ALAN WILSON
ATTORNEY GENERAL

August 29, 2016

The Honorable Jeffrey Bradley, Member
South Carolina House of Representatives
P.O. Box 22300
Hilton Head Island, SC 29925

Dear Representative Bradley:

You have sought our opinion "regarding SC Code §§ 9-1-1550, 9-1-1815, 9-1-1970, 9-1-1980 et seq." You note that "[t]hese state statutes identify the criteria to be met before state employees are allowed to participate in the South Carolina retirement system. These sections also contain formulas for determining the amount vested state retirement plan participants will receive at their retirement." By way of background, you further state:

> While statutes generally do not create contracts, the South Carolina Supreme Court, in Layman v. State, found that language contained in SC Code Ann. § 9-1-2210 constituted a contract for certain Teacher and Employee Retirement Incentive [TERI] program participants.
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> With this holding in mind, it appears that the State Retirement System for many years had in place automatic cost of living adjustments [COLAs] for retirement plan beneficiaries, under SC Code Ann. § 9-1-1810. This code section was repealed in 2012. Passed in 1969, it required the Retirement System to annually add COLAs to retirees' monthly checks. In our research, we have not found any other statute passed since 2012 that either modified or replaced this repealed statute. Also, we are not aware of any continued practice by the Retirement System to award automatic COLAs to state retirees each year, other than the 1% or $500 cap in allowance adjustments for current retirees, as set forth in the newer SC Code Ann. § 9-1-1815 that was enacted in 2012.
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> In your September 16, 2014 opinion letter to Rep. James E. Smith, you found statutory savings clauses enacted by the legislature exist "...only as a matter of legislative grace."
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> The General Assembly, as empowered by SC Const. Art. Ill, § 1 et seq., will be reviewing the South Carolina Retirement System to ensure that current state employees will receive retirement benefit payments when they retire. In light of constitutional authority granted to the General Assembly, prior decisions by our 1Supreme Court, your prior opinion letter to Rep. Smith dated September 16. 2014,

and the General Assembly's prior repeal of SC Code Ann. § 9-1-1810, we have these questions as we begin our work:

1. Do SC Const. Art. Ill, as well as, SC Code Ann. §§ 9-1-1550. 9-1-1815, 9-1-1970. 9-1-1980. et seq., in their current forms, and SC Code Ann. § 9-1-1810. prior to its repeal, create any contractual relationships between plan participants and the State of South Carolina? Is there a contract created with current retirees and/or with prospective retirees or is the annual allowance adjustment for retirees also only "...a matter of legislative" grace?

2. If your answer to Question 1 is 'yes. there is a contract,' then is the General Assembly limited, in any way, from altering any aspects of these current state retirement system plans for public employees, including, but not limited to. COLAs, contributions made to the plan by employees, benefits to be paid to them at retirement, or other steps deemed necessary by the General Assembly to be taken in order to keep the plan solvent?

3. If there are limitations, what are they?

4. Because the automatic, annual COLAs for state retirement plan beneficiaries, under SC Code Ann. § 9-1-1 810. have been apparently replaced by the percentage or flat rate allowance adjustment under the newer SC Code Ann. § 9-1-1815 is the General Assembly, through appropriate legislation, nevertheless empowered to direct the Retirement System to never make COLAs, or alternatively, to require that COLAs be awarded to beneficiaries, or to make other retirement plan modifications?

5. By doing so, would the General Assembly be creating any contractual relationships between the plan and its beneficiaries?

Law/Analysis

You request our opinion regarding possible modifications to the state retirement system in an effort to resolve the financial problems surrounding such system. Your questions concern whether the State Retirement System constitutes a "contract" with members and, if so, what steps may be taken by the Legislature to keep the system financially sound? In particular, you wish to know if a court would find a constitutional violation if the General Assembly repealed or suspended the so-called "benefit adjustment," which was enacted in 2012 pursuant to Act No. 278 of 2012 as a replacement for "Cost of Living Adjustments." Section 2, providing for the "benefit adjustment," is today codified at Section 9-1-1815 as follows:

> [e]ffective beginning July 1, 2012, and annually thereafter, the retirement allowance received by retirees and their surviving annuitants inclusive of supplemental allowances payable pursuant to the provisions of Sections 9-1-1910, 9-1-1920 and 9-1-1930, must be increased by the lesser of one percent or five hundred dollars. Only those retirees and their surviving annuitants in receipt of an allowance on July first

> preceding the effective date of the increase are eligible to receive the increase. Any increase in allowance granted pursuant to this section must be included in the determination of any subsequent increase.

As you state in your letter, former § 9-1-1810, which provided "cost of living adjustments" (COLA's) to retirees was repealed by Act No. 278 of 2012 and replaced with the "benefit adjustment" specified by § 9-1-1815. As PEBA (Public Employee Benefit Authority) explained in its presentation regarding Act 278 of 2012, the post-retirement "benefit adjustment" was formerly called a COLA. Previously, according to the PEBA analysis, there was an automatic 1% COLA in SCRS and an ad hoc COLA in the Police Officers Retirement System (PORS). Beginning on July 1, 2012, the benefit adjustment for SCRS and PORS was 1% or $500 per year, whichever is less. See PEBA Analysis of Act 278 of 2012, "Impact of Changes From An Employer and Employee Perspective." The issue now is whether the repeal or suspension of this provision or some other legislative action would violate the "impairment of contract" clause of the state or federal constitutions. See Art. 1, § 4 of the South Carolina Constitution; Art. 1, § 10 of the United States Constitution, or other provisions of the Constitution.

Regarding the constitutionality of acts of the General Assembly, such as a statute repealing the foregoing benefit adjustment, we have consistently stated as follows:

> . . . legislation passed by the General Assembly is presumed constitutional. Horry County School Dist. v. Horry County, 346 S.C. 621, 631, 552 S.E.2d 737, 742 (2001) ("All statutes are presumed constitutional and will, if possible, be construed so as to render them valid."). "A legislative enactment will be declared unconstitutional only when its invalidity appears so clearly as to leave no room for reasonable doubt that it violates a provision of the constitution." Joytime Distribs. and Amusement Co., Inc. v. State, 338 S.C. 634, 640, 528 S.E.2d 647, 650 (1999). Moreover, "[w]hile this Office may comment upon potential constitutional problems, it is solely within the province of the courts of this State to declare an act unconstitutional." Op. S.C. Att'y Gen., August 9, 1997.

Op. S.C. Att'y Gen., 2010 WL 1808720 (April 6, 2010). With that background, we turn now to the issues raised in your letter.

Art. X, § 16 of the South Carolina Constitution provides as follows:

> [t]he governing body of any retirement or pension system in this State funded in whole or in part by public funds shall not pay any increased benefits to members or beneficiaries of such system above the benefit levels in effect on January 1, 1979, unless such governing body shall determine that funding for such increase on a sound actuarial basis has been provided or is concurrently provided.
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> The General Assembly shall annually appropriate funds and prescribe member contributions for any state-operated retirement system which shall insure the

> availability of funds to meet all normal and accrued liability to the system on a sound actuarial basis as determined by the governing body of the system.
>
> Assets and funds established, created and accruing for the purpose of paying obligations to members of the several retirement systems of the State and political subdivisions shall not be diverted or used for any other purpose.
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> Notwithstanding the provisions of Section 11 of this article, the funds of the various state-operated retirement systems may be invested and reinvested in equity securities.

(emphasis added). Our Supreme Court has recognized that maintenance of the fiscal integrity and soundness of the South Carolina Retirement Systems is paramount and is strongly in the public interest. In Wehle v. S.C. Retirement System, 363 S.C. 394, 400, 611 S.E.2d 240, 242-3 (2005), for example, Special Referee (now Justice) Kittredge, whose report was adopted by the Court, noted that Art. X, § 16 requires that, should it be determined that "any retirement system is not funded on a sound actuarial basis, the General Assembly must provide funding necessary to restore the fiscal integrity of the System." 363 S.C. at 399, 611 S.E.2d at 242. And, in Kennedy v. South Carolina Retirement System, 345 S.C. 339, 351, 549 S.E.2d 243, 249 (2001), the Court reasoned as follows:

> [p]olicy considerations also weigh in favor of the retirement system's interpretation. It must be assumed the legislature intends to maintain the soundness of the State Retirement System. . . .
>
> Furthermore, we find the Employees' interpretation of the statute, which would have the unused annual leave added after the total is averaged, leads to an absurd result the Legislature could not have intended. . . . We hold the Employees' interpretation of the statute leads to the absurd result of rendering the State Retirement System arbitrarily unsound. . . .
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> Construing the statute so as to cause such a devastating impact on the fiscal integrity of the State Retirement System, especially in the absence of any fiscal impact report or meaningful debate from the Legislature, would lead to an absurd result that could not have been intended by the legislature.

Thus, it is clear that the General Assembly possesses the duty under the South Carolina Constitution to preserve the fiscal integrity and soundness of the State Retirement System.

Our Supreme Court, on a number of occasions, has addressed specific claims that a legislative change operates as an impairment of a contract. Several of these lawsuits have involved modifications to the state retirement system, other than the reduction of benefits, made in the interest of protecting the System's fiscal integrity. For example, in Anonymous Taxpayer v. S.C. Dept. of Revenue, 377 S.C. 425, 661 S.E.2d 73 (2008), the Court reviewed a statute which, in response to a United States Supreme Court decision (Davis v. Mich. Dept. of Treasury, 489 U.S. 803 (1989)), sought to equalize taxation on federal and state retirees by "deleting the

full tax exemption to state and local government retirees, increasing state retirement benefits by 7%, and allowing a comprehensive exception for only the first $3,000 of all government retirement benefits." 377 S.C. at 430, 561 S.E.2d at 75. The Court upheld the legislative change as constitutional, concluding that the previous statutory tax exemption did not constitute a "contract" for purposes of the constitutional prohibition against contract impairment. The Court's analysis was as follows:

> "'[a]lthough the contact clause appears literally to proscribe 'any' impairment, . . . the prohibition is not an absolute one and is not to be read with literal exactness like a mathematical formula.'" United States Trust Co. of New York v. New Jersey, 431 U.S. 1, 21, 97 S.Ct. 1505, 52 L. Ed.2d 92 (1977) (quoting Home Bldg. & Loan Assn. v. Blaisdell, 290 U.S. 398, 428, 54 S.Ct. 231, 78 L. Ed. 413 (1934)). "The Contract Clause is not an absolute bar to subsequent modification of a State's own financial obligation. As with laws impairing the obligations of private contracts, an impairment may be constitutional if it is reasonably and necessary to serve an important public purpose." United States Trust Co., 431 U.S. at 25, 97 S.Ct. 1505. To establish a contract clause violation, Appellant must show: (1) the existence of a contract; (2) the law changed actually impaired the contract and the impairment was substantial; and (3) the law was not reasonable and necessary to carry out a legitimate government purpose. Hodges v. Rainey, 341 S.C. 79, 93, 533 S.E.2d 578, 585 (2000).

The Supreme Court in Anonymous Taxpayer continued its analysis by summarizing the law relating to the creation of a contract by statutory enactment as follows:

> "Generally, statutes do not create contractual rights." Layman v. State, 368 S.C. 631, 637, 630 S.E.2d 265, 268 (2006). However, a contract created by statute may be found to exist in this State only where contractual rights are expressly found in the language of the statute." Id. at 641, 630 S.E.2d at 270. In Layman, the contractually-significant language included words to the effect that "a member who is eligible," "complies with the requirement of this article," and "shall agree." Id. at 639, 630 S.E.2d at 269.

377 S.C. at 433, 661 S.E.2d at 77. The Court examined the particular statute at issue, -- the tax exemption for retiree's benefits, -- under the three-pronged test of Hodges v. Rainey, and found that the criteria were not met. Most importantly, the Court rejected the argument that there had been created a contract at all by the earlier tax exemption law. The argument for a binding contract was that "the language from other sections of the entire Retirement Code renders all the subsections in the Code, including the tax exemption, a contract with State retirees." However, the Court concluded that the tax exemption provision must stand on its own in creating a contract without the rest of the Retirement Code being "piggybacked" on it:

> [t]his argument is unavailing in light of our opinion in Layman where the language of the statute sections were evaluated individually for contractually-significant language. See Layman, 368 S.C. at 643, 630 S.E.2d at 271 (evaluating separately the

> TERI statute and the working retirees statute, both found within the Retirement Code, to determine that the former TERI statute amounted to a contract and the former working retirees statute did not). Appellant cannot pick separate language from separate sections within the entire Code to render the entire tax exemption a contract.

377 S.C. at 434, 661 S.E.2d at 77. Thus, the statute at issue must contain "contractually-significant language" to create a contract before the remaining criteria of the Hodges v. Rainey test are examined. In the case of the exemption, the Court found not only was there no contract, but went onto conclude that there was no substantial impairment and that the public interest was served by complying with the Davis decision of the United States Supreme Court.

Again, in Ahrens v. State, 392 S.C. 340, 708 S.E.2d at 54 (2011), our Supreme Court upheld legislation requiring working retirees to make contributions to the Retirement System. Previously, working retirees, within certain limits, did not have to contribute to the System. However, the General Assembly, in 2005, enacted Act. No. 153 of 2005, known as the State Retirement System Preservation and Reform Act, which required that "retired members pay the employee contribution as if they were active members but without accruing additional service credit" 392 S.C. at 345, 709 S.E.2d at 57. An action was brought by working retirees, challenging the validity of that statute, contending that it is "unlawful for the State to change the terms of the old working retiree program after the Retirees irreversibly retired, and with the understanding that contributions to the Retirement System would not be required." Id.

The Supreme Court, however, found no contract to have been breached and no estoppel against the State. Again, the Court contrasted its earlier Layman decision, finding a contract with respect to the old TERI system, with Layman's holding as to working retirees:

> [t]his Court found in Layman that the old TERI statute outlined the rights and responsibilities of each party. Id. at 639, 630 S.E.2d at 269. In exchange for the right to lock in a retirement benefit based on the average final compensation of the member, "a program participant shall agree to continue employment with an employer participating in the system for a program period, not to exceed five years." S.C. Code Ann. § 9-1-2210(A) (Supp. 2001) (emphasis added). During this term of employment, the receipt of retirement benefits was deferred, and placed in a non-interest bearing trust account. Id. at § 9-1-2210(B). A program participant was not required to make any further retirement contributions, accrued no service credit, and was not eligible to receive certain employment benefits. Id. at § 9-1-2210(D). This Court found that following terms used in the old TERI statute as "indicative of a contract: 'A . . . member who is eligible [to retire under TERI] . . . and complies with the requirements of this article . . . shall agree to continue employment. . . .'" Layman, 368 S.C. at 639 (quoting S.C. Code Ann. § 9-1-2210(A) (emphasis added)).
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> In contrast, the Court found that the General Assembly did not outline the rights and responsibilities of each party in the SCRS statute. See § 9-1-1970(A) (Supp. 2001). The SCRS statute provided that sixty days after a state employee officially retires, he "may return to employment covered by the system and earn up to fifty thousand

> dollars a fiscal year without affecting the monthly retirement allowance he is receiving from the system." Id. (emphasis added). Under this statute, an employee's decision to return to work after retiring was optional, as was an employer's decision to rehire that employee. The question of whether the PORS [Police Officer Retirement system] statute created a contractual right was not before this Court in Layman. However, because the language of the PORS statute is largely similar to the SCRS statute, we find our analysis of the SCRS statute in Layman to be binding precedent with regard to the PORS statute.

392 S.C. at 349-350, 709 S.E. 2d at 59. Thus, it is clear that, aside from the situation in Layman, where "contractually significant language" was present with respect to the old TERI statute, constitutional claims made against various other legislative changes to the Retirement System have been rejected by our Supreme Court, because no contract with retirees has been created.

Indeed, Layman concluded that the Court's decision was "a very narrow one which affects only those TERI participants who joined the old TERI program, originally enacted in 2001, prior to July 1, 2005." 368 S.C. at 644, 630 S.E.2d at 644. Moreover, in Layman, the Court also held that "the old working retiree statute does not use the same contractually significant language as utilized in the old TERI statute. . . ." As a result "the old working retiree statute does not create a binding contract between the State and the old working retirees prohibiting the State from altering the statute exempting old working retirees from further contributions to the retirement system. Stated differently, the old working retiree statute does not evidence an intent by the legislature to be bound to any terms relating to the old working retiree program." 368 S.C. at 643, 630 S.E.2d at 271. See also, Alston v. City of Camden, 322 S.C. 38, 471 S.E.2d 174 (1996) [personnel ordinances did not give rise to any contract between the City and employees. Even if it did, such contract did not give rise to any expectation that fringe benefits would continue for any specific time; thus, ordinances did not substantially impair a contract in violation of the Contract Clause].

The Court has not been as clear, however, with respect to the more fundamental question of whether retirement benefits paid to retirees by the State Retirement System constitute a contractual obligation. In McKinney v. South Carolina Police Officers Retirement System, 311 S.C. 372, 429 S.E.2d 797 (1993), the Court seemingly stated not:

> McKinney misconstrues the nature of his right to retirement benefits: the source of his rights is the statutes, not a contract. See Anderson v. South Carolina Retirement System, 278 S.C. 161, 293 S.E.2d 312 (1982). Neither McKinney nor respondent have the authority to convert this statutory right into a contractual one.

311 S.C. at 375, 429 S.E.2d at 798. See also Smith v. S.C. Retirement System, 336 S.C. 505, 520 S.E.2d 339 (Ct. App. 1999) [entitlement to state retirement benefits is purely statutory].

On the other hand, in Evans v. State, 344 S.C. 60, 67, 543 S.E.2d 551 (2001), the Court assumed a contract between the State and retirees in a breach of contract action brought by state retirees against the Retirement System. In that case, the Court stated:

> [i]n their breach of contract cause of action, State Retirees assert the various Retirement systems breached their contracts with them by unilaterally reducing the amount of tax exemption on their retirement benefits. . . . Assuming there is a contract between the Retirement System and State Retirees and that the full tax exemption is part of that contract, the Retirement systems cannot be liable for the alleged breach because it was impossible for Retirement Systems to perform under the contract's terms once Act 189 became law.

(emphasis added).

Moreover, in Wright v. City of Florence, 229 S.C. 419, 93 S.E.2d 215 (1956), the Court concluded that repeal by the City of Florence of an ordinance establishing a Civil Service Commission did not impair a contract. However, by way of dicta, the Supreme Court, relying upon McQuillin Municipal Corporations, 3d ed., Vol. 6, § 21.10 distinguished the repeal in that situation from other instances, including repeal of an ordinance establishing a pension fund:

> '[o]ne council may not by an ordinance bind itself or its successors so as to prevent free legislation in matters of municipal government. Accordingly, in the absence of a valid provision to the contrary, a municipal council or assembly, having the power to legislate on, or exercise discretionary or regulatory authority over any given subject may exercise that power at will by enacting or repealing an ordinance in relation to the subject. Thus, the power of repeal extends to legislative enactments and, a fortiori, to ordinances of an administrative character, as, for example, an ordinance fixing the fiscal year of a municipal corporation. The power does not extend, however, to authorize impairment of a contract or deprivation of property without due process of law.'
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> Beside the limitation upon the right of repeal which impairs a contract or deprives one of property without due process of law or, rather the effect of the repeal . . . McQuillin notes another exception to the rule of implied power of repeal, which exists where an ordinance has been enacted under a narrow, limited grant of authority to do a single designated thing in the manner and at the time prescribed by the legislature, which excludes the implication that the city council is given any further jurisdiction over the subject than to do the one act. He expresses it another way, that no power of repeal exists as to an ordinance that constitutes the exercise of municipal power which is exhausted by its single exercise. An example of the latter is Thompson v. City of Marion, 1938, 134 Ohio St. 122, 16 N.E.2d 208, 210, where the city attempted to repeal an ordinance which set up a police and firemen's pension fund. The statute provided that such a system might be set up by ordinance where the council declared the necessity for it. The court concluded that the rule of implied power of repeal did not apply because the statute expressly limited authority to council to do a certain thing in the manner and within the time fixed by the

> legislature, and it was said in the opinion: 'If [council] had only the power of determination of the question of necessity and when that was found in the affirmative, its power was exhausted.'

229 S.C. at 424-426, 93 S.E.2s at 218. See also Grimsley v. S.C. Law Enforcement Div., 396 S.C. 276, 721 S.E.2d 423 (2012) [Plaintiffs have a cognizable property interest in the percentage of their salary deducted for retirement in violation of § 9-11-90].

It is also worthy of note that the Administrative Law Court (ALC) has found that "the South Carolina General Assembly intended all the benefits contained in the Retirement Code to be both contractual and vested rights." The ALC noted that "the provisions of the Retirement Code promise benefits upon retirement; they are more than a chance for benefits." That Court's decision, finding a contract, was based upon numerous factors: the overwhelming case law in other jurisdictions; provisions in the Retirement Code, such as §§ 9-1-1690, 9-8-200, 9-9-190 and 9-11-280; the fact that the "Retirement Code is replete with multiple references" suggesting a "contract"; and the fact that in Ball v. Ball, 314 S.C. 445, 447, 445 S.E.2d 449, 450 (1994), our Supreme Court had held that retirement benefits are deferred compensation. The ALC rejected the argument that McKinney had concluded no contract existed as to retirement benefits. While the Supreme Court subsequently held that removal of the tax exemption as to retirees did not constitute a contract, the Administrative Law Court's conclusion that the "Retirement Code . . . creates a contract between the State of South Carolina and private parties (the members of the Retirement Systems)" is instructive here. See Anonymous Taxpayers v. S.C. Dept. of Revenue, 2002 WL 1486983 (ruling of Administrative Law Court) (June 14, 2002).

Moreover, as the Administrative Law Court in Anonymous Taxpayers recognized, case law elsewhere concludes that a governmental retirement system has contractual obligation to its retirees. One legal treatise has explained:

> . . . it is generally accepted that retirement plans of State and local governments give rise to contractual rights within the scope of the Contract Clause. . . . When a public employee's right to retirement benefits becomes absolutely vested, a contract exists between the employee and the State which cannot be modified by unilateral action on the part of the legislature.

16A C.J.S. Constitutional Law § 549. Further, as the District Court of Maryland noted, "in Maryland, as in most states, public employee pension plans embody contractual rights and duties between an employee and the government as employer under the well-settled Contract Clause analytical approach." Howell v. Anne Arundel County, 14 F. Supp.2d 752, 754 (D. Md. 1998). See also 16B Am. Jur.2d Constitutional Law § 788 ["Any attempt to reduce or terminate benefits for government employees that are established by a statute or ordinance is prohibited by the Contracts Clause. . . ."].

Commentators are in accord that a contact generally existing between the government and retirees as part of the government-created pension fund. As one commentator has noted,

"although a majority of states find that retirement benefits are contractual in nature, there is a disparity among the states regarding the exact time at which retirement members rights vest in the contract." See Selby, "Pensions In a Pinch: Why Texas Should Reconsider Its Policies on Public Retirement Benefit Protection," 43 Tex. Tech. L.Rev. 1211, 1232 and n. 142 (2011) [referencing numerous decisions find a contract between governmental entity and pensioners]. Another legal commentator traces the historical development of the constitutional protection of public pension benefits as follows:

> [l]egislative interference with pension rights raises state and federal constitutional concerns. . . . Specifically, government alteration of the defined benefit plan or its basic features could potentially violate the state and federal due process clauses, takings clauses, and contract clauses. . . . Legal protection extends only to existing employees and retirees, not new hires.
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> The traditional view of public pensions sees them as gratuities granted by the state that can be modified or abolished even after retirement. . . . Texas courts still consider pensions as gratuities. . . . As far as the Constitution is concerned, lawmakers in states that have adopted the gratuity approach have the most freedom to fix pension problems. . . . They may be constrained by moral and policy concerns, but not the law.
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> An overwhelming majority of states, however, have transformed tradition and retreated from the notion of pensions as unprotected gratuities and adopted a modern view that is more protective of the retirement security of public employees. . . . Change has come by judicial interpretation and legislative enactment. . . . The modern view postulates that it is possible for government workers to have a protectable interest in their pensions. . . .

Anenson, "Reforming Public Pensions," 33 Yale L.S. Policy Rev. 1, 15 (2014).

It appears that our own Supreme Court may similarly be in the process of recognizing this evolution, moving from the "gratuity" theory to constitutional protection, at least in certain instances. McKinney may well represent some form of the "gratuity" theory, by deeming retirement benefits as purely statutory, while Layman appears to have opened the door in terms of constitutionally protected contractual obligations. While the Court has not yet squarely decided the issue as to whether retirement benefits constitute a contractual obligation of the State, we believe it is likely the Court will join the majority of jurisdictions which have so held.

In contrast to the question of whether the payment of basic retirement benefits are a contractual obligation, a number of decisions in other jurisdictions have dealt with the separate question of repealing or suspending "cost of living" increases for governmental retirees and whether such action violates the Contract Clause. While our own Supreme Court has not dealt with the question of COLA's, almost universally, courts elsewhere have concluded that such repeal or limitation does not impair a contract. See Justus v. State, 336 P.3d 202 (Colo. 2014); Am. Fed. of Teachers v. State, 111 A.3d 63 (N.H. 2015) [no vested right in a COLA]; Bartlett v.

Cameron, 316 P.3d 889, 893 (N.M. 2013) [a cost-of-living adjustment to a retirement benefit is not necessarily the same thing as the underlying benefit]; Maine Assn. of Retirees v. Bd. Of Trustees of the Maine Public Employees Retirement System, 758 F.3d 23 (1st Cir. 2014) [it is not unmistakably clear that COLAs fall within the umbrella of benefits that the Legislature is assumed to be contractually obligated not to reduce]; Claypool v. Wilson, 4 Cal. App. 4th 646, 6 Cal. Reptr.2d 77 (1992) [repeal of COLA did not impair contracts]; Berg v. Christie, 137 A.3d 1143 (N.J. 2016) [suspending COLAs does not impair contracts]; Wash. Ed. Assn. v. Wash. Dept. of Retirement Systems, 332 P.3d 439 (Wash. 2014) (en banc) [repeal of COLA not violative of the Constitution; employees did not contribute to the adjustments]; Picard v. Members of Employees Retirement Bd. Of Providence, 275 F.3d 139 (1st Cir. 2001) [restriction of COLA does not deprive retirees of property or contract rights]; Puckett v. Lexington-Fayette Urban Co. Gov't., 60 F.Supp.3d 772 (E.D. Ky. 2014); Md. State Teachers Assn., Inc. v. Hughes, 594 F.Supp. 1353 (D. Md. 1984) [good public policy to protect an actuarially sound system]; Robertson v. Kulongoski, 359 F.Supp. 1094 (D. Oregon 2004) [reduction of COLA does not impair contracts].

In Maine Assn. of Retirees, supra, the 1st Circuit Court of Appeals' analysis was similar to that of our own Supreme Court in the decisions referenced above. Thus, the Court held that "Plaintiffs, regardless of whether they retired before or after the 1999 amendment, have no contractual entitlement to COLA benefits calculated under pre-2011 law." 758 F.3d at 32. In Justus, the Court noted that "[b]y its very nature a statutory cost of living adjustment is a periodic exercise of legislative discretion that takes account of changing economic conditions in the State and/or nation." 336 P.3d at 209.

Moreover, as the United States Supreme Court has explained, "absent some clear indication that the legislature intends to bind itself contractually the presumption is that a law is not intended to create private contractual or vested rights but merely declares a policy to be pursued until the legislature shall ordain otherwise." National R.R. Passenger Corp. v. Atchison, Topeka & Santa Fe Ry. Co., 302 U.S. 74, 79 (1937). There, the Court added:

> . . . the principal function of a legislature is not to make contracts, but to make laws that establish the policy of the state. . . . Policies, unlike contracts, are inherently subject to revision and repeal and to construe laws as contracts when the obligation is not clearly and unequivocally expressed would be to limit drastically the essential powers of a legislative body.

Id.

Further, in Frazier v. City of Chattanooga, 151 F.Supp.3d 830, 838 (E.D. Tenn. 2015), the Court stated that a COLA "is an adjustment to the pensioners' benefits rather than a benefit itself. It is designed to ameliorate the effects of inflation and is a compounded adjustment to the pension benefit." And, in Cherry v. Mayor and City Council of Balt. City, 762 F.3d 366 (4th Cir. 2014), the Fourth Circuit denied the Contract Clause claim, affirming the District Court, which had concluded that the City had acted reasonably in substituting a cost-of-living adjustment for

variable benefit in order to stabilize the plan. In Washington Ed. Assn., supra the Supreme Court of Washington observed that:

> [t]he nature of the UCOLA benefit also supports the enforceability of the legislature's right to repeal this benefit. Employees do not contribute to the UCOLA and the adjustment provided is not "pay withheld to induce continued faithful service" in the same way that a basic pension plan is. . . . This is particularly true of members who retired prior to UCOLA's enactment in 1995. Whereas a basic pension plan is deferred compensation and induces long and faithful service over time, a COLA merely enhances the value of the basic pension payment by adjusting for inflation and cost of living increases. Surely the legislature can make the addition of such a bonus subject to its right to amend and repeal the program in the future. To say otherwise would strongly disincentivize the legislature from providing additional benefits beyond a basic pension.

332 P.3d at 446. Further, in Cameron, supra, the Supreme Court of New Mexico concluded that "[u]nless we are satisfied that the Legislature intends to create a property right, this Court presumes that the Legislature is implementing public policy when it enacts a statute, policy which it is free to change in the future. . . . To presume otherwise would upset the balance of the separation of powers, and affect the Legislature's ability to respond to changing economic conditions." 316 P.3d at 894-895. In Cameron, retirees "received a smaller COLA increase on July 1, 2013, and will continue to so in future years – up to twenty percent less – as compared with what they would have received under the COLA provisions in effect at the time of their respective retirements." Id. at 891. Thus,

> . . . The COLA is provided independently from the obligation and payment of the retirement benefit. Reducing the COLA prospectively may affect the retiree's economic purchasing power, but it does not reduce the employee's substantive retirement benefit.

Id. at 894.

Thus, it may be seen that the law with respect to the State Retirement Systems is in the process of evolving. Since the McKinney case, decided in 1993, our Supreme Court has decided a number of cases, including the landmark Layman decision. Yet the Court has not yet addressed the specific issues raised in your letter. Our best "guess," based upon decisions in other jurisdictions, as well as Layman, is that our Supreme Court would find a "contract" with respect to retirement benefits, but would not so find with respect to COLA's or the so-called "benefit adjustment." We stress that only the Court can decide these difficult questions, having before it a full record and a particular statute which is challenged as impairing a contract or in contravention of some other constitutional provision.

Conclusion

While our Supreme Court has not directly addressed the question of whether the laws relating to State Retirement Systems create contractual obligations between the State and retirees generally, we believe that the Court could well conclude that they do. Section 9-1-1690 expressly references "[a]ll agreements or contracts." Moreover, in Evans, supra, the Court assumed the existence of a contract in this respect. In Layman, the Court found a contract with regard to the old TERI program. There, the Court found "that the language in the old TERI statute demonstrates, in unambiguous terms, the intent of the legislature to bind itself to the forms in the statute." 368 S.C. at 639, 630 S.E.2d at 269. We note, however that there is language in the McKinney case which characterizes the Retirement System as statutory rather than contractual. However, the Administrative Law Court in Anonymous Taxpayers concluded that McKinney was not dispositive and that ". . . the South Carolina General Assembly intended all the benefits in the Retirement Code to be both contractual rights and vested rights." In light of the Court's reasoning in Layman and other more recent cases discussed above, it is not clear at all that McKinney is controlling as to this question.

As discussed above, other jurisdictions reach the conclusion that a contract between the State and retirees protects retirement benefits. One treatise states that "it is generally accepted that the retirement plans of state and local governments give rise to contractual rights within the scope of the Contract Clause." 16A C.J.S. Constitutional Law § 549. Thus, based upon the criteria set forth in Layman and other cases, the answer to your first question is most likely "yes." While the Court has yet to face the issue directly, we believe it is probable that the Court would follow the authorities in other jurisdictions, and find that the continuing payment of retirement benefits is a contract for purposes of the Contract Clause.

In this same regard, we would note that courts elsewhere have concluded that reduction of retirement benefits constitutes an impairment of contract. See e.g. Falkenbury v. Teachers' and State Employees' Retirement System of North Carolina, 483 S.E.2d 422 (N.C. 1997); Felt v. Bd. Of Trustees of Judges Retirement System, 481 N.E.2d 698, 700 (Ill. 1985) ["The change in the basis of computation clearly effects a reduction or impairment in the retirement benefits of the plaintiff members of state retirement systems in violation of the constitutional assurance. . . ."]; Bender v. Anglin, 60 S.E.2d 756 (Ga. 1950); Pfleger v. City of Reading, 1996 WL 377112 (E.D. Pa. 1996) [". . . the rights and responsibilities of the public employers and employees are contractual in nature, are established when the employees enter the retirement system and are not thereafter subject to unilateral change. Such reasoning and rule does not, however, mean that the retirement system cannot be altered for new employees prior to their entry into the system."].

On the other hand, COLA's may be a different question altogether. The Court has issued a number of decisions, distinguishing Layman in which it has concluded that there was no contract with respect to certain specific benefits which are bestowed upon retirees in addition to the retirement benefit itself. Thus, later action taken by the General Assembly in order to protect the soundness of the System, or to serve some overriding public purpose, was, in certain

circumstances, held not to constitute an "impairment of contract" for purposes of the Constitution. For example, in Anonymous Taxpayer, supra, the Court found no contract created by the pre-1989 tax exemption for retirement benefits. Distinguishing Layman with respect to the old TERI statute, where "contractually significant language" was used in enacting the original law, the Court held that the fact that the exemption was in the Retirement Code did not create a contract. According to the Court, the language of the specific statute creating the benefit must be evaluated individually and that statute must contain "contractually-significant language." Moreover, even if a contract had been created, any impairment thereof must be "substantial" and if the Legislature's action is deemed "reasonable and necessary to carry out a legitimate state purpose," no unconstitutional impairment has occurred. We stress that the question of COLA's has not been addressed by our Court. However, based upon the decisions in other jurisdictions, as well as our cases such as Akrens and Anonymous Taxpayer, COLA's or benefit adjustments could well be held to fall in this same category, particularly where it is necessary to preserve the fiscal soundness of the System. In other words, our Court may well deem COLA's or a "benefit adjustment" not to be a contract.

Further, it must be noted that Art. X, § 16 of the Constitution requires the General Assembly to maintain the fiscal integrity and soundness of the Retirement Systems. Thus, any action taken by the General Assembly to protect the System would be viewed by the Court in that light. Given that one of the criteria for an impairment of contract action is that the "law [is]... not reasonable and necessary to carry out a legitimate government purpose," should the Legislature take action to preserve the fiscal soundness of the System, and such action does not reduce retirement benefits, but instead addresses issues such as COLA's, a court will give strong consideration to that fact. Accordingly, it will be most difficult to succeed in any breach of contract or impairment of contract action so long as the Legislature is acting pursuant to its constitutional authority pursuant to Art. X, § 16 to protect the soundness of the Retirement System. As our Court has concluded, "the Court looks for contractually significant language within the statute in determining whether a contract was intended to be created by the Legislature." Anonymous Taxpayer, id. And, a significant public purpose, such as preservation of the fiscal soundness of the Systems, served by the legislative action will be deemed by the Court to be paramount.

Moreover, with respect to reduction or removal of COLA's or "benefit adjustments," it is important to note courts elsewhere have differentiated such adjustments from the retirement benefit itself. Our review of legislative actions concerning reduction or removal of COLA's in other jurisdictions finds that courts have almost universally upheld such actions. A COLA or a "benefit adjustment" aimed at keeping the retiree up with economic or inflationary changes is simply not viewed in the same light by the courts, legally, as the benefit itself.

As one court has concluded, "a basic pension plan is deferred compensation and induces long and faithful service over time, [but] a COLA merely enhances the value of the basic pension payment by adjusting for inflation and cost of living increases." Wash. Ed. Assn., supra. The language of § 9-1-1815, providing for the "benefit adjustment," uses words like "annually

thereafter." Absent a contract, one Legislature does not bind another to appropriate funds. See Caddell v. Lexington Co. Sch. Dist., 296 S.C. 397, 373 S.E.2d 598 (1998). In Puckett v. Lexington-Fayette Urban County Government, ___ F.3d ___, 2016 WL 4269802 (August 15, 2016), the Sixth Circuit, just days ago, rejected the claim by "retired public employees who contend they have a contract with the State of Kentucky entitling them to have their base pension benefit annually adjusted by the specific cost of living adjustment ("COLA") formula in existence at the time they retired." Tellingly, the Court noted that "[a]lmost every court to have considered the issue has rejected claims that statutory pension schemes and provisions about COLA's created contract rights subject to the constraints of the Contract Clause." Slip Op. at 7 [referencing numerous decisions, many of which are referenced herein]. The Sixth Circuit found also that the statutory reduction did not violate the Due Process Clause or the Takings Clause. We believe that a court in South Carolina would well reach the same conclusion concerning removal or reduction of COLAs or benefit adjustments with respect to the State Retirement Systems. However, as you are well aware, only a court can answer this question definitively.

We must thus emphasize, however, that our analysis is simply our best "prediction" as to how a court would rule. We have not examined any specific legislative proposal, and thus we must advise you, based upon our Supreme Court's previous decisions, as well as case law in other jurisdictions. Except for the special and unique circumstance in Layman, where the Act in question contained "contractually-significant language" with respect to the old TERI statute, our Court has not found a contract impairment with respect to various actions taken by the General Assembly concerning the protection of the State Retirement Systems. Any legal challenge must find the existence of a "contract," a "substantial" impairment, and that "the law was not reasonable and necessary to carry out a legitimate government purpose." Considering that the Legislature has a constitutional duty to protect the fiscal soundness of the system, this is a very difficult hurdle for any constitutional challenge to overcome, particularly if such challenge is based upon a continuing entitlement to a COLA or "benefit adjustment" enacted at the time of retirement. See Puckett v. Lexington-Fayette Urban County Government, id.

Sincerely,

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Solicitor General