

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV 2017-001200

07/20/2017

HONORABLE TIMOTHY J. THOMASON

CLERK OF THE COURT
K. Ballard
Deputy

KENNETH FIELDS, et al.

COLIN F CAMPBELL

v.

ELECTED OFFICIALS RETIREMENT PLAN,
THE, et al.

BENNETT EVAN COOPER

CHARLES A GRUBE

UNDER ADVISEMENT RULING

FINDINGS OF FACT

1. Plaintiff, the Honorable Kenneth Fields, is a retired judge of the Superior Court, State of Arizona. He is an Arizona resident. He retired as a state court judge in June 2007. Plaintiff, the Honorable Gerald Porter, is a retired judge of the Superior Court, State of Arizona. He retired as a state court judge in June 2015. (Judge Fields and Judge Porter are collectively referred to as the "Plaintiffs".)

2. As retired judges, Plaintiffs are fully vested members in the Elected Officials Retirement Plan ("EORP" or the "Plan"), a defined benefits plan for judges and other elected officials created by Arizona statutes.

3. The Defendant EORP is a defined benefit plan and a jural entity under Arizona law, which can sue and be sued. Its principal offices are in Maricopa County, Arizona.

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4. Prior to legislative changes made in 2013 session laws, employer contributions to the EORP were set and made based on actuarial methods and assumptions consistent with generally accepted accounting standards. Then existing A.R.S. § 38-810(C) stated:

As determined by actuarial valuations performed by the plan's actuary, each employer shall make level per cent compensation contributions sufficient under the actuarial valuation to meet both the normal cost plus the actuarially determined amount required to amortize the unfunded accrued liability over a rolling period of at least twenty and not more than thirty years that is established by the board taking into account the recommendation of the plan actuary

5. In the 2013 regular session, the legislature passed and on June 19, 2013, the Governor signed House Bill 2608, codified as Laws 2013, chap. 217, § 6. It modified EORP statutes in several ways. As of January 1, 2014, newly elected officials would no longer become members of EORP; instead, there is a new defined contribution plan available for those elected officials not entitled to remain members of the Arizona State Retirement System. A.R.S. § 38-804(J). Also beginning on January 1, 2014, each EORP employer must "make level per cent compensation contributions of twenty-three and one-half per cent of the compensation of all employees of the employer who are either members under this article, article 3.1 of this chapter or article 2 of this chapter pursuant to [A.R.S. § 38-727(B)] to meet the normal cost plus an amount to amortize the unfunded accrued liability. . . ." A.R.S. § 38-810(C). For each fiscal year beginning 2013-2014 until 2042-2043, the legislature appropriated an additional five million dollars per year to supplement the normal cost and amortize the unfunded accrued liability. A.R.S. § 38-810(I). The bill provides that beginning July 1, 2044, the employers shall make level per cent contributions sufficient to pay both the normal cost and the unfunded accrued liability over a rolling period of between 20 and 30 years as set by the board. A.R.S. § 38-810(D).

6. The Board of Directors of EORP retained Gabriel Roeder Smith & Company ("Gabriel Roeder") to prepare a consolidated report on the EORP plan. Gabriel Roeder prepared a report dated November 29, 2016.

7. The Gabriel Roeder report calculated, for the 2017–2018 plan year, the employer contribution rate for EORP using actuarial methods and assumptions that are consistent with generally accepted accounting standards.

8. The Gabriel Roeder report concluded that the employer contribution rate for the fiscal year beginning July 1, 2017, and ending June 30, 2018, should be 106.55% of aggregate payroll. The Gabriel Roeder report does not include in its calculation judicial fees paid to the

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EORP or a \$5,000,000 general fund contribution to the EORP paid annually by the State of Arizona.

9. After taking into account a \$10,000,000 payment for judicial fees and the annual \$5,000,000 payment by the State of Arizona, Gabriel Roeder concluded that the employer contribution rate to the EORP, based on actuarial methods, should be 53%.

10. Gabriel Roeder actuary James Anderson acknowledged in his deposition that the 106.55% rate would only apply if one used only the EORP members' salaries as the basis, not the wider pool of salaries authorized by the 2013 statute. (Anderson Dep. at 61-63) If the wider pool were used, the rate would only be 53.7%. (*Id.*) In the alternative, the legislature could keep the 23.5% employer contribution rate, but would need to add 43 million additional dollars, including the 15 million dollars already provided in court fees and the lump sum annual appropriation. (*Id.* at 53-54)

11. Mr. Anderson made it very clear that the use of a flat rate for employer contributions is not a problem in and of itself; instead, the actuarial concern is when the flat rate plus additional revenue falls short. (Anderson Dep. at 53, lines 2-4) He conceded that a flat rate contribution plan can be operated consistently with generally accepted actuarial standards. (*Id.* at 59, lines 20-23) He also acknowledged that the amounts necessary to fund the ongoing operations of the Plan could be paid by any combination of methods and still meet appropriate standards of actuarial funding. (*Id.* at 66, lines 2, 8-67) Anderson also testified that a different actuary might come to somewhat different conclusions about the required amounts. (*Id.* at 66, lines 2-7) He also confirmed that the EORP is presently paying all benefits on time and he is not aware of any plan to stop paying them. (*Id.* at 63, lines 19, 24-64)

12. The Gabriel Roeder 2016 report concluded that "it is most important that this Plan receive contributions at least equal to the rates shown in this report." (emphasis in original report) The Gabriel Roeder report concluded that "if contributions are not increased, assets are likely to be depleted in the next 13 years."

13. Jared Smout, the administrator for the EORP, testified that, if the statutory cap on employer contributions is not lifted, then the EORP will likely run out of money at some point in time in the not too distant future. The Court concludes that if the statutory funding mechanism is not changed, EORP will run out of money within the next fifteen years, at the most, and possibly within ten years.

14. Since the statutory cap on employer contribution rates was instituted, the EORP has asked the State legislature each year to lift the cap and allow EORP to set the employer contribution rate by actuarial means and methods. The legislature has not done so.

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CONCLUSIONS OF LAW

1. Plaintiffs have standing to bring their claims for declaratory and injunctive relief because there is a current, definite, and justiciable controversy before the Court: does the statutory cap of employer contributions implemented by the legislature when it amended A.R.S. § 38-810 violate the Arizona Constitution and breach the State's contracts with EORP beneficiaries?

2. Arizona courts are not "constitutionally constrained to decline jurisdiction based on lack of standing." *Sears v. Hull*, 192 Ariz. 65, 71 ¶ 24, 961 P.2d 1013, 1019 (1998). Instead, standing in Arizona is a purely prudential concern. It is therefore well within this Court's discretion to grant jurisdiction where, as here, Plaintiffs raise an issue of great public importance that is likely to recur every year until the state's unconstitutional statute is corrected. *Goodyear Farms v. City of Avondale*, 148 Ariz. 216, 217 n.1, 714 P.2d 386, 387 n.1 (1986).

3. "Arizona's Uniform Declaratory Judgments Act (the "Act"), A.R.S. §§ 12-1831 through 1846, is an 'instrument of preventive justice' that allows a court to determine a person's 'rights, status or other legal relations' . . . *before* the occurrence of a breach or injury necessary to sustain a coercive action (one seeking damages or injunctive relief)." *Canyon del Rio Inv'rs, L.L.C. v. City of Flagstaff*, 227 Ariz. 336, 341 ¶ 18, 258 P.3d 154, 159 (Ct. App. 2011) (citations omitted) (emphasis added); *see also Elkins v. Vana*, 25 Ariz. App. 122, 126, 541 P.2d 585, 589 (1975) ("An action for a declaratory judgment is intended to serve as an instrument of preventive justice, to relieve litigants of the common law rule that no declaration of right may be judicially adjudged until that right has been violated, and to permit adjudication of rights or status without the necessity of a prior breach.").

4. "The declaratory judgments act is interpreted liberally." *Keggi v. Northbrook Prop. & Cas. Ins. Co.*, 199 Ariz. 43, 45 ¶ 10, 13 P.3d 785, 787 (Ct. App. 2000) (reversing trial court's conclusion that the plaintiff lacked standing under the Act). A controversy is justiciable under the Act when "there is 'an assertion of a right, status, or legal relation in which the plaintiff has a definite interest and a denial of it by the opposing party.'" *Id.*, quoting *Samaritan Health Servs. v. City of Glendale*, 148 Ariz. 394, 395, 714 P.2d 887, 888 (Ct. App. 1986) (finding a justiciable controversy where a hospital sought preemptive declaration of its duty to assert the physician-patient privilege).

5. Plaintiffs are in danger of suffering actual financial harm because of the shortfall in EORP funding.

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6. A.R.S. § 12-821 applies to “(a)ll actions against any public entity...” Despite the fact that A.R.S. § 12-821 is included in a set of statutes that appear to deal with actions for damages, that statute itself applies to “all actions...” As such, the Court concludes that statute applies to the present case, despite the fact that it is a claim for declaratory and injunctive relief. *See Flood Control Dist. of Maricopa Cty. v. Gaines*, 202 Ariz. 248, 43 P.3d 196 (Ct. App. 2002). The statute of limitations for declaratory judgment claims is the relevant analogous limitation period for the underlying claim. *La Canada Hills Ltd. P’ship v. Kite*, 217 Ariz. 126, 129, 171 P.3d 195, 198 (Ct. App. 2007).

7. The cause of action, however, does not accrue until a person realizes that the person has been damaged and knows or reasonably should know the act or event that caused or contributed to the damage. *Mayer Unified Sch. Dist. v. Winkleman*, 219 Ariz. 562, 566, 201 P.3d 523, 527 (2009). The State contends that the cause of action here accrued when the statute was passed in 2013. Plaintiffs, however, did not suffer any actual damage when the statute was passed. In fact, the State argued at trial that the EORP was fiscally sound when the statute was passed in 2013. (*See* Trial Br. 4:11) The State also argued that Plaintiffs have still suffered no damage as of the time of trial. As such, the cause of action did not accrue when the statute was passed.

8. Plaintiffs’ claim is not barred by the statute of limitations. The November 29, 2016 Gabriel Roeder report showed the possibility of actual harm in the future. The Complaint was filed promptly thereafter. As explained above, a declaratory judgment may issue before a breach, resulting in damages. No showing has been made that Plaintiffs were damaged more than one year before the filing of the Complaint.

9. Under the Arizona Constitution, Article 29, Section 1(C)-(D), “membership in a public retirement system is a contractual relationship that is subject to Article II, § 25” [no law impairing the obligation of contract shall ever be enacted]...and “public retirement system benefits shall not be diminished or impaired...” Ariz. Const. art. XXIX, § 1 (C)-(D) (2016). This Arizona Constitutional provision is consistent with a long history of Arizona Supreme Court cases that have held that Arizona pension plans fall under the “impairment of contract” protections of the Arizona Constitution. Accordingly, under Arizona law, Plaintiffs’ benefits under EORP are based on a contractual relationship between Plaintiffs and the State of Arizona and Plaintiffs’ benefits cannot be impaired or diminished.

10. Under the Arizona Constitution, Article 29, Section 1(A), “[p]ublic retirement systems shall be funded with contributions and investment earnings using actuarial methods and assumptions that are consistent with generally accepted accounting standards.” Ariz. Const. art. XXIX, § 1 (A). The requirement that contributions be set based upon actuarial methods and assumptions that are consistent with generally accepted accounting standards is an Arizona

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constitutional requirement and forms part of the contract between Plaintiffs and the State of Arizona.

11. The EORP administers a pension contract between Plaintiffs and the State of Arizona which incorporates by law the requirements of the Arizona Constitution.

12. In *Hall v. Elected Officials' Retirement Plan*, the Supreme Court held, among other things, that the State of Arizona could not unilaterally raise the employee contribution rate to the EORP. Based upon judicial precedent, the Court stated:

[T]he law in Arizona has been clear since 1965 that public employees are contractually entitled to the retirement benefits specified in their initial employment contract. This protected relationship prevents the legislature from changing the employee's pension terms at will after the terms have vested, and provides public employees reasonable expectations that their retirement benefits are protected by the law of contracts. The parties may subsequently agree to modify the contract, of course, but the State may not unilaterally change the contractual terms unless the change benefits the employee.

Hall v. Elected Officials' Ret. Plan, 241 Ariz. 33, 40 ¶ 20, 383 P.3d 1107, 1114 (2016) (citations omitted). The *Hall* Court held that the statutory contribution rate made by employees, 7% of their pay, was a part of the employment contract with the State of Arizona, vested on the first day of employment, and that the statutory contribution rate could not be unilaterally changed by the State of Arizona. *Id.* at 41 ¶ 23, 383 P.3d at 1115 (“[A]n increase in the Class Members’ proportionate share of the contribution rate above 7% and the change in the statutory formula granting permanent benefit increases without the Class Members’ consent are breaches of that contract and infringe upon the Class Members’ contractual relationship with the State.”).

13. The *Hall* Court also noted that the statutory provisions of the Plan for setting the employer contribution rate ensures the economic soundness of the Plan and places the risk of increased contributions on the employer:

[T]he Plan’s actuarial soundness is within the Legislature’s control. The Legislature is responsible for setting the amounts of the employer contributions and court filing fees, *see* A.R.S. § 38-810 (B)–(D), and the Legislature may not “reduce the amount of the contributions to the fund if thereby the soundness of the fund is jeopardized,” *Yeazell*, 98 Ariz. at 116, 402 P.2d at 546. If the Plan is underfunded because the inadequate investment returns, the State may increase employer contributions and filing fees.

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Hall, 241 Ariz. at 42 ¶ 26, 383 P.3d at 1116. When investment returns are inadequate to ensure the soundness of the plan, “the State’s funding obligation is necessarily increased.” *Id.* at 42 ¶ 27, 383 P.3d at 1116.

14. Under the “new” statute, the State is evading its constitutional obligations to fund the EORP and to actuarially set the employer contribution rate:

The reward and risk of investment returns falls on the State. This is simply the nature of defined benefit plans. *See Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 439 (1999) (stating that in a defined benefit plan “the employer typically bears the entire investment risk” and “must cover any underfunding as the result of a shortfall that may occur from the plan’s investments”). Because the State bears the risk of the claimed mistake, the State cannot rely on the defense of mutual mistake of fact to justify changes to the Plan.

Id. at 42 ¶ 27, 383 P.3d at 1116. The State contends that the EORP was actuarially sound when the 2013 statute was passed and implemented and that financial issues only developed later, after subsequent Court decisions found other statutory changes to be unconstitutional. That is not a defense. As noted above, the State bears the risk and must cover any underfunding. “Mistake of fact” is simply not a viable defense.

15. Part of Plaintiffs’ contract with the State is to have employer contributions placed at sufficient levels, under actuarial valuations, to meet the normal cost plus the actuarially determined amount required to amortize the unfunded accrued liability over 20-30 years. In addition, the Constitution requires that EORP be funded with contributions using “actuarial methods and assumption that are consistent with generally accepted accounting standards.” Ariz. Const. art. XXIX, § 1(A). The 2013 legislative changes violate Plaintiffs’ contract and the Constitution.

16. The prior statute required that employer contributions had to be made in an actuarially appropriate amount, based on actuarial valuations performed by the Plan’s actuary. This element of the pension arrangement was a contractual benefit that became part of the public pension contract. Setting the employer contribution at a specific rate, without providing for other necessary funding sources, improperly modified the employment contract and was prohibited by the Arizona Constitution.

17. The Arizona statute that sets employer contribution rates at 23.5%, without providing for alternate appropriate sources of funding, violates the constitutional requirement that funding be based on contribution rates and earnings based on actuarial methods and assumptions that are consistent with generally accepted accounting standards.

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18. The State's contention that the new funding mechanism is a "benefit" to EORP members is wrong. Specifically, the State contends that the 2013 statute benefitted members by basing employer contributions on a larger pool of employees. This one piece of the new statute can be seen as a benefit, in a vacuum. The new statute as a whole, however, was not a benefit to EORP members. The prior statute ensured that EORP was financially sound by requiring employer contributions to be set at a level to ensure that the cost and unfunded liability would be paid. The new statute, however, by setting employer contributions at a set level, does not ensure that the cost and unfunded liability will be paid. In fact, it is undisputed that the current levels of funding are insufficient to meet the actual cost and unfunded liability. Accordingly, the EORP is not being funded with contributions and earnings according to actuarial methods consistent with generally accepted accounting standards. This is hardly a "benefit" to EORP members.

19. The denial of Plaintiffs' constitutional rights under Article 29 is an irreparable and immediate injury.

20. It is evident to the Court that the current statute is unconstitutional. As written, the statute does not provide any assurance that EORP is funded with contributions and investment earnings using actuarial methods and assumptions that are consistent with generally accepted actuarial standards, as required by the Constitution. The Court orders that the State of Arizona must, as early as reasonably possible, set the employer contribution rates and other funding for EORP, as a whole, based on actuarial methods and assumptions that are consistent with generally accepted accounting standards. The State is not constrained by the contribution cap in the 2013 legislation, which is unconstitutional. *TP Racing, L.L.P. v. Simms*, 232 Ariz. 489, 495, 307 P.3d 56, 62 (Ct. App. 2013) ("An injunction may serve to undo accomplished wrongs, or to prevent future wrongs that are likely to occur.")

21. It is the Court's function to ensure that whatever measure the legislature enacts to address the problem comport with the Arizona Constitution. *Hall v. Elected Officials' Ret. Plan*, 241 Ariz. 33, 43, 383 P.3d 1107, 1117 (2016). The capping of employer contribution rates at 23.5% is unconstitutional, given the other sources of funding (or lack thereof) currently set forth in the law.

22. The Court is not improperly invading the legislature's authority. This Court defers to the legislature in developing specific methods to ensure that EORP contribution rates and other funding mechanisms are based on actuarial methods and assumptions that are consistent with generally accepted accounting standards.

23. The State acknowledged that adjustments need to be made to EORP. (State's Trial Br. at 5) Indeed, the State explicitly stated that the legislature is prepared to address this problem at the earliest feasible time. As such, the State conceded, as it must, that the current

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state of EORP is not actuarially sound. Rather, the State contended that the Court should do nothing and presume that the legislature will “fix” the problem. As mentioned above, however, it is the Court’s function to determine if the legislature is complying with the Constitution. The Court would be shirking its responsibility if it sat idly by and presumed that the legislature will promptly “fix” the problem.

24. The Court is not going to “pontificate” about the specifics about how to “fix” the problem. That will be up to the legislature. The current funding mechanism, however, is unconstitutional and needs to be resolved promptly.

25. There may be a myriad of ways to resolve the problem. One of them may be keeping the current employer contribution rate at the present level and finding other sources of funding that would render the current employer contribution rate to be consistent with a rate set based on actuarial methods and assumptions that are consistent with generally accepted accounting standards. For example, the actuaries have calculated the amount of money necessary to fund EORP in an actuarially sound manner if contributions are maintained at the 23.5% level. (Ex. 22—EORP 399) The Court fully understands that employer contributions are not the only funding mechanisms for EORP. The legislature can certainly decide, if it so chooses, to “fix” the problem, in accordance with Constitutional mandates, by keeping the 23.5% level, as long as additional funding, through a supplemental appropriation, is provided to ensure that EORP is funded at an actuarially sound level.

26. As noted above, the State acknowledges that adjustments will have to be made to EORP funding and that the legislature needs to act. Therefore, the Court’s ruling, as detailed above, should not be controversial. The State assured the Court during trial that the legislature is prepared to act. As such, this Court declines to stay its ruling pending appeal.

27. Plaintiffs have vindicated a right that benefits a large number of people, requires private enforcement, and is of societal importance. Plaintiffs are entitled to at least some of their reasonable costs and attorneys’ fees under the private attorney general doctrine and A.R.S. § 12-341.01. A “China Doll” affidavit shall be submitted within **10 days** from this Order. A response may be filed **10 days** thereafter. There will be no reply.