

STATE OF MICHIGAN
COURT OF APPEALS

AFT MICHIGAN, HENRY FORD
COMMUNITY COLLEGE ADJUNCT
FACULTY ORGANIZATION, AFL CIO, AFT,
ALPENA MONTMORENCY ALCONA ISD
PARAPROFESSIONALS, ALPENA
MONTMORENCY ALCONA ISD TEACHERS,
ARENAC EASTERN FEDERATION, BAY
ARENAC SKILLS CENTER FEDERATION,
BROWN CITY EMPLOYEES ORGANIZATION,
BROWN CITY FEDERATION OF TEACHERS,
CHEBOYGAN OTSEGO PRESQUE ISLE
SUPPORT PERSONNEL, CHEBOYGAN
OTSEGO PRESQUE ISLE INTERMEDIATE
PARAPROFESSIONALS, CHESANING UNION
AUXILIARY SERVICE EMPLOYEES, CLARE
GLADWIN ISD FEDERATION, CRAWFORD
AUSABLE BUS DRIVERS FEDERATION,
CRAWFORD AUSABLE CUSTODIANS
SECRETARIAL FEDERATION, CRAWFORD
AUSABLE FEDERATION OF TEACHERS,
CRAWFORD AUSABLE SUPPORT STAFF
FEDERATION, CRESTWOOD FEDERATION
OF TEACHERS, CTR FEDERATION,
DEARBORN FEDERATION OF SCHOOL
EMPLOYEES, DEARBORN FEDERATION OF
TEACHERS, DETROIT ASSOCIATION OF
EDUCATIONAL OFFICE EMPLOYEES,
DETROIT FEDERATION OF
PARAPROFESSIONALS, DETROIT
FEDERATION OF TEACHERS, EAST
DETROIT FEDERATION OF TEACHERS,
ECORSE FEDERATION OF TEACHERS,
FAIRVIEW FEDERATION OF TEACHERS,
FEDERATION OF TEACHERS, GLEN LAKE
FEDERATION OF TEACHERS, HALE
FEDERATION OF TEACHERS, HAMTRAMCK
FEDERATION OF TEACHERS, HEMLOCK
FEDERATION OF TEACHERS, HENRY FORD
COMMUNITY COLLEGE ADJUNCT
FACULTY ORGANIZATION,

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HENRY FORD COMMUNITY COLLEGE
FEDERATION OF TEACHERS, HIGHLAND
PARK FEDERATION OF
PARAPROFESSIONALS, HIGHLAND PARK
FEDERATION OF TEACHERS, HURON
VALLEY CONTINUING EDUCATION, IMLAY
CITY FEDERATION OF TEACHERS, INKSTER
FEDERATION OF TEACHERS, IOSCO ISD
FEDERATION OF TEACHERS, IOSCO ISD
INTERMEDIATE FEDERATION OF
AUXILIARY EMPLOYEES, KINGSLEY
FEDERATION OF TEACHERS, KIRTLAND
COMMUNITY COLLEGE FEDERATION OF
TEACHERS, LAMPHERE FEDERATION OF
PARAPROFESSIONALS, LAMPHERE
FEDERATION OF TEACHERS, LANSING
COMMUNITY COLLEGE ADMINISTRATIVE
ASSOCIATION, LES CHENEAX
FEDERATION OF SUPPORT STAFF, LES
CHENEAX FEDERATION OF TEACHERS,
LAKE CITY SUPPORT STAFF FEDERATION,
LAKE CITY TEACHERS AND
PARAPROFESSIONALS FEDERATION, LAKE
SHORE FEDERATION OF EDUCATIONAL
SECRETARIES, LAKE SHORE FEDERATION
OF TEACHERS, LAKE SHORE FEDERATION
SUPPORT STAFF, MACOMB INTERMEDIATE
FEDERATION OF PARAPROFESSIONALS,
MACOMB INTERMEDIATE FEDERATION OF
TEACHERS, MELVINDALE NAP
FEDERATION OF TEACHERS, MELVINDALE
NAP PARAPROFESSIONALS, MIDLAND
FEDERATION OF PARAPROFESSIONALS,
MIDLAND ISD FEDERATION OF
PARAPROFESSIONALS, MIDLAND ISD
FEDERATION OF TEACHERS, NORTHVILLE
FEDERATION OF PARAPROFESSIONALS,
ONAWAY FEDERATION OF SCHOOL
RELATED PERSONNEL, ONAWAY
FEDERATION OF TEACHERS, PLYMOUTH
CANTON COMMUNITY SCHOOL
SECRETARIAL UNIT, PLYMOUTH CANTON
FEDERATION OF PLANT ENGINEERS,
ROMULUS FEDERATION OF
PARAPROFESSIONALS, ROSEVILLE
FEDERATION OF TEACHERS, RUDYARD

FEDERATION OF AIDES, RUDYARD
FEDERATION OF TEACHERS, SAGINAW ISD
FEDERATION OF TEACHERS, TAWAS AREA
FEDERATION OF TEACHERS, TAYLOR
FEDERATION OF TEACHERS, UTICA
FEDERATION OF TEACHERS, VAN DYKE
EDUCATIONAL ASSISTANTS FEDERATION,
VAN DYKE PROFESSIONAL PERSONNEL,
WARREN WOODS FEDERATION OF
PARAPROFESSIONALS, WASHTENAW
INTERMEDIATE SCHOOL EMPLOYEES
FEDERATION, WATERFORD ASSOCIATION
OF SUPPORT PERSONNEL, WAYNE COUNTY
COMMUNITY COLLEGE FEDERATION OF
TEACHERS, WAYNE COUNTY COMMUNITY
COLLEGE PROFESSIONAL AND ADMIN
ASSOCIATION, WAYNE COUNTY RESA
SALARIED STAFF, WEXFORD MISSAUKEE
ISD FEDERATION OF TEACHERS,
WHITEFISH TOWNSHIP FEDERATION OF
TEACHERS, CHEBOYGAN OTSEGO
PRESQUE ISLE ISD TEACHERS and
HEMLOCK AUXILIARY SERVICE
EMPLOYEES,

Plaintiffs-Appellees,

V

STATE OF MICHIGAN,

Defendant-Appellant.

No. 303702
Court of Claims
LC No. 10-000091-MM

TIMOTHY L. JOHNSON, JANET HESLET,
RICKY A. MACK and DENISE ZIEJA,

Plaintiffs-Appellees/Cross-
Appellants,

V

PUBLIC SCHOOL EMPLOYEES RETIREMENT
SYSTEM, PUBLIC SCHOOL EMPLOYEES
RETIREMENT SYSTEM BOARD, TRUST FOR
PUBLIC EMPLOYEE RETIREMENT HEALTH

No. 303704
Court of Claims
LC No. 10-000047-MM

CARE and DEPARTMENT OF TECHNOLOGY,
MANAGEMENT, AND BUDGET,

Defendants-Appellants/Cross-
Appellees,

and

DIRECTOR OF DEPARTMENT OF
TECHNOLOGY MANAGEMENT AND
BUDGET, DIRECTOR OF RETIREMENT
SERVICES OFFICE and STATE TREASURER,

Defendants.

DEBORAH MCMILLAN, THOMAS BRENNER,
THERESA DUDLEY, KATHERINE DANIELS
and COREY CRAMB,

Plaintiffs-Appellees/Cross-
Appellants,

V

PUBLIC SCHOOL EMPLOYEES RETIREMENT
SYSTEM, PUBLIC SCHOOL EMPLOYEES
RETIREMENT SYSTEM BOARD, TRUST FOR
PUBLIC EMPLOYEE RETIREMENT HEALTH
CARE and DEPARTMENT OF TECHNOLOGY,
MANAGEMENT, AND BUDGET,

Defendants-Appellants/Cross-
Appellees,

and

DIRECTOR OF DEPARTMENT OF
TECHNOLOGY MANAGEMENT AND
BUDGET, DIRECTOR OF RETIREMENT
SERVICES OFFICE and STATE TREASURER,

Defendants.

No. 303706
Court of Claims
LC No. 10-000045-MM

Before: SHAPIRO, P.J., and SAAD and BECKERING, JJ.

SHAPIRO, P.J.

In the three cases consolidated in this appeal, plaintiff public school employees and their representative organizations raise various constitutional challenges to MCL 38.1343e. This provision was adopted in 2010 and amended Article 3 of the Public School Employees Retirement Act of 1979, which governs the Michigan Public School Employees Retirement System (MPERS). MCL 38.1343e requires that public school districts and other “reporting units”¹ withhold three percent of each employee’s wages and remit the amount to the MPERS as an “employer contribution” to the trust that funds retiree health care benefits.

We conclude that MCL 38.1343e violates multiple constitutional rights set forth in both the United States and Michigan Constitutions and is therefore invalid. Specifically, we conclude that the statute violates federal and state constitutional protections against: state impairment of contracts, the taking of private property by the government without compensation as well as the constitutional guarantee of substantive due process. The prohibition against governmental impairment of contracts is violated because the statute requires that school employees be paid three percent² less than the amount they and their employers freely agreed upon in contracts. The prohibition against the taking of private property is violated because the MCL 38.1343e does not merely create a general obligation on the part of active employees to pay a certain sum, but instead directs that unique and definable monies in which plaintiffs have a property interest be confiscated by their government employers. Moreover, the confiscated wages are then used to pay the statutory-mandated *employers’* contributions to a state fund. Finally, while the fund in question funds health benefits for present retirees, the active employees whose wages are taken, have no vested right themselves to receipt of health benefits upon their own retirement.

I. BACKGROUND

MCL 38.1343e became effective in 2010 and reads as follows:

(1) Except as otherwise provided in this section, beginning July 1, 2010, each member shall contribute 3% of the member's compensation to the appropriate funding account established under the public employee retirement health care funding act [MCL 38.2731 *et seq.*]. For the school fiscal year that begins July 1, 2010, members who were employed by a reporting unit [i.e., school district] and were paid less than \$18,000.00 in the prior school fiscal year and members who were hired on or after July 1, 2010 with a starting salary less than

¹ These include intermediate school districts, public school academy, tax-supported community or junior colleges, universities and any agency having employees on its payroll who are members of the retirement system.

² The statute required any public school employee whose salary is less than \$18,000 to contribute 1.5 percent for the fiscal year starting July 1, 2010. MCL 38.1343e. Beginning July 1, 2011, all employees were required to contribute the full three percent. *Id.*

\$18,000.00 shall contribute 1.5% of the member's compensation to the appropriate funding account established under the public employee retirement health care funding act. For each school fiscal year that begins on or after July 1, 2011, members whose yearly salary is less than \$18,000.00 shall contribute 3% of the member's compensation to the appropriate funding account established under the public employee retirement health care funding act. The member contributions shall be deducted by the employer and remitted as employer contributions in a manner that the retirement system shall determine.

(2) As used in this act, “funding account” means the appropriate irrevocable trust created in the public employee retirement health care funding act for the deposit of funds and the payment of retirement health care benefits. [Footnote omitted.]

Another provision of 2010 PA 77, codified as MCL 38.2733(6) provides, in pertinent part:

This act shall not be construed to define or otherwise assure, deny, diminish, increase, or grant any right or privilege to health care benefits or other postemployment benefits to any person

Accordingly, MCL 38.1343e cannot be read to grant any “right or privilege” to retiree health care benefits beyond that already in place. And as determined by the Michigan Supreme Court in *Studier v MPSERB*, 472 Mich 642; 698 NW2d 350 (2005), school employee retiree health care benefits are not guaranteed by contract and do not constitute an accrued benefit protected from impairment or elimination by Const 1963, art 9, §24.³

After the effective date of MCL 38.1343e, school districts began to withhold three percent of employee wages for remittance as employer contributions to the MPSERS. Plaintiffs brought suit in the Court of Claims to enjoin further withholding, to obtain a declaratory ruling that the statute was unconstitutional and to have the withheld wages returned to them with statutory interest. The court ordered that the withheld wages be placed in an interest-bearing account, rather than the MPSERS trusts, and that they be maintained there until the legal challenge was resolved. The court later granted summary disposition in favor of plaintiffs in each of the three cases, two of which were brought by individual school employees and one by an array of labor organizations representing school employees.

The court rejected defendants’ motion to dismiss the labor organizations as plaintiffs finding that they had standing to challenge the statute. It also rejected the defendants’ assertion that the claims were not ripe for review.

³ This provision of the Michigan constitution provides in part that “accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation which shall not be diminished or impaired thereby.”

As to the substance of the constitutional challenges, the court held that the statute violated plaintiffs' rights under both the Takings Clauses and the Due Process Clauses of the federal and state constitutions. The trial court held that the statute did not violate the constitutional provisions barring impairment of contracts by the state and also dismissed a common law breach of contract claim.

II. STANDING

Defendants argue that the plaintiff labor organizations in case no. 303702 do not have standing to bring suit. Whether a party has standing is a question of law that this Court reviews *de novo*. *Glen Lake-Crystal River Watershed Riparians v Glen Lake Ass'n*, 264 Mich App 523, 527; 695 NW2d 508 (2004). In reviewing a motion under MCR 2.116(c)(5), this Court considers the pleadings, affidavits, depositions, admissions, and any other documentary evidence submitted by the parties to determine whether the moving party is entitled to judgment as a matter of law. MCR 2.116(g)(5); *Kuhn v Secretary of State*, 228 Mich App 319, 332-333; 579 NW2d 101 (1998).

“It is not disputed that, under Michigan law, an organization has standing to advocate for the interests of its members if the members themselves have a sufficient interest.” *Lansing Schs Ed Ass'n v Lansing Bd of Ed*, 487 Mich 349, 373 n 21; 792 NW2d 686 (2010). Defendants concede that if the organizational plaintiffs represent public school employees, then they have standing. The plaintiffs each assert that they represent public school employees. Defendants complain that these plaintiffs have not produced evidence of their memberships. However, defendants do not provide any evidence to the contrary and it is plain that these plaintiffs represent public school employees. They have names such as “American Federation of Teachers – Michigan,” “Dearborn Federation of School Employees” and “Detroit Association of Educational Office Employees.” Certainly defendants have not demonstrated that they are entitled to judgment on this point as a matter of law.

III. RIPENESS

Defendants also argue that the substantive issues in these cases are not ripe for decision. “A claim is not ripe if it rests upon contingent future events that may not occur as anticipated, or indeed may not occur at all.” *Mich Chiropractic Council v Comm'r of the Office of Fin & Ins Servs*, 475 Mich 363, 371 n14; 716 NW2d 561 (2006), *rev'd on other grounds*, *Lansing Schs*, 487 Mich at 371 n18. Defendants argue that it is speculation to suggest that plaintiffs will fail to receive health care when they retire. However, plaintiffs have not brought a claim to require provision of health care benefits upon their retirement. Rather, plaintiff employees complain that *currently* three percent of their salaries are being withheld to pay for the healthcare of others, i.e. present school retirees. This Court addressed a similar situation in *AFSCME Council 25 v State Employees Retirement System*, 294 Mich App 1; ___ NW2d ___ (2011):

Although defendants characterize plaintiffs' claims as seeking relief from a hypothetical event, plaintiffs allege a current confiscation of their compensation without adherence to the provisions of Const 1963, art 11, § 5 and in violation of their CBA and contractual rights. Specifically, irrespective of the future availability of retiree health benefits to current employees, plaintiffs challenge the reduction in wages from November 1, 2010 through September 30, 2013. In light of the present reduction in compensation, defendants' challenge to jurisdiction by claiming that plaintiffs are raising a hypothetical scenario regarding events occurring upon their retirement fails.

See also *Haring Twp v City of Cadillac*, 290 Mich App 728; ___ NW2d ___ (2010), (holding that case was ripe because the township had declared its intent not to renew the contract at issue, despite the fact that future councils might still decide to renew the contract), aff'd 490 Mich 987 (2012).

Because defendants are confiscating three percent of plaintiffs' wages now, not at some hypothetical point in the future, this case is ripe for decision.

IV. IMPAIRMENT OF CONTRACT

The trial court concluded that MCL 38.1343e did not violate the contract clauses of the Michigan and United States Constitutions. US Const, art 1, § 10 and Const 1963, art 1, § 10 both prohibit the enactment of a statute that impairs a contract and the two provisions are interpreted similarly. *In re Certified Question*, 447 Mich 765, 776-777; 527 NW2d 468 (1994), cert den sub nom *Fun 'N Sun RV, Inc. v Michigan*, 514 US 1127; 115 S Ct 2000; 131 L Ed 2d 1001 (1999). The first step is to determine "whether the state law has, in fact, operated as a substantial impairment of a contractual relationship." *Id.*, quoting *Allied Structural Steel Co v Spannaus*, 438 US 234; 98 S Ct 2716; 57 L Ed 2d 727 (1978).

A. IMPAIRMENT OF PENSION BENEFITS

Plaintiffs argue that requiring present employees to acquiesce in the confiscation of three percent of their wages infringes on their right to receive their pensions. All parties agree that those pensions are accrued financial benefits under 1963 Const art 9, sec 24 and so may not be impaired. Plaintiffs essentially argue that because acquiescence in the three percent wage confiscation is a condition of employment, any refusal to do so may result in loss of employment and thus a loss, i.e. impairment, of pension benefits that would have been earned during continued employment. We reject this argument as it amounts to a claim that every condition of employment is subject to constitutional challenge simply because sanctions for failure to comply with such conditions may result in discharge and loss of potential pension benefits. Since prospective increases in pensions are not already accrued, this does not violate 1963 Const art 9, § 24.

B. IMPAIRMENT OF CONTRACTUALLY-SET WAGES

We agree with plaintiffs that MCL 33.1343e operates as a substantial impairment of the employment contracts between the plaintiffs and the employing educational entities. The contracts provide for a particular level amount of wages and the statute requires that the employers not pay the contracted-for wages, but instead pay 3 percent less than the contracts provide.⁴ We note that this is not a broad economic or social regulation that impinges on certain contractual obligations by happenstance or as a collateral matter. Rather, the statute directly and purposefully requires that certain employers not pay contracted-for wages. Such an action is unquestionably an impairment of contract by the state. “In the employment context, there likely is no right both more central to the contract’s inducement and on the existence of which the parties more especially rely, than the right to compensation at the contractually specified level.” *Baltimore Teachers Union, American Federation of Teachers Local 340, AFL-CIO v Mayor and City Council of Baltimore*, 6 F3d 1012, 1018 (CA 4, 1993). See also, *Buffalo Teachers Federation v Tobe*, 464 F3d 362, 370 (CA 2, 2006) (“Contract provisions that set forth the levels at which union employees are to be compensated are the most important elements of a labor contract. The promise to pay a sum certain constitutes not only the primary inducement for employees to enter into a labor contract, but also the central provision upon which it can be said they reasonably rely.”).

In *Baltimore Teachers*, the Fourth Circuit held that a temporary furlough plan under which employees lost .95 percent of their annual salary for one year constituted a substantial impairment of contract.⁵ The present case involves a reduction three times as great and in perpetuity, not merely for a single year. The plaintiffs have agreed to provide their labor and expertise to the school districts for wages bargained for and set forth in contract. For the state to mandate a 3 percent reduction in the contractually agreed-upon price of their labor is unquestionably a state impairment of contract.

That does not, however, resolve the constitutional question. In order to determine whether that impairment violates the Contract Clause, we must determine whether the state has shown that it did not: (a) “consider impairing the . . . contracts on par with other policy alternatives;” (b) “impose a drastic impairment when an evident and more moderate course would serve its purpose equally well,” nor; (3) act unreasonably “in light of the surrounding circumstances[.]” *Buffalo Teachers*, 464 F3d at 371, quoting *US Trust Co of New York v New Jersey*, 431 US 1, 30-31; 97 S Ct 1505; 52 L Ed 2d (1977). Put more generally, we are to

⁴ Defendants argue that plaintiffs failed to attach copies of their collective bargaining agreements to their pleadings. However, defendants do not dispute that plaintiffs *had* contracts that specified how much plaintiffs were to be paid by their respective districts. Indeed, defendants could not plausibly deny it.

⁵ The *Baltimore Teachers Union* court noted that “because individuals plan their lives based upon their salaries, we would be reluctant to hold that any decrease in an annual salary beyond one that could fairly be termed *de minimis* could be considered insubstantial.” *Id.* at 1018.

determine whether the particular impairment is “*necessary* to the public good.” *In re Certified Question*, 447 Mich at 777 (emphasis added).

In addressing these issues, we must consider that the employers in question are themselves governmental entities and that these entities will benefit as a result given that they are to use those monies as “employer contributions” that they would have otherwise had to pay to the retiree health care benefits fund.⁶ Because a governmental entity is party to the contract and benefits from the impairment, we are to employ heightened scrutiny in our review of the statute. *Buffalo Teachers*, 464 F3d at 370-371 (CA 2, 2006).

As a general rule, courts have found statutes impairing contractual obligations to be reasonable and necessary when the impairment is the consequence of remedial legislation intended to correct systemic imbalances in the marketplace. Such legislation may have positive or negative effects on particular economic actors and may in some cases result in altered contractual obligations without offending the Contract Clause. For example, we rejected a Contract Clause challenge in *Health Care Assoc Workers Compensation Fund v Bureau of Worker’s Compensation*, 265 Mich App 236; 694 NW2d 761 (2005), which involved a statute designed to unclog the marketplace for workers’ compensation insurance by eliminating unduly anti-competitive contractual provisions that punished employers for changing insurers. *Id.* at 242. Similarly, the U.S. Supreme Court held that correcting an imbalance between gas prices on the interstate and intrastate markets was a significant and legitimate state interest. *Energy Reserves Group, Inc v Kansas Power and Light Co*, 459 US 400, 417; 103 S Ct 697; 74 L Ed 2d 569 (1983). The present case, however, does not involve corrections to the marketplace to assure free competition.

We recognize that there are cases holding that a modest temporary impairment of government contracts may be imposed as a matter of last resort to address a fiscal emergency. However, as the cases relied upon by defendants show, such circumstances must be extraordinary and the degree of the impairment in amount and in time is central to the question whether the impairment passes constitutional muster. “The severity of the impairment measures the height of the hurdle the state legislation must clear.” *Allied Structural Steel Co v Spannaus*, 438 US 234, 245; 98 S Ct 2716; 57 L Ed 2d 727 (1978). As in *Allied Structural*, the statute at issue here works “a severe, permanent and immediate change in [contractual] relationships.” *Id.* at 250.

In *Baltimore Teachers* the city of Baltimore responded to sudden budget shortfalls caused by reductions in state aid of over \$37 million during the last three months of 1991 by imposing involuntary furloughs for city employees. 6 F3d at 1014. These furloughs were not conceived of as a long-term funding mechanism, but instead as a temporary response to a fiscal emergency. *Id.* at 1021. The furlough days resulted in Baltimore reducing annual salaries by less than one percent and only for a single year. Moreover, while the furloughs were involuntary, employees

⁶ According to the record, the 3 percent wage reduction will cover nearly 40 percent of the overall employer contributions for retiree health care benefits. (Affidavit of Phillip Stoddard, June 17, 2010).

were provided with reduced hours equivalent to the reduction in their wages. The Fourth Circuit held that while the actions constituted an impairment of contract, they did not violate the Contract Clause because the wage reduction was temporary, the amount of the resulting reduction in wages was no greater than necessary to meet the immediate budgetary shortfall and because the city had first taken other actions including a significant cut in city services and laying off employees. *Id.* at 1020.

MCL 33.1343e reduces public school employees' wages by an amount more than three times that which concerned the court in *Baltimore Teachers* and with no time off in exchange. More important, MCL 33.1343e is not a temporary measure. It provides that the salaries of public school employees will be *permanently* reduced by three percent of whatever they and their employers agree to. *Baltimore Teachers* allowed for a far more modest change and only on a temporary basis to address an immediate crisis. Here, the state imposed a permanent impairment on the most fundamental aspect of employment contracts and did so, not to deal with a short-term crisis, but as a long-term mechanism to restructure retirement benefit funding. Defendants presented no evidence to the trial court that other means of undertaking long term restructuring of retiree health benefit funding had been attempted or even reviewed. No proofs were offered as to why state interference with agreed-upon contracts was necessary where the state unequivocally asserts (and plaintiffs concede) that the state has the authority to reduce retiree health care benefits at anytime and in any fashion since under *Studier* those benefits are not protected as "accrued financial benefits." The state has not shown that it first undertook to reduce retiree health benefits, or to require present retirees to contribute to their own health care plans, or to restructure the benefits system in any way other than to legislate state-imposed modifications of freely-negotiated contracts.

Defendants also rely on *Buffalo Teachers* where the state imposed a temporary wage freeze preventing scheduled raises from going into effect which the court held "substantially impairs the workers' contracts with the City." 464 F3d at 368. As in *Baltimore Teachers*, the factors that led the court to uphold the wage freeze were: the temporary nature of the freeze; the fact that it did not reduce present wages, but only delayed increases, and fact that the imposition of the temporary freeze came only after the city had raised taxes and laid-off staff. *Id.* at 371-372. In this case, we are far from the facts that allowed the Baltimore and Buffalo actions to survive challenge.

Other courts have been unwilling to even go that far. In *University of Hawaii Professional Assembly v Cayetano*, 183 F3d 1096 (CA 9, 1999), the federal appeals court concluded that the state's action in delaying paydays by a few days, even without a reduction in the actual amount of pay, constituted a substantial impairment of contract where the timing of payment was part of the collective bargaining agreement. *Id.* at 1102-1104. As in *Baltimore Teachers* and *Buffalo Teachers* the *University of Hawaii* court noted the higher level of scrutiny applicable to legislative interference with governmental as opposed to private contracts and struck down the payday delays noting that "although perhaps politically more difficult, numerous other alternatives exist which would more effectively and equitably raise revenues" such as additional budget restrictions, the repeal of tax credits and the raising of taxes. *Id.* at 1107; see also, *Donohue v Paterson*, 715 F Supp 2d 306 (ND NY 2010).

Many courts have held that impairments of government employee contracts by the state that have indefinite or permanent application clearly violate the Contract Clause. *Oregon State Police Officers Association v State*, 918 P2d 765 (Oregon, 1996) (striking down a state statute that required public employees to contribute 6 per cent of their salaries to retiree benefits contrary to contract); *Opinion of the Justices*, 303 NE2d 320 (Mass, 1973) (striking down legislation increasing present employee contributions to retiree benefits without an increase in the subject employees own retirement benefits as “presumptively invalid” under the Contract Clause); *Singer v City of Topeka*, 607 P2d 467 (Kansas,1980) (statute mandating increase in public employee contributions to retirement plan without commensurate increase in benefits “is an unconstitutional impairment of contract rights.”); *Marvel v Dannemann*, 490 F Supp 170 (DC Del, 1980); *Hickey v Pension Board*, 106 A2d 233 (Penn, 1954); *Allen v City of Long Beach*, 287 P2d 765 (Cal, 1955).

For these reasons, we conclude that MCL 381.1345e violates US Const, art 1, §10 and Const 1963, art 1, §10.

II. TAKINGS CLAUSE

Plaintiffs argue that MCL 38.1343e violates the Takings Clause of the Fifth Amendment to the U.S. Constitution and Const 1963, art 10, § 2 each of which “prohibit the taking of private property for public use without just compensation.”⁷ Plaintiffs’ salaries are specific funds, in which plaintiffs unquestionably have a property interest. *Sims v United States*, 359 US 108, 110; 79 S Ct 641; 3 L Ed 2d 667 (1959) (“[I]t is quite clear, generally, that accrued salaries are property.”).

Clearly, the government has “taken” 3 percent of defendant’s wages in the dictionary definition sense of the word. The state does not dispute that the school districts are taking possession of wages that by contract belong to plaintiffs and sending them to state-mandated funds as *employer* contributions. The question, however, is whether this action constitutes a “taking” as it has been defined for purposes of the Fifth Amendment and its Michigan constitutional counterpart. We conclude that it does.

It is well settled that where government directly seizes property in which a person has a property interest, a Fifth Amendment taking occurs requiring that the government pay compensation. However, taking cases involving a direct seizure of property typically involves real property and the exercise of eminent domain. Taking jurisprudence also commonly deals with claims that governmental regulatory actions impose such limits on property use that it amounts to a taking.

Defendant argues that the confiscation or seizure of money as opposed to physical property cannot constitute a taking. Defendant points out that several courts have held that the general imposition of monetary assessments by the government does not raise Fifth Amendment

⁷ Because the two clauses are coextensive, we will simply refer to “the Takings Clause” for simplicity.

concerns. See, e.g., *McCarthy v City of Cleveland*, 626 F3d 280 (CA 6, 2010). The law is, however, equally clear that where the government does not merely impose an assessment or require payment of an amount of money without consideration, but instead asserts ownership of a specific and identifiable “parcel” of money, it does implicate the Takings Clause. Indeed, the U.S. Supreme Court has termed such actions “per se” violations of the Takings Clause. *Brown v Legal Foundation of Washington*, 538 US 216, 235; 123 S Ct 1406; 155 L Ed 2d 376 (2003). In *Brown*, the Court held that where the government asserted a right to control the interest on lawyer trust accounts, even where such amounts were de minimis, it constituted an unconstitutional taking. *Id.* We applied this principle in *Butler v State Disbursement Unit*, 275 Mich App 309; 738 NW2d 269 (2007) where we found an unconstitutional taking of property where the state disbursement unit that collects and disburses child support payments was depositing interest on the amounts awaiting disbursement into the state treasury. The amount in question was merely 83 cents and it could certainly be argued that the state could reasonably assess such a sum to pay for the collection service that benefited the children and custodial parent. However, because the money was part of definable and distinct parcel of money in which the eventual recipient had a property interest, it could not be taken without payment of just compensation.⁸

In *Webb’s Fabulous Pharmacies, Inc v Beckwith*, 449 US 155; 101 S Ct 446; 66 L Ed 2d 358 (1980) a Florida county court retained the interest from a fund in its custody intended for payment of Webb’s creditors. *Id.* at 156-158. The Supreme Court held that the Florida statute authorizing the retention of the interest “has the practical effect of appropriating for the county the value of the use of the fund for the period in which it is held.” *Id.* at 164. Further, the interest could not be treated as a fee for the use of the court because another statute specifically provided for a court fee based on the size of the fund deposited with the court. *Id.* at 164. “To put it another way: a State, by *ipse dixit*, may not transform private property into public property without compensation.” *Id.*⁹

⁸ In *Brown* the government was not required to pay compensation because the clients could not have earned any interest if they had deposited the funds on their own. 538 US at 239-240. Similarly, in *Butler* no compensation was ordered because the government’s administrative costs were greater than plaintiff’s accrued interest, and plaintiff’s net loss was therefore zero. 275 Mich App at 313.

⁹ In *Eastern Enterprises v Apfel*, 524 US 498; 118 S Ct 2131; 141 L Ed 2d 451 (1998) the plaintiff alleged that the Coal Industry Retiree Health Benefit Act of 1992 violated the Takings Clause because it required the plaintiff, to pay premiums into a fund to cover benefits for retirees it had not employed. 524 US at 503-504. The Supreme Court found this to be unconstitutional. Four of the Justices concluded that it violated the Takings Clause while Justice Kennedy reached his conclusion under the Due Process Clause. However, the concerns raised by Justice Kennedy as to the applicability of the Takings Clause do not arise in the instant case. In his concurrence, Justice Kennedy stated:

Defendants rely upon to two cases from the Federal Circuit Court of Appeals as support for their position, but neither case provides such support. In *Adams v United States*, 391 F3d 1212 (Fed Cir, 2004), the federal government concluded that certain federal law enforcement personnel were administrative employees and so not entitled to overtime pay under the Fair Labor Standards Act. The employees sued under the FLSA and also asserted that the government's failure to pay those sums constituted a taking. *Adams* held that an action to enforce payment of a statutory obligation for payment, unlike a *contract* for payment, does not establish a vested property right, without which a takings claim cannot arise. *Id.* at 1223. In *Adams*, the takings claim put the cart before the horse by arguing that failure to pay overtime constituted a taking before any right to that overtime was determined to exist. *Id.* at 1221-1222. This is not so here as it is undisputed that plaintiffs have a contract-based property right in their own wages.

Kitt v United States, 277 F3d 1330, 1336-1337 (Fed Cir, 2002), is similarly inapposite as it involved only a general obligation to pay money under a disputed provision of the tax code. The government did not assert ownership of any particular property and the court relied on that very point to reject the takings claim, noting that “[i]n some situations money itself may be subject of a taking, for example, the government’s seizure of currency or its levy upon a bank account. . . . In the present case, however, the government did not seize or take any property of the Kitts. All it did was to subject them to a particular tax to which they previously had not been subject. That government action did not constitute a taking of the amount of the tax they had to pay.” *Id.* at 1337.

Defendants lastly submit that the Takings Clause is not applicable because the plaintiffs seek to invalidate MCL 38.1343e instead of seeking compensation for lost property. Defendant cites *Eastern Enterprises* for this proposition, but only Justice Kennedy made such a statement. 524 US at 545 (Kennedy, J., concurring). Further, the Supreme Court in *Webb’s* held a Florida statute unconstitutional under the Takings Clause. It appears that the defendants are arguing that rather than striking down the statute, we are limited to ordering that the confiscated wages be paid back in full as compensation. This unsupported view would require that we approve the continued taking of employees’ wages by the government, but require the government to promptly return identical amounts (with interest) to those same employees. We decline to adopt this absurd and costly remedy.

The Coal Act does not appropriate, transfer, or encumber an estate in land . . . a valuable interest in an intangible . . . *or even a bank account or accrued interest*. The law simply imposes an obligation to perform an act, the payment of benefits. The statute is indifferent as to how the regulated entity elects to comply *or the property it uses to do so.*” (emphasis added).

That is by no means the case here. MCL 38.1343e confiscates a specific fund, i.e. plaintiffs’ paychecks, and removes 3 percent of the property before allowing plaintiffs to take possession of their property.

Because MCL 38.1343e takes private property without providing any form of compensation, the trial court correctly ruled that the statute violates the Takings Clause of the Fifth Amendment and Const 1963, art 10, § 2.

III. SUBSTANTIVE DUE PROCESS

We also affirm the trial court's conclusion that MCL 38.1343e is unconstitutional under the Due Process Clause of the Fourteenth Amendment and Const 1963, Art 10, §2.

The Fourteenth Amendment to the United States Constitution and the Const 1963, art 1, § 17 guarantee that no state shall deprive any person of "life, liberty or property, without due process of law." Textually, only procedural due process is guaranteed by the Fourteenth Amendment; however, under the aegis of substantive due process, individual liberty interests likewise have been protected against certain government actions regardless of the fairness of the procedures used to implement them. The underlying purpose of substantive due process is to secure the individual from the arbitrary exercise of governmental power. [*People v Sierb*, 456 Mich 519, 522-523; 581 NW2d 219 (1998) (internal quotations omitted)].

"The essence of a claim of violation of substantive due process is that the government may not deprive a person of liberty or property by an *arbitrary* exercise of power." *Landon Holdings, Inc v Grattan Twp*, 257 Mich App 154, 173; 667 NW2d 93 (2003) (emphasis in original).¹⁰

Defendants argue that the compelled contributions are not arbitrary because they are assessed against public school employees to support a fund that pays for retiree healthcare for public school employees. This, however, is an overly-general characterization that gives the false impression that the plaintiff employees are being required to contribute toward the funding of their own retirement benefits. The mandatory contributions imposed on current public school employees, do not go to fund their own retirement benefits, but instead to pay for retiree healthcare for already-retired public school employees.

While present employees and retired employees share a common employer, that does not mean that their interests as individuals (or even as groups of employees) are identical. Defendants have offered no legal basis for the conclusion that it comports with due process to require present school employees to transfer three percent of their incomes in order to fund retirement benefits of others. Rather, it is a mandatory direct transfer of funds from one discrete group, present school employees, for the benefit of another, retired school employees. The fact

¹⁰ Defendants argue that plaintiffs must show government action that shocks the conscience, but that standard applies only to executive, not legislative action. See *County of Sacramento v Lewis*, 523 US 833, 849; 118 S Ct 1708; 104 L Ed 2d 1043 (1998) ("[F]or half a century now we have spoken of the cognizable level of *executive* abuse of power as that which shocks the conscience.") (emphasis added).

that these groups share employers does not render the scheme outside the constitutional protection of substantive due process.

Defendants' seek to blur the issue by repeatedly arguing in their briefs that it is only fair for those who receive a healthcare benefit to help pay for it.¹¹ This principle, however, is as irrelevant as it is self-evident. As noted, the statute does not provide that the monies obtained by involuntary collection of three percent of the workers' wages will be used to fund the retiree health care benefits of those whose wages are being taken.

In *Studier v Michigan Public School Employees' Retirement Board*, 472 Mich 642; 698 NW2d 350 (2005) our Supreme Court made clear that public school retiree health care benefits do not constitute "accrued financial benefits" and so are not subject to Const 1963, art 9, section 24. The first clause of that provision provides that

the accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby.

¹¹ See, e.g. defendant-appellant's brief at p 1 ("[i]n exchange [for payment of 3% of their income], the Trust fund *will pay* for the cost of health care for . . . Plaintiff-Appellee's when they retire" [emphasis added]); p 14, ("[plaintiffs] are simply being required to pay for a *future benefit*" [emphasis added]); p 18 ("Since Plaintiffs . . . *are the beneficiaries* of paid [retiree] health care, it is only fair that they help pay a portion of its costs"); p 19 ("Once individual plaintiffs retire, they *will* receive the benefit of [their] contributions." [emphasis added]); p 20, (MCL 38.1343e is a rational attempt to impose a portion of the cost of retiree health care on those who. . . *will receive* those very health care benefits when they retire." [emphasis added]); p 26, it is proper to "require[e present employees] to contribute to the cost of the health care that they *will receive* when they retire." [emphasis added]; p 27 ("It is only fair that those who receive a health care benefit should have to help pay for it."); p 30 ("it is only fair and reasonable for those who *will benefit* from health care coverage to have to pay for a portion of its costs." [emphasis added]). Defendant-cross-appellant's brief similarly states: p 3, "Once Plaintiffs retire, their health care costs . . . will be paid from the assets in this fund"); p 17 ("Plaintiffs will receive health care benefits when they retire in exchange for their contributions"); p 22 ("Plaintiffs will receive health care when they retire in exchange for their contributions").

At the same time, however, defendant-cross-appellee's brief repeatedly affirms the state's position that it has no obligation to pay health care benefits to the plaintiffs upon their retirement: p 1 ("no contract exists that requires the payment of retiree health care costs . . . providing for health care benefits for public school retirees does not create a contractual right"); p 25 ("[Plaintiff] asserts that MCL 38.1343e impairs an 'accrued financial benefit' because they are required to pay 3% of their compensation. However, retiree health care is not an 'accrued financial benefit'"); p 26 ("MCL 38.1391 did not create a contract which require[s] MPSEERS to provide retiree health care"); p 27 ("Plaintiffs do not have a contract to receive health care when they retire").

Since this clause does not apply to retiree health care benefits, the state has no contractual obligation to provide present state employees with such benefits and employees have no enforceable or vested right to receive such benefits. As a legal matter, an unenforceable promise is no promise at all.

Under *Studier*, the second clause of the provision mandating that benefits be paid for in the year they are accrued¹² is also not applicable to retiree health care benefits. Thus, the 3 percent of wages withheld do not go to pre-fund present employees' own benefits. Moreover, these employees are not possessed of any right to receive such benefits, however paid for, upon their own retirement.

We cannot envision a court constitutionally approving a statute that requires certain individuals to turn a portion of their wages over to the government in return for a "promise" that the government will return the monies with interest in twenty years where the government retains the unilateral right to "cancel" the "promise" at any time and will not even agree that if they do so, the monies taken will be returned. School employees cannot constitutionally be required to "loan" money to their employer school districts,¹³ with no enforceable right to receive anything in exchange and without even a legal guarantee assurance that the "loan" will be repaid.

Defendants argue that the present case is analogous to *Michigan Manufacturers Assoc v Director of Workers' Disability Compensation Bureau*, 134 Mich App 723; 352 NW2d 712 (1984), where this Court upheld a statute requiring all employers in the state to contribute to a fund that helped defray the costs of workers' disability for the logging industry. However, that case considered only whether the statute was enacted for a proper purpose and did not address whether it met the second prong of the constitutional test. *Id.* at 733-735. Moreover, the statute related to the broad policy objectives of the worker compensation system that effects every worker and employer in the state. Workers compensation was adopted 100 years ago to create a system of risk sharing and limited, but prompt, compensation of injured workers. In addition to obtaining general insurance or to self-insure, all employers in the state may be required to contribute to specialized funds such as the second injury fund, the silicosis and dust fund and the self-insurers' security fund. MCL 418.551. These assessments are part of a state-wide economic regulatory system and contributions to the funding of that system are required of all employers in the state. The statute in *Michigan Manufacturers* represented a small modification in an overall system of risk-sharing intended to assure stability in the industrial marketplace.

The instant case is wholly different. Payment of health care benefits owed by the government to a particular set of its retired employees is not analogous to the maintenance of a statewide risk-sharing system to assure market and economic stability for the private sector.

¹² "Financial benefits arising on account of service rendered in each fiscal year shall be funded during that year and such funding shall not be used for financing unfunded accrued liabilities." Const 1963, art 9, § 24.

¹³ We reiterate that the wages appropriated from employees are defined as "employer contributions" to the fund.

Rather, it is a question of the government meeting a particular set of its own fiscal obligations. Here, the government seeks to do so by requiring a small subset of Michigan's population to surrender 3 percent of their wages, above and beyond that which they pay in taxation, with no guarantee of anything in return, to meet the government's obligation to other individuals. Defendant posits no evidence or even argument to suggest that the funding of these retirement benefits cannot be satisfied by measures that do not raise due process concerns.¹⁴ We stress that the mechanism defined in MCL 38.1343e is *neither* general taxation for a general fund with specific uses of the monies later determined by the legislature nor a fee for service to the payee. Nor is it a requirement that individuals fund benefits they themselves have a vested right to receive. The statute instead provides that the government confiscate the income of one discrete group in order to fund a specific government obligation to another discrete group. The fact that the members of one of these groups work for the same entities from which the members of the other group retired does not provide a rational basis to mandate what amounts to a direct transfer of income. MCL 38.1343e is thus unreasonable, arbitrary and capricious, and violates the Due Process Clause.

VI. CONCLUSION

We are not unmindful of the budgetary challenges facing local school districts and Michigan's institutions of higher education. Moreover, we recognize that the State Legislature is within its authority to adopt legislation to aid these entities as they seek to address those budgetary challenges. In exercising that authority, however, the Legislature remains constrained by the state and federal Constitutions and the rights they guarantee. MCL 38.1343e violates multiple provisions of these Constitutions. Accordingly, we affirm the trial court's orders granting summary disposition in favor of plaintiffs in each of the cases before us, terminate the stay ordered by this Court on March 18, 2011, and remand for further proceedings consistent with this opinion. We do not retain jurisdiction.

/s/ Douglas B. Shapiro

/s/ Jane M. Beckering

¹⁴ We offer no opinion as to what funding choices would best fulfill the policies chosen by the legislature, but note that the parties agree that such choices exist. The state always retains the authority to modify general taxes and it is not disputed that under *Studier* retiree health care benefits may be modified or reduced by statute. It would also seem that the constitutional defects in the 3 percent wage assessment could be addressed by adopting legislation categorizing retiree health care benefits as "accrued financial benefits."