, awarding them raises. After the contracts had been

executed, however, the legislature held a special session and reduced appropriations for the coming year. Upon receiving lower appropriations than it had expected, the Board of Regents rescinded the raises awarded in its faculty contracts. A group of professors brought suit seeking to enforce the salary provisions of their contracts, and the Supreme Court ruled in their favor, holding that the Board of Regents' rescission of the professors' raises was an unconstitutional impairment of contract.

In support of its argument that the impairment was permissible due to the budget shortfall, the Board of Regents cited to a 1934 United States Supreme Court decision, *Home Bldg. & Loan Assoc. v. Blaisdell*, 290 U.S. 398 (1934), in which that Court approved a Minnesota law that, in light of the economic emergency of the 1930s, temporarily extended the time allowed for redeeming property from foreclosure and sale under existing mortgages. The state Supreme Court noted that it had previously declined to apply the *Blaisdell* holding in Georgia (principally because a similar Georgia law was not temporary in nature) and explained: "Again we decline to apply *Blaisdell* for the additional reason that no showing of economic necessity comparable to the depression of the 1930s has been made." The Court further explained: "When the General Assembly met in special session it had decisions to make. Those choices undoubtedly were extremely difficult. However, it has not been shown that the General Assembly had no choice but to depropriate sums already committed by contracts." *Busbee*, 235 Ga. at 763.

The Georgia Supreme Court did not reject the legal rationale upon which the United States Supreme Court decided *Blaisdell* under the federal constitution. In *Blaisdell*, the Court found a "necessary residuum of state power" which qualifies the prohibition against impairment in that situation. Two years after the Georgia Supreme Court decided the *Busbee* case and found insufficient justification in that situation for exercising such a residual state power, however, the United States Supreme Court issued its opinion in *United States Trust Co. v. New Jersey*, 431 U.S. 1 (1977), which has come to be seen as making clear that *Blaisdell* was not intended to interpret away the impairment prohibition. More importantly for present purposes, the impairment at issue was an impairment of a contract made by the State itself. The Court explained that "an impairment may be constitutional if it is reasonable and necessary to serve an important public purpose" and some judicial deference to legislative policy decisions is warranted. The Court cautioned, however, that in regard to state contracts "complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State's self-interest is at stake" and that if "a State could reduce its financial obligations whenever it wanted to spend the money for what it regarded as an important public purpose, the Contract Clause would provide no protection at all." *Id.* at 25-26.

Since the *United States Trust Co.* decision, courts evaluating challenges to laws under the federal impairment clause have developed an analytical framework that includes the following steps in analysis "(1) whether the law substantially impairs a contractual relationship; (2) whether there is a significant and legitimate public purpose for the law;

and (3) whether the adjustments of rights and responsibilities of the contracting parties are based upon reasonable conditions and are of an appropriate nature." *Vesta Fire Ins. Corp. v. Florida*, 141 F.3d 1427, 1433 (11th Cir. 1998) (citing *Energy Resources Group, Inc. v. Kansas Power & Light Co.*, 459 U.S. 400 410-13 (1983)).

The courts of a number of other states utilize a similar "comparative advantage" analysis when evaluating changes to their public pension systems. As described by the California Supreme Court, that approach allows modifications to vested contractual pension rights "to permit adjustments in accord with changing conditions and at the same time maintain the integrity of the system." *Betts v. Bd. of Admin., Public Employees Retirement Sys.*, 582 P.2d 614, 617 (Cal. 1978). To be approved, such alterations must be reasonable and "must bear some material relation to the theory of a pension system and its successful operation, and changes in a pension plan which result in disadvantage to employees should be accompanied by comparable new advantages." *Id.* "The comparative analysis of disadvantages and compensating advantages must focus on the particular employee whose own vested pension rights are involved." *Id.*

"Comparative advantage" analysis is not universally followed, and even when it is, it has been difficult to persuade courts to accept unilateral changes in pension systems. There is in fact a great variation in approaches to retirement cases in the courts of other states. It can be said conclusively, however, that it is now a near universal rule that increasing a member contribution rate without more is an unconstitutional impairment of contract. *See, e.g., Singer v. Topeka*, 607 P.2d 467, 476-77 (Kan. 1980); *Brazelton v. Kansas Public Employees Retirement Sys.*, 607 P.2d 510, 516 (Kan. 1980); *Collar Workers v. Wills*, 232 Cal. Rptr. 164 (Cal. App. 1986); *Ass'n of State Colleges & Univ. Faculties v. State Sys. of Higher Educ.*, 479 A.2d 962, 966 (Pa. 1984). Further, whatever the federal standard and that of some other states, any changes to the ERS plan would have to survive scrutiny under the Georgia Constitution as interpreted by the Georgia Supreme Court. *See, e.g., Pope v. City of Atlanta*, 240 Ga. 177, 178 (1977) (explaining that "[q]uestions of the construction of the State Constitution are strictly matters for the highest court of this state" and that "construction of similar federal constitutional provisions, though persuasive authority, is not binding on this state's construction of its own Constitution").

To this point, Georgia courts have generally only allowed public pension systems to unilaterally change the terms of a retirement plan if the governing statute has reserved the power to make changes. In such a situation, the potential for changes has been made a part of the terms of the contract from its inception. For example, in the case of *Pulliam v. Ga. Firemen's Pension Fund*, 262 Ga. 411 (1992), a retired firefighter challenged the termination of his disability benefits after he was found to be engaged in gainful employment. Because this termination was based on an amendment to the Georgia Firemen's Pension Fund that was enacted after he began his employment (and apparently even after he had retired), he claimed it to be an unconstitutional impairment of his

contractual rights. The Supreme Court disagreed because the statute contained the following provision at the time the firefighter began his employment: "Benefits under this chapter shall be subject to future legislative change and revision and no member of this fund or any other person shall be deemed to have any vested right to any benefits. . . ." *Id.* at 411 (quoting O.C.G.A. § 47-7-121). The Court further explained:

> . . . The basis for the constitutional vesting of rights in pensions is that the pension rights are property and cannot be taken. However, they are property because they become part of the contract of employment, and as this court pointed out in *Pritchard* [*v. Board of Comm'rs of Peace Officers Annuity & Benefit Fund*, 211 Ga. 57 (1954)], the provision for subsequent amendment was part of the contract when [the plaintiff] entered into it. . . .

Id. at 413.

The Georgia courts have also indicated that changes to a public pension system may be binding on a member or retiree if the individual member or retiree voluntarily consents to the changes and the changes include new advantages for the member or retiree. For instance, in *Webb v. Whitley*, 114 Ga. App. 153 (1966), the widow of a retired firefighter challenged the amount of the monthly pension payment she received after her husband died because it was calculated under the terms of an amendment to his firefighter's pension plan that was enacted after he began his employment. The Georgia Court of Appeals, however, denied her claim and held that she was only entitled to the pension payment dictated by the amended terms of the plan. Her husband began his employment prior to the 1925 enactment of a pension plan that promised him, upon his retirement, a monthly benefit equal to 50% of his monthly salary and promised to his wife, upon his death, the same monthly benefit. In 1945, the plan was amended such that it would increase his monthly benefit to 55% of his monthly salary upon his retirement but decrease his wife's monthly benefit upon his death to 75% of the amount of his monthly retirement benefit. Later in 1945, he signed a statement that read, in pertinent part: "I hereby authorize City Comptroller to make deductions from my salary in order that I may participate in the 1924 Pension Act as amended. . . ." The Court of Appeals held:

> The fireman, however, by execution and delivery of a written statement by which he authorizes deductions from his wages for the express purpose of participating in the pension benefits provided by the statute as amended, irrevocably consents to the law as changed by amendment and surrenders any right to claim benefits as originally provided by the pension law, where in return for his

> consent he receives consideration by way of additional benefits and changed contributions.

Webb, 114 Ga. App. at 157 (citing *Hartsfield v. Mitchell*, 210 Ga. 197 (1953)). Because both parties expressly agreed to changes to the terms of their contract and both parties received a benefit from the revised agreement (the firefighter got a benefit set at 55% of his salary rather than 50%, and the city only had to pay his widow 75% of his retirement benefit rather than 100%), the Court found it to be a binding revision to the agreement.

Thus, under the existing Georgia case law, the terms of a public retirement system form a binding contract between the retirement system and its members and retirees, and a unilateral change of those terms by the system to the detriment of its members or retirees is generally barred by the constitutional prohibition on impairment of the obligations of contracts. The terms of that contract are set when the member/employee begins work and gives the consideration required by law for participation.[14] A public retirement system generally may only change the terms of the contract to the detriment of its members or retirees if the governing statute specifically allows for such changes or, perhaps, where the individual member or retiree voluntarily consents to changes that also include a new benefit for him or her.[15]

1. <u>May ERS increase the employee contribution levels for current members?</u>

It is my advice that under the terms of the statutory contract already in place, ERS may raise the employee contribution rate up to a total of an additional ¼ % of members' earnable compensation for the specific purpose of funding (or helping to fund) the cost of COLA's for future retirees. Section 47-2-29(a), which has been in place since 1967, authorizes the ERS Board to adopt a method for awarding retiree COLA's based upon, in addition to actuarial considerations, "[i]ts application to the retirement income of members retiring on or after the adoption of such method by the board of trustees" and "[a]ny additional contribution by the member in an amount not to exceed one-fourth of 1 percent of his monthly earnable compensation." O.C.G.A. § 47-2-29(a)(3) and (4). ERS has never adopted a method for implementing COLA's that includes a ¼ % increase in member contributions, but ERS is still authorized to do so under § 47-2-29(a). A

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[14] For example, a particular retirement plan may only require some period of employment and not a contribution. *See, e.g., Malcolm v. Newton County*, 244 Ga. App. 464, 467 (2000).

[15] On the other hand, a retirement system is generally free to increase benefits and/or decrease the costs for its members after their employment begins as the member's continued service will constitute sufficient consideration in exchange for the increased benefits or decreased costs. *See, e.g., City of Atlanta v. Anglin*, 209 Ga. 170, 174-75 (1952).

decision to do so should be based on a recommendation of ERS's actuary and/or a specific finding that doing so would help to maintain the actuarial soundness of the system. *See* O.C.G.A. § 47-2-29(a)(1) and (2).[16]

In doing so, ERS must follow the terms of both § 47-2-29(a)(3), which indicates the COLA method is to apply only to those who retire after its effective date, and O.C.G.A. § 47-20-10(g), which mandates that "[i]n no event will employee contributions of active members of a retirement system be used to pay benefits to beneficiaries under the retirement system." Under these two provisions, if ERS adopts a new method for COLA implementation that includes an additional ¼ % employee contribution, the funds raised from the additional contributions could only be used to defray the costs of COLA's awarded to future retirees who are members at the time or after that method is adopted.

Based on the consistent holdings of the Georgia appellate courts described above, however, it is also my advice that ERS may not (nor could the General Assembly) otherwise raise the employee contribution rates for current members beyond the ¼ % provided for in § 47-2-29(a). The contribution levels are part of the terms of the contract between ERS and its members, and otherwise raising them without express statutory authority would unconstitutionally change the terms of – and impair the obligations of – the contract. This is true for member contribution rates generally. Thus, although the terms of the "new plan" allow ERS to change the employee contribution rate toward member annuities within a certain range (between 1% and 1½ %), the rate is already set at the upper limit of that range.

I have not found any indication that the Georgia courts have ruled on this issue specifically in the context of raising contributions (as opposed to reducing benefits), but I believe that the courts would likely analyze a general increase in contributions in the same manner in which they have consistently analyzed decreases in benefits, as have other states. While the two procedurally differ in that one raises the amount a member pays on the front end and the other lowers the amount a retiree receives on the back end, I

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[16] It is my advice that the rate could only be raised a total of an additional ¼ %, not that ERS could raise the rate another ¼ % every time it approves a new COLA. Although the language of § 47-2-29 is not perfectly clear, ¼ % appears to be a cap on how much ERS can raise the employee contribution rate to help effectuate COLA's for retirees. I believe that a reasonable reading of the ERS statutes as a whole leads to this conclusion. The statutes carefully set out a precise system of calculations involving a specific range of employee contributions, formula for employer contributions, and formula for retiree benefits, in addition to an allowance for necessary COLA's to prevent a decrease in retirees' purchasing power. It would not seem to fit with this precisely laid out system for ERS to be able to raise the employee contribution rate apparently limitlessly as long as it did so in ¼ % increments.

believe that the courts would find the net effect to be the same – a change in the terms of the pension contract to the disadvantage of the employee.

While Georgia courts could be receptive to arguments made successfully in other states, it must be remembered that the state Supreme Court has already rejected economic arguments in *Busbee* and the Atlanta pension cases. Indeed, the Court in *Busbee* declined the Board of Regents' budget shortfall argument in part because, while the legislature undoubtedly faced difficult decisions, "it ha[d] not been shown that the General Assembly had no choice but to depropriate sums already committed by contracts." *Id.* at 763. In order to succeed on a similar argument, therefore, ERS would have to show that it – and/or the legislature – has no alternative option that would not involve changing the terms of its contractual obligations to its members.[17] In the alternative, ERS would have to persuade the Georgia courts to adopt the "comparative advantage" rule used by some other states and then show that a proposed change would meet that standard.

It is my further advice, though, that ERS may be able to further raise the employee contribution rate <u>if</u> it correspondingly provides new advantages for its current members/future retirees <u>and</u> agreement to such changes is strictly voluntary for individual members. As explained above, the Georgia appellate courts have not ruled on this issue in very direct language, but their holdings imply that a public pension system and a public employee/member may agree to binding changes to the pension plan if the consent is truly voluntary and the employee/member gains a new advantage he or she did not have before. *See, e.g., Webb v. Whitley*, 114 Ga. App. 153 (1966). Therefore, it appears that ERS, via statutory amendments by the General Assembly, could create a voluntary revised plan for current members that would raise their employee contribution rate and provide some other comparable new benefit to the members who chose to participate.

Two points bear repeated emphasis here. First, the case law is not entirely clear as to whether courts would approve such a plan against a constitutional impairment of contractual obligation challenge. Past holdings imply, though, that such a plan could be approved by the courts. Second, to be bound, individual members would have to specifically opt to be included in this new voluntary plan and would need to individually sign consent forms indicating, at the least, their voluntary consent, their understanding that they are free to decline and remain covered by the current terms of the system, and their understanding of the changes.

It is, therefore, my advice that ERS may increase the employee contribution rate up to a total of an additional ¼ % in order to fund COLA's for those who retire after the adoption of such a new method but without more courts would likely disfavor any mandatory

[17] Such a showing may be difficult, among other reasons, in light of the fact that ERS has lowered employers' contributions from approximately 18% of employees' compensation to approximately 10% since 1990.

increase in the employee contribution rate beyond that for any purpose. ERS may, however, be able to further raise employee contribution rates for members who voluntarily agree to participate in exchange for new advantageous provisions. [18]

2. <u>May ERS implement a lower COLA for retirees than it usually has in the past or decline to implement a COLA for retirees at all?</u>

It is my advice that, under its current rules, ERS may implement a lower COLA than it has in the past or decline to implement a COLA at all if its decision to do so is based on a lack of available funds to maintain the actuarial soundness of the system.

Section 47-2-29 provides that "the board of trustees is authorized to adopt a method of providing for postretirement benefit adjustments for the purpose of maintaining essentially no less purchasing power for a beneficiary in his postretirement years." O.C.G.A. § 47-2-29(a). "Such method shall be based upon:" (1) the recommendation of the actuary; (2) maintaining the system's actuarial soundness; (3) "[i]ts application to the retirement income of members retiring on or after the adoption of such method by the board of trustees;" and (4) "[a]ny additional contribution by the member in an amount not to exceed one-fourth of 1 percent of his monthly earnable compensation." *Id.* Although the wording of the statute is not entirely clear, it is my advice that the statute gives ERS authority to create a method for awarding COLA's but does not require ERS to automatically award COLA's at any certain level. It gives ERS the discretion to set up a system for awarding COLA's if it could do so while maintaining the actuarial soundness of the system. *See* 1984 Op. Att'y Gen. 84-19 (opining in a different context that "the decision as to the amount or percentage [of a COLA] is left to the discretion of the governing board of trustees based on the actuary's recommendation and subject to the fundamental concern for the maintenance of the actuarial soundness of the system"). It is my advice that the ERS statutes give ERS the discretion to provide retirees with COLA's but do not on their own make COLA's a binding part of the members' pension contract.[19]

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[18] I note that many of the questions you have raised were also raised 26 years ago – just prior to the 1982 amendment to the "old plan" and creation of the "new plan." In a letter dated September 1, 1981, then-Assistant Attorney General Carl Jones advised then-Director of ERS Abe Domain in regard to employee contribution, retiree COLA and retiree benefit issues. In response to the question "Can our contributions to the retirement system be increased?," he advised as follows: "The ERS Act is silent on the question of whether contributions can be increased. The answer to this question would depend on whether the Georgia courts viewed an increase in contributions to be the dilution or impairment of a right granted by the Retirement System Act. Authorities in this country are divided on this issue."

[19] In the aforementioned September 1, 1981 letter, the Assistant Attorney General advised the ERS Director – in response to the questions "Is a cost-of-living raise guaranteed in

We must also determine, though, whether any decision not to award a COLA or to award a COLA of less than 1½ % would potentially impair the pension contract vis-à-vis the method that ERS has established for awarding COLA's pursuant to its statutory authority. In that regard, § 47-1-31 makes clear that any COLA "granted on or after July 1, 1993, by the board of trustees of any public retirement system pursuant to the authority to grant such increases . . . shall not be considered an element of any contract of employment." Note also, however, that § 47-1-31 does not permit administrative retraction. The discretionary, post-retirement benefits are "subject to reduction by subsequent legislation."

The Georgia courts have not provided clear guidance as to whether the COLA rules and methods that ERS administratively adopted pursuant to its statutory authority prior to the enactment of § 47-1-31 form a binding part of the pension contract between ERS and its members or retirees. Even if we assume for the sake of argument that they do, however, it is my advice that a decision to award a COLA of less than 1½ % or to award no COLA, if based on a lack of "necessary appropriations/funds . . . available to maintain the actuarial soundness of the System," would not violate the terms of the COLA rules that have been in effect for the last twenty years. Since 1987, ERS's officially promulgated COLA rule has expressly provided that "[a]ny such increase in benefit shall become effective only if the necessary appropriations/funds are available to maintain the actuarial soundness of the System." A COLA decision based on a lack of such funds, therefore, would clearly be in accordance with the current rule. While not as explicit, the funding statements of the original policy concerning both COLA's and the separately funded supplemental payments seem also to indicate intent to condition the award on funding availability. This is consistent with the requirement of actuarial soundness.

I must caution, however, that there is a possibility that those who were contributing members of ERS while the earlier methodologies were in effect could still argue that they became, and are still, contractually entitled to such COLA's. As was explained above, the original method indicated that a "cost of living increment will be granted two times per year" based on the calculation of a ratio between the current CPI average and a base index, up to a maximum of 1½ % every six months. The original version of the methodology did not clearly make COLA's contingent upon the availability of funds.

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our retirement system? And if so, is there a minimum amount that we will receive on an annual basis?" – as follows: "The ERS Act provides for postretirement benefit adjustments in Ga. Code Ann. § 40-2502(2)(e). This statute does not guarantee a postretirement benefit adjustment but rather provides that the Board of Trustees may adopt a method of providing for these adjustments based upon four enumerated factors, which include a recommendation of the actuary and the maintenance of the actuarial soundness of the retirement system. There is no minimum amount of postretirement benefit adjustment specified in the statute."

Note also that the original policy also included the possibility of a reduction if the calculated CPI ratio fell below a certain level. Based on information provided by ERS, it is my understanding that, during the period that the 1968 methodology was in effect, COLA's were awarded at rates below the 1½ % maximum on a number of occasions (though they were never actually reduced). ERS promulgated its new COLA rule including a more express reservation that COLA's are contingent upon the availability of necessary funds in 1987, and the rule was amended in 1992 to eliminate a tie between COLA's and the CPI.

It cannot definitively be said how a court would rule on a claim that retirees who were members while previous methodologies were in effect are contractually entitled to a COLA based on the CPI. ERS could reasonably argue in response that, even though the precise methodology has changed, the effective status of COLA's for retirees has not substantively changed because now, as then, retirees may receive COLA's of up to 1½ % every six months but they may receive less – and therefore, a decision not to award a COLA or to award a smaller COLA than has traditionally been awarded, would not unconstitutionally impair the members/retirees' contract because they have never been guaranteed either an increase or an increase of any specific amount. It bears repeating, however, that the Georgia courts have not provided guidance as to how they would view such a claim of a contractual right to the precise methodology previously used.

It is my advice, therefore, that ERS may, under its current rules, decide to award a COLA of less than 1½ % or not to award a COLA at all if the decision to do so is based on a lack of "necessary appropriations/funds . . . available to maintain the actuarial soundness of the System." I caution, though, that retirees who were active members while earlier COLA methodologies were in effect could argue that they are entitled to a COLA based on the CPI calculation described in previous policies, and it is not clear how a court would react to such an argument.

3. <u>May ERS lower the benefits to be paid to "new plan" retirees by reducing the percentage multiplier for benefit calculations?</u>

It is my advice that neither ERS nor the legislature can lower the benefit to be paid to "new plan" retirees by reducing the percentage multiplier for benefit calculations.

The statute provides that "new plan" retirees shall receive:

> A monthly pension which, together with the annuity, shall provide a total retirement allowance equal to more than 1.5 percent, but not greater than 2 percent, the actual percent to be set by the board of trustees in direct relation to the amount of increased appropriations provided

> by the General Assembly to fund the provisions of this paragraph, of the member's highest average monthly earnable compensation during a period of 24 consecutive calendar months while a member of the retirement system, multiplied by the number of the member's years of service.

O.C.G.A. § 47-2-334(b)(1)(B). It is my understanding that the ERS Board has ultimately set the percentage at 2%.

As explained in detail above, the Georgia courts have consistently held that a public pension system may not lower the retirement benefits it has already promised to its active members and retirees. To do so would unconstitutionally impair the obligations of the contract between the system and its members and retirees. *See, e.g., Bender v. Anglin*, 207 Ga. 108 (1950). Having now promised to pay its "new plan" retirees a pension calculated based on the amount that is 2% of the member's highest average monthly salary, therefore, ERS may not unilaterally lower the basis of that calculation and thereby lower the benefit.

Although the statute initially gave a range in which ERS was to set the percentage multiplier (between 1 ½ % and 2%) based on "the amount of increased appropriations provided by the General Assembly to fund the provisions of this paragraph," it does not provide ERS with discretion to subsequently lower the percentage. The General Assembly, for instance, did not provide that, after setting thc percentage based on increased funding, ERS could later lower the percentage in the event of decreased funding. Under the rule of statutory construction known as *expressio unius est exclusio alterius* ("the express mention of one thing implies the exclusion of another"), we can reasonably conclude then that the legislature did not intend to allow ERS to lower the percentage multiplier after setting it. In wording § 47-2-334(b)(1)(B) as it did, the legislature likely was not certain, at the time it passed the statute, of the level at which it would concurrently fund the benefit and, as a result, instructed ERS to set the exact level of the benefit after ERS was ultimately able to ascertain the available funding level. *See, e.g.*, O.C.G.A. §§ 47-20-50 and 47-20-50.1

It is therefore my advice that neither ERS nor the legislature can lower the benefits to be paid to "new plan" retirees by reducing the percentage multiplier for benefit calculations.[20]

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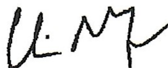
[20] In the aforementioned September 1, 1981 letter, in response to the question "Can the benefits of the present employee be reduced at a later date?," the Assistant Attorney General advised the ERS Director as follows: "...[I]t is clearly the law in Georgia that rights granted by statutes to public employees as members of a public retirement fund become part of the employee's employment contract, so long as the employee makes contributions and performs services while the statute is effective. Those rights cannot be

Conclusion

As explained herein, it is my advice that: (1) ERS has existing statutory authority to adopt a method for awarding COLA's that increases the employee contribution rate up to a total of an additional ¼ % in order to fund COLA's for those who retire after the adoption of such a new method, but courts would likely disfavor any further mandatory increase for existing members in the employee contribution rates set by law for COLA's or annuities. Under existing case law, if a statutory increase is accompanied by comparable new advantages in exchange, ERS could be authorized by the General Assembly to further raise employee contribution rates for members who voluntarily agree to participate in exchange for new advantageous provisions. A unilateral, involuntary increase, however, even with comparable new advantages would require very strong justification and even then would require Georgia courts to change their long-standing interpretation of the constitutional prohibition against impairment of contracts in public pension cases; (2) Consistent with long-standing administrative interpretation and practice and advice, ERS has statutory discretion to determine whether to award a COLA and its amount, but any such award must be consistent with the statutory authority, with the method adopted under the statute, and with the actuarial soundness of the system; and (3) ERS cannot, under existing law, lower the benefits to be paid to "new plan" retirees by reducing the percentage multiplier for benefit calculations.

Sincerely,



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repealed, diluted or restricted by later statutes. See, e.g., Burks v. Board of Trustees, 214 Ga. 251 (1958); Bender v. Anglin, 207 Ga. 108 (1950). Accordingly, it would appear that benefits made available pursuant to the Employees Retirement System Act could not be reduced at a later date as to any employees who contributed and performed employment service while the rights or benefits extended by law were effective."