S T A T E   O F   M I C H I G A N

C O U R T   O F   A P P E A L S

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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Plaintiffs-Appellees,

v

STATE OF MICHIGAN,

Defendant-Appellant.

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

Advance Sheets Version

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,

Advance Sheets Version

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

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

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,

Advance Sheets Version

and

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

Defendants.

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

SHAPIRO, P.J.

In these three cases consolidated for 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, MCL 38.1341 *et seq*., which governs the Michigan Public School Employees Retirement System (MPSERS), MCL 38.1321. 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 MPSERS as "employer contributions" 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 the impairment of contracts by the state and 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 percent[2] less than the amount they and their employers freely agreed on in contracts. The prohibition against the taking of private property is violated because 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 plaintiff employees have a property interest be confiscated by their governmental employers. Moreover, the confiscated wages are then used to pay the statutorily mandated *employers'* contributions to a state fund. Finally, while the fund in question funds health care benefits for present retirees, the active employees whose wages are taken have no vested right themselves to the receipt of health care 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

[1] These include intermediate school districts, public school academies, tax-supported community or junior colleges and 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.*

> 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 \$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.

A 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 Michigan Pub Sch Employees' Retirement Bd*, 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 their employees' wages for remittance as employer contributions to the MPSERS. Plantiffs brought suits 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 or partial 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, holding that they had standing to challenge the statute. It also rejected defendants' assertion that the claims were not ripe for review.

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[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 thereof which shall not be diminished or impaired thereby."

With regard 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 the 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 Docket 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 was 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 Sch 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 organizational plaintiffs 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 "AFT Michigan" (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 Office of Fin & Ins Servs Comm'r*, 475 Mich 363, 371 n 14; 716 NW2d 561 (2006) (quotation marks and citations omitted), overruled on other grounds by *Lansing Sch*, 487 Mich at 371 n 18 (2010). Defendants argue that it is speculation to suggest that plaintiff employees will fail to receive health care benefits when they retire. However, plaintiff employees have not brought a claim to require the 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 health care of others, i.e. present school retirees. This Court addressed a similar situation in *AFSCME Council 25 v State Employees' Retirement Sys*, 294 Mich App 1, 7-8; 818 NW2d 337 (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 [collective-bargaining agreement] 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' jurisdictional challenge claiming that plaintiffs are raising a hypothetical scenario regarding events that may occur upon their retirement fails.

See, also, *Haring Charter Twp v City of Cadillac*, 490 Mich 987 (2012) (holding that the case was ripe for decision because the city had declared its intent not to renew the contracts at issue, despite the fact that future city councils might still decide to renew the contracts), aff'g *Haring Charter Twp v City of Cadillac*, 290 Mich App 728 (2010).

Because defendants are confiscating three percent of plaintiff employees' 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 I, § 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). The first step is to determine "'whether the state law has, in fact, operated as a substantial impairment of a contractual relationship.'" *Id.* at 777, quoting *Allied Structural Steel Co v Spannaus*, 438 US 234, 244; 98 S Ct 2716; 57 L Ed 2d 727 (1978).

A. IMPAIRMENT OF PENSION BENEFITS

Plaintiff employees 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 Const 1963, art 9, § 24 and, therefore, 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 because 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 from employment and loss of potential pension benefits. Because prospective increases in pensions are not already accrued, this does not violate Const 1963, art 9, § 24.

B. IMPAIRMENT OF CONTRACTUALLY SET WAGES

We agree with plaintiffs that MCL 38.1343e operates as a substantial impairment of the employment contracts between plaintiffs and the employing educational entities. The contracts provide for a particular amount of wages and the statute requires that the employers not pay the contracted-for wages, but instead pay three 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 Baltimore Mayor & City Council*, 6 F3d 1012, 1018 (CA 4, 1993). See, also, *Buffalo Teachers Federation v Tobe*, 464 F3d 362, 368 (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 United States Court of Appeals for the Fourth Circuit held that a temporary furlough plan under which employees lost 0.95 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. Plaintiff employees have agreed to provide their labor and expertise to the school districts for wages bargained for and set forth in contracts. For the state to mandate a three percent reduction in the contractually agreed-upon price of their labor is unquestionably an impairment of contract by the state.

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: "(1) 'consider impairing the . . . contracts on par with other policy alternatives' or (2) '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 *United States Trust Co of New York v New Jersey*, 431 US 1, 30-31; 97 S Ct 1505; 52 L Ed 2d 92 (1977). Put more generally, we are to 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 of the challenged legislation, given that they are to use the monies from the wage reduction to pay "employer

[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 plaintiff employees were to be paid by their respective districts. Indeed, defendants could not plausibly deny it.

[5] In *Baltimore Teachers*, 6 F3d at 1018 n 8, the 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."

contributions" to the retiree health care benefits fund.[6] Because governmental entities are parties to the contracts and benefit from the impairment, we are to employ heightened scrutiny in our review of the statute. *Buffalo Teachers*, 464 F3d at 370-371.

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 the alteration of contractual obligations without offending the Contract Clause. For example, we rejected a Contract Clause challenge in *Health Care Ass'n Workers Compensation Fund v Bureau of Worker's Compensation Director*, 265 Mich App 236; 694 NW2d 761 (2005), which involved a statute designed to unclog the marketplace for workers' compensation insurance by eliminating unduly anticompetitive contractual provisions that punished employers for changing insurers *Id.* at 242. Similarly, the United States Supreme Court has 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 & 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 governmental contracts may be imposed as a matter of last resort to address a fiscal emergency. However, as the cases relied on by defendants show, such circumstances must be extraordinary and the degree of the impairment with regard to its amount and its duration 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*, 438 US at 245. 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*, 6 F3d at 1014, 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 on city employees. 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, the employees' work hours were reduced to correspond with 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

[6] According to the record, the three percent wage reduction will cover nearly 40 percent of the overall employer contributions for retiree health care benefits. Affidavit of Phillip Stoddard, Director of the Office of Retirement Services of the Michigan Department of Technology, Management, and Budget, June 17, 2010.

shortfall, and the city had first taken other actions including a significant cut in city services and laying off employees. *Id.* at 1020.

MCL 38.1343e 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 38.1343e 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. The *Baltimore Teachers* court allowed 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 in the trial court that other means of undertaking long-term restructuring of retiree health care benefit funding had been attempted or even reviewed. No proofs were offered regarding why state interference with agreed-upon contracts was necessary in this situation, 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 because, under *Studier*, those benefits are not protected as "accrued financial benefits." The state has not shown that it first undertook to reduce retiree health care 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 of New York imposed a temporary wage freeze preventing scheduled raises for employees of the city of Buffalo 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 the 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 removed from the facts that allowed the challenged governmental actions in *Baltimore Teachers* and *Buffalo Teachers* to survive the challenge.

Other courts have been unwilling to even go that far. In *Univ of Hawaii Prof 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 because the timing of the regularly scheduled payment was part of the collective bargaining agreement. *Id.* at 1102-1104. As in *Baltimore Teachers* and *Buffalo Teachers*, the *Univ 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 the district court's statement 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 governmental employees' contracts by the state that have indefinite or permanent application clearly violate the Contract Clause. *Oregon State Police Officers' Ass'n v State*, 323 Or 356; 918 P2d 765 (1996) (striking down a state statute that required public employees to contribute six percent of their salaries to retiree benefits contrary to their contract); *Opinion of the Justices*, 364 Mass 847, 864; 303 NE2d 320 (1973) (striking down legislation increasing present employees' 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*, 227 Kan 356, 369; 607 P2d 467 (1980) (holding that a statute mandating an increase in public employees' contributions to their retirement plan without a commensurate increase in benefits "is an unconstitutional impairment of contract rights"); *Marvel v Dannemann*, 490 F Supp 170 (D Del, 1980); *Hickey v Pittsburgh Pension Bd*, 378 Pa 300; 106 A2d 233 (1954); *Allen v City of Long Beach*, 45 Cal 2d 128; 287 P2d 765 (1955).

For these reasons, we conclude that MCL 38.1343e violates US Const, art I, § 10 and Const 1963, art 1, § 10.

V. TAKINGS CLAUSE

Plaintiffs argue that MCL 38.1343e violates the Takings Clause of the Fifth Amendment of the United States Constitution and Const 1963, art 10, § 2, each of which prohibits the taking of private property for public use without just compensation.[7] Plaintiff employees'salaries are specific funds in which they unquestionably have a property interest. *Sims v United States*, 359 US 108, 110; 79 S Ct 641; 3 L Ed 2d 667 (1959) ("it is quite clear, generally, that accrued salaries are property").

Clearly, the government has "taken" three percent of plaintiff employees' 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 plaintiff employees and are 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 when the 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 involve real property and the exercise of eminent domain. Taking jurisprudence also commonly deals with claims that governmental regulatory actions impose such limits on the use of property that they amount to a taking.

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

[7] Because the two clauses are coextensive, we will simply refer to "the Takings Clause" for simplicity.

a specific and identifiable "parcel" of money, it does implicate the Takings Clause. Indeed, the United States Supreme Court has termed such actions violations "per se" 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 accrued on lawyer trust accounts (IOLTAs), even where such amounts were *de minimis*, it constituted an unconstitutional taking. *Id.* We applied this principle in *Butler v Michigan State Disbursement Unit*, 275 Mich App 309; 738 NW2d 269 (2007), where we found an unconstitutional taking of property when the state disbursement unit that collects and disburses child support payments deposited into the state treasury interest on the amounts awaiting disbursement. The amount in question with regard to the plaintiff, a recipient of child support payments, was merely 83 cents in 2005 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 a 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 the 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.* "To put it another way: a State, by *ipse dixit*, may not transform private property into public property without compensation . . . ." *Id.*[9]

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[8] In *Brown*, the government was not required to pay compensation because the clients whose funds had been placed in an IOLTA account could not have earned net income, i.e., interest in excess of administrative costs, had the funds been deposited in a non-IOLTA account. *Brown*, 538 US at 239-240. Similarly, in *Butler*, no compensation was ordered because the government's administrative costs were greater than the plaintiff's accrued interest, and the plaintiff's net loss was therefore zero. *Butler*, 275 Mich App at 313.

[9] In *Eastern Enterprises v Apfel*, 524 US 498, 503-504; 118 S Ct 2131; 141 L Ed 2d 451 (1998), the plaintiff alleged that the Coal Industry Retiree Health Benefit Act, 26 USC 9701 *et seq.*, violated the Takings Clause, because it required the plaintiff to pay premiums into a fund to cover benefits for retirees it had not employed. The Supreme Court found this to be unconstitutional. Four of the justices concluded that it violated the Takings Clause while Justice Kennedy, in an opinion concurring in the judgment and dissenting in part, reached his conclusion under the Due Process Clause. However, the concerns raised by Justice Kennedy regarding the applicability of the Takings Clause do not arise in the instant case. In his opinion, Justice Kennedy stated:

Defendants rely on 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 (CA Fed, 2004), the federal government had concluded that certain federal law enforcement personnel were administrative employees and, therefore, were not entitled to overtime pay at the rate specified in the Fair Labor Standards Act, 29 USC 201 *et seq*. The employees sued under the act and also asserted that the government's failure to pay overtime at the rate specified in the act constituted a taking. The *Adams* court held that an action to enforce payment of a statutory obligation for the payment, unlike a *contract* for a payment, did not concern a vested property right, without which a taking claim cannot arise. *Id.* at 1223. In *Adams*, the taking claim put the cart before the horse by arguing before any right to overtime pay at the rate specified in the act was determined to exist that the failure to pay overtime at that rate constituted a taking. *Id.* at 1221-1222. That is not the case here because it is undisputed that plaintiff employees have a contract-based property right in their own wages.

Kitt v United States, 277 F3d 1330, 1336-1337 (CA Fed, 2002), is similarly inapposite because 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 taking claim, noting that "[i]n some situations money itself may be the 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 plaintiffs seek to invalidate MCL 38.1343e instead of seeking compensation for lost property. Defendants cite *Eastern Enterprises v Apfel*, 524 US 498; 118 S Ct 2131; 141 L Ed 2d 451 (1998), for this proposition, but only Justice Kennedy made such a statement in that case. *Id*. at 545 (Kennedy, J., concurring in the judgment and dissenting in part). Further, the Supreme Court in *Webb's* held a Florida statute unconstitutional under the Takings Clause. It appears that defendants here 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*." *Eastern Enterprises*, 524 US at 540 (emphasis added).

That is by no means the case here. MCL 38.1343e confiscates a specific fund, i.e., plaintiff employees' paychecks, and removes three percent of the property before allowing them 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 Clauses of the Fifth Amendment and Const 1963, art 10, § 2.

VI. SUBSTANTIVE DUE PROCESS

We also affirm the trial court's conclusion that MCL 38.1343e is unconstitutional under the Due Process Clauses of the Fourteenth Amendment and Const 1963, art 1, § 17.

> The Fourteenth Amendment to the United States Constitution and 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) (some quotation marks omitted; citations 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).[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 health care for public school employees. This, however, is an overly general characterization that gives the false impression that 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 health care for already-retired public school employees.

While the present employees and the retired employees have in common their present or former employment by a public school 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 the retirement benefits of others. Rather, it is a mandatory, direct transfer of funds from one discrete group, present school employees, for

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[10] Defendants argue that plaintiffs must show governmental action that shocks the conscience, but that standard applies only to executive, not legislative, action. See *Sacramento Co v Lewis*, 523 US 833, 846; 118 S Ct 1708; 140 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).

the benefit of another, retired school employees. The fact 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 health care 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 the 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*, 472 Mich 642, 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, § 24. The first clause of that provision provides that "[t]he 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." Because 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.

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[11] See, e.g., defendants-appellants' brief ("[i]n exchange [for payment of three percent of their income], the Trust fund *will pay* for the cost of health care for . . . Plaintiffs-Appellees' when they retire") (emphasis added); ("[plaintiffs] are simply being required to pay for a *future benefit*") (emphasis added); ("Since Plaintiffs . . . *are the beneficiaries* of paid [retiree] health care, it is only fair that they help pay a portion of its costs.") (emphasis added); ("Once individual plaintiffs retire, they *will* receive the benefit of [their] contributions . . . .") (emphasis added); (MCL 38.1343e is a rational attempt to impose a portion of the cost of retiree health care on those persons who. . . *will receive* those very health care benefits when they retire.") (emphasis added); (it is proper to "[r]equir[e present employees] to contribute toward the cost of the health care that they *will receive* when they retire") (emphasis added); ("It is only fair that those who receive a health care benefit should have to help pay for it."); ("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: ("Once Plaintiffs retire, their health care costs . . . will be paid from the assets in this fund."); ("Plaintiffs will receive health care when they retire in exchange for their contributions."); ("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: ("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"); ("[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.'"); ("MCL 38.1391 did not create a contract which require[s] MPSERS to provide retiree health care"); ("Plaintiffs do not have a contract to receive health care when they retire.").

Under *Studier*, the second clause of the provision, mandating that benefits be paid for in the year they are accrued,[12] is also not applicable to retiree health care benefits. Thus, the three percent of their wages being withheld does not go to prefund the 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 approving as constitutional 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 20 years when the government retains the unilateral right to "cancel" the "promise" at any time and does 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 binding guarantee that the "loan" will be repaid.

Defendants argue that the present case is analogous to *Mich Mfr Ass'n v Workers' Disability Compensation Bureau Director*, 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 to help defray the costs of workers' disability compensation 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 workers' compensation system that affect every worker and employer in the state. Workers' compensation legislation was adopted 100 years ago to create a system to share risks and to provide for the limited, but prompt, compensation of injured workers. In addition to obtaining general insurance or insuring themselves, all employers in the state may be required to contribute to specialized funds such as the Second Injury Fund, the Silicosis, Dust Disease, and Logging Industry Compensation 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 *Mich Mfr* represented a small modification in an overall system of sharing risks 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. Rather, it is a question of the government's 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 three percent of their wages, above and beyond that which they pay in taxes, with no guarantee of anything in return, to meet the government's obligation to other individuals.

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[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.

Defendants posit 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* one involving general taxation for a general fund with specific uses of the monies later determined by the Legislature *nor* one imposing a fee for service to the payee. It is also not a mechanism that requires individuals to fund benefits that 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 governmental 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.

VII. 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 or partial 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 regarding 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 three percent wage assessment could be addressed by adopting legislation categorizing retiree health care benefits as "accrued financial benefits."