IN THE SUPREME COURT OF THE STATE OF ALASKA

PETER METCALFE, Individually and on Behalf of All Others Similarly Situated, Appellant, v. STATE OF ALASKA Appellee.	)	Supreme Court No.: S-17157

Trial Court Case No.: **1JU-13-00733 CI**

APPEAL FROM THE SUPERIOR COURT,
FIRST JUDICIAL DISTRICT AT JUNEAU,
THE HONORABLE KEVIN G. MILLER, PRO-TERM, PRESIDING

BRIEF OF APPELLEE, STATE OF ALASKA

KEVIN G. CLARKSON
ATTORNEY GENERAL

By:

Jessica M. Alloway
Senior Assistant Attorney General
Department of Law
1031 West Fourth Avenue, Suite 200
Anchorage, AK 99501
Alaska Bar No. 1205045
(907) 269-5232

Filed in the Supreme Court of
the State of Alaska, this _____
day of _____, 2019.

Marilyn May, Clerk of Court

By: _____
Deputy Clerk

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ALASKA STATE CONSTITUTION

Alaska Constitution Article XII, § 7

Membership in employee retirement systems of the State or its political subdivisions shall constitute a contractual relationship. Accrued benefits of these systems shall not be diminished or impaired.

STATUTES

AS 39.35.001

The purpose of this chapter is to encourage qualified personnel to enter and remain in service with participating employers by establishing plans for the payment of retirement, disability, and death benefits to or on behalf of the members.

AS 14.25.062 [Repealed June 30, 2010]

A member who has received a refund of contributions in accordance with AS 14.25.150 forfeits corresponding credited service under AS 14.25.009 - 14.25.220. A member may elect to reinstate credited service associated with the refund by repaying the total amount of the refund. If an election is made under this section, an indebtedness to the plan in the amount of the total refund shall be established. Compound interest at the rate prescribed by regulation shall be added to the reinstatement indebtedness from the date of the refund to the date of repayment or the date of retirement, whichever occurs first.

AS 14.25.220 [Excerpts]

(18) "former members" means a member who is terminated and who received a total refund of the balance of the mandatory contribution account, or who has requested in writing a refund of the balance of the mandatory contribution account;

(20) "inactive teacher or member" means a member who is terminated and who has not received a refund from the plan or a member who is on leave of absence and who is not making contributions under AS 14.20.345;

(44) "teacher" and "member" are used interchangeably under AS 14.25.009--14.25.220 and mean a person eligible to participate in the plan and who is covered by the plan, limited to

(A) a certificated full-time or part-time elementary or secondary teacher, a certificated school nurse, or a certificated person in a position requiring a teaching certificate as a condition of employment in a public school of the state, the Department of Education and Early Development, or the Department of Labor and Workforce Development;

(B) a full-time or part-time teacher of the University of Alaska or a person occupying a full-time administrative position at the University of Alaska that requires academic standing; the approval of the administrator must be obtained before an administrative position qualifies for membership in the plan; however, a teacher or administrative person at the university who is participating in a university retirement program under AS 14.40.661--14.40.799 is not a member under this plan;

(C) a state legislator who elects membership under AS 14.25.040(b);

AS 39.35.130 [Repealed 1977]

An employee shall be excluded from the system upon termination of his employment with the employer, unless he is eligible for a retirement benefit at that time. If the employee does not receive a refund of his contributions at the time of his termination, his contribution accounts, including voluntary contributions shall continue to be held in the system, earn interest at the prescribed rate and according to the prescribed method of allocation under § 100 of this chapter, and are available to the employee . . . in one of the alternative settlement options under § 220 of this chapter within 60 days of an application for their withdrawal.

AS 39.35.350 [Effective 1968 - 1977]

If an employee's employment is terminated for any reason before he becomes eligible for a retirement benefit and the employee is subsequently reemployed, the employee is entitled to the credited service he had accumulated at the time of his last termination, if the employee makes a contribution to the system equal to the amount of the refund paid upon his last termination, and attributable to the balance in his employee contribution account at that time, together with interest at the prescribed rate to the date of repayment of the contribution. A repayment to establish credit for the last period of interrupted service will not be permitted more than three years after the date on which notice of the amount of contribution and interest due was mailed to the employee at his place of employment.

AS 39.35.350 Reinstatement of Credited service [Effective 1977 - 1982]

(a) An employee who receives a refund of contributions in accordance

with AS 39.35.200 forfeits corresponding credited service under AS 39.35.095 - 39.35.680.

(b) An employee may reinstate credited service associated with a refund by repaying the total amount of the refund. A former member who received a total refund of the former member's contribution account balance because of a levy under AS 09.38.065 or a federal tax levy may reinstate credited service in the same manner as an employee. Interest accrues from the date of the refund until repayment of the refund or retirement, whichever occurs first. Payments shall be applied first to accrued interest and then to principal.

(c) Any outstanding indebtedness that exists at the time an employee is appointed to retirement necessitates an actuarial adjustment to the benefits payable based on service reinstated under this section.

AS 39.35.350(b) [Effective 1988 – Repeal 2010]

(b) An employee may reinstate credited service associated with a refund by repaying the total amount of the refund. A former member who received a total refund of the former member's contribution account balance because of a levy under AS 09.38.065 or a federal tax levy may reinstate credited service in the same manner as an employee. Interest will accrue from the date of the refund until repayment of the refund or retirement, whichever occurs first. Payments shall be applied first to accrued interest and then to principal.

AS 39.35.130 [Repealed 1977]

An employee shall be excluded from the system upon termination of his employment with the employers, unless he is eligible for a retirement benefit at that time.

AS 39.35.680 [1977 Version]

(1) "active member" means an employee who is employed by an employer, is receiving compensation for seasonal, permanent full-time, or permanent part-time services, and is making contributions to the plan;

(19) "former member" means an employee who is terminated and who has received a total refund of the balance of his employee contribution account or who has requested in writing a refund of the balance in the employee contribution account, or who is eligible for a refund under § 200 (b) of this chapter;

(20) "inactive member" means an employee eligible who is terminated and who has not received a refund from the system or an employee on leave-without-pay

status or layoff status;

(21) "member" or "employee"

(A) means a person eligible to participate in the system and who is covered by the system;

(B) includes

(i) active member;

(ii) inactive member;

(iii) vested member;

(iv) deferred vested member;

(v) nonvested member;

(vi) disabled member;

(vii) retired member;

(C) does not include

(i) former members

Senate Bill No. 141 of 2005 [Excerpts]

Sec. 133. AS 14.25.061(c), 14.25.062; and AS 39.35.350 are repealed.

Sec. 149. Sections 12, 13, 15, 16, 21, 89–94, 107, 113, and 133 of this Act take effect June 30, 2010.

INTRODUCTION

Peter Metcalfe enrolled in the State's retirement system as a Tier I member in 1980 when he began state employment. When Metcalfe left state employment in 1981, he cashed out every contribution that he made to the retirement system over the previous year. For the 29 years immediately following termination of his state employment, Metcalfe had the ability to return to state service, pay back his contribution with interest, and reenroll in the State's retirement system as a Tier I member. He never returned to state employment, and he never accepted that offer.

In 2005, the Alaska Legislature revoked Metcalfe's ability to buy-back his previous status in the retirement system. In doing so, the Legislature delayed revocation of the offer for five years. Meaning former employees—like Metcalfe—that cashed out their contribution had until 2010 to return to state service and buy-back their retirement status.

Article XII, Section 7 states that membership in a public employee retirement system is a "contractual relationship" and the "accrued benefits" earned as part of that contract cannot be diminished or impaired. This Court has never held that Article XII, Section 7 protects benefits offered to non-members of the State's retirement systems. All of the Court's prior decisions focus on the contractual relationship between the State and the members of its retirement systems and the need to protect the benefits the employees will receive at retirement. The offer to reinstate service credit was not the equivalent of deferred compensation nor was the offer a requirement that a retiree had to satisfy to receive her retirement benefit. The offer of reinstatement was just that, an offer that

required acceptance after reemployment. The class members did not return to state service and accept the offer, they are not members of the State's retirement systems, and they have no constitutionally protected right to reinstate their service credit. This Court should reject the class members' request to expand the diminishment clause beyond what it already protects—the contractual relationship between the State and members of its retirement systems.

ISSUE PRESENTED

Is the State constitutionally required to keep open, in perpetuity, an offer of reinstatement to former employees who left public employment and received a full refund of their contribution to the State's retirement system?

STATEMENT OF THE CASE

I. The State once offered former employees the option to buy back into the defined benefit plan upon reemployment.

The purpose of the Alaska Public Employees' Retirement System ("PERS")[1] is to attract qualified public employees by offering a variety of benefits to members and their survivors.[2] Employees who entered PERS prior to July 1, 2006, are members of the PERS defined benefit plan.[3] A defined benefit plan "defines the benefit first, and then the

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1 The Teachers' Retirement System ("TRS") has the same purpose. The issues raised by the class members' complaint apply equally to TRS and PERS. For ease of reference, the State will refer only to PERS throughout its brief. Although the State will only cite to AS 39.35.350, the Court's holding will apply to AS 14.25.062 as well.

2 AS 39.35.001.

3 *See* AS 39.35.095 (stating that the Defined Benefit Plan applies only to members first hired before July 1, 2006).

plan administrator attempts to set the current contribution rates to pay for those future benefits."[4]

PERS defines the ways in which a non-member can enter the benefit system, and membership in PERS is a condition of employment for most state employees.[5] As a "joint contributory plan," both the employee and the employer jointly contribute to funding the cost of the benefits provided.[6] The State of Alaska pays employer contributions for State of Alaska employees only.

Subject to a limited exception, a PERS member who leaves public employment may receive a refund of the balance of the employee's contribution account.[7] For example, the class representative, Peter Metcalfe, became a PERS member in 1980 while working for the State of Alaska. [Exc. 4] In 1981, Metcalfe left state employment and took a refund of his PERS contribution. [Exc. 5] Metcalfe neither returned to state employment, nor did he repay his contribution amount. [Exc. 5] The factual scenario is similar for every member in the recognized class. [*See* Tr. 92] Every class member left state employment, took a refund of their contribution, and did not return to state employment on or before June 30, 2010. [*See* Tr. 92]

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4 *Moro v. State*, 351 P.3d 1, 9 (Or. 2015) (referring to 26 U.S.C. § 414(j)).

5 AS 39.35.120(b).

6 *See* AS 39.35.115(d) ("[PERS] is a joint contributory plan."); *see also* AS 39.35.160–240 (defining contributions by employees); AS 39.35.255 (defining contributions by employers).

7 AS 39.35.200.

Prior to 2010, the State offered former employees who cashed out their contribution the ability to reenter the system and buy back their previous status within the system. First codified in 1960, AS 39.35.350 has had multiple versions, but none of the differences are material to this appeal. From 1968 through 1977, that statute read:

> If an employee's employment is terminated for any reason before he becomes eligible for a retirement benefit and the employee is subsequently reemployed, the employee is entitled to the credited service he had accumulated at the time of his last termination, if the employee makes a contribution to the system equal to the amount of the refund paid upon his last termination, and attributable to the balance in his employee contribution account at that time, together with interest at the prescribed rate to the date of repayment of the contribution. A repayment to establish credit for the last period of interrupted service will not be permitted more than three years after the date on which notice of the amount of contribution and interest due was mailed to the employee at his place of employment.[8]

From 1977 through 1988, the relevant portion of the statute read:

> (b) An employee may reinstate credited service associated with a refund by repaying the total amount of the refund. Interest will accrue from the date of the refund until repayment of the refund or retirement, whichever occurs first. Payments will apply first to accrued interest and then to principal.[9]

From 1988 through its repeal in 2010, the relevant portion read:

> (b) An employee may reinstate credited service associated with a refund by repaying the total amount of the refund. A former member who received a total refund of the former member's contribution account balance because of a levy under AS 09.38.065 or a federal tax levy may reinstate credited service in the same manner as an employee. Interest will accrue from the date of the refund until

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8 Sec. 3, ch. 235 SLA 1968.

9 Sec. 30, ch. 128 SLA 1977.

> repayment of the refund or retirement, whichever occurs first. Payments will apply first to accrued interest and then to principal.[10]

Now repealed, AS 39.35.350 provided an avenue to former members, like Metcalfe, to reestablish their PERS membership and service credit if they (1) returned to PERS employment, and (2) repaid their earlier refund with interest.[11]

II. In 2005, the Legislature took steps to close the defined benefit plan.

In 2005, the Legislature passed Senate Bill 141 ("SB 141"). One of several major efforts of the Alaska Legislature during the last 25 years to address the health of the PERS system, SB 141 closed the PERS defined benefit plan and established the PERS defined contribution plan for employees who joined the PERS system for the first time after July 1, 2006. Corresponding with its effort to close the defined benefit plan, SB 141 implemented a process for withdrawing the State's offer to allow former members to rejoin PERS under AS 39.35.350.

The Legislature repealed AS 39.35.350, but delayed the repeal for five years, until June 30, 2010, giving former members like Metcalfe a five-year window to reestablish their participation in the defined benefit plan. After July 1, 2010, a former member reentering state employment automatically becomes a member of the PERS defined contribution plan.

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10 AS 39.35.350(b); Sec. 4, ch. 89 SLA 1988.

11 AS 39.35.350 [repealed 2005 by SB 141, effective 2010].

III. The class includes all former employees who received a refund of their retirement contribution and did not return to the defined benefit plan on or before June 30, 2010.

Metcalfe originally filed this class action lawsuit in June 2013. [Tr. 360–375] The superior court granted the State's motion to dismiss, which Metcalfe appealed. In a decision issued in 2016, this Court held that a violation of the diminishment clause could not give rise to a breach of contract claim.[12] It affirmed the dismissal of Metcalfe's monetary damages claim.[13] But the Court also ruled that the statute of limitations did not bar Metcalfe's claim for declaratory and injunctive relief and remanded the case for further proceedings on that cause of action.[14]

In December 2016, Metcalfe filed his First Amended Class Action Complaint for Declaratory Judgment and Injunctive Relief, along with a motion to certify the class pursuant to Alaska Rule of Civil Procedure 23(c)(1). The State answered and filed a limited non-opposition to Metcalfe's motion to certify. [Tr. 106] The Court certified the class in February 2017.

The class is defined as follows:

> Every person who became an Alaska Public Employees' Retirement System ("PERS") or Teachers' Retirement System ("TRS") member between January 1, 1961 and July 27, 2005 who, at some point, left PERS and TRS qualifying employment, took a refund of their retirement contributions to PERS or TRS, and did not return to PERS or TRS qualifying employment before June 30, 2010.

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12 *Metcalfe v. State*, 382 P.3d 1168, 1169–70 (Alaska 2016).

13 *Id.* at 1179.

14 *Id.* at 1170.

[Tr. 92–93] An individual meeting that definition has four characteristics: (1) they were a member of PERS between January 1, 1961 and July 27, 2005;[15] (2) they left state employment; (3) they received a total refund of their contributions to the system; and (4) they did not return to PERS qualifying employment on or before June 30, 2010.

By definition, the class members were not PERS members in 2005, when SB 141 was enacted, or in 2010, when the repeal of AS 39.35.350 went into effect. In 1960 the State made clear that a former employee of the state is not a PERS member. Alaska Statute 39.35.130—repealed in 1977— provided that "[a]n employee shall be excluded from the system upon termination of his employment with the employers, unless he is eligible for a retirement benefit at that time."[16]

After the repeal of AS 39.35.130, PERS membership was defined by AS 39.35.680. A "member" is a "person eligible to participate in the plan and who is covered by the plan."[17] A "member" does not include "former members."[18] The statute currently defines a "former member" to be "an employee who is terminated and who has received a total refund of the balance of the employee contribution account or who has requested in writing a refund of the balance in the employee contribution account."[19] The previous version of the statute included a nearly identical definition: a "former member"

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15 July 27, 2005 is the date SB 141 was signed into law.

16 Sec. 5, ch. 143 SLA 1960.

17 AS 39.35.680(22)(A).

18 AS 39.35.680(22)(C)(i).

19 AS 39.35.680(20).

is an employee who has "received a total refund" of their employee contribution account.[20]

STANDARD OF REVIEW

The proper standard of review is de novo, both because the superior court decided this case on summary judgment and because it presents only issues of law.[21]

ARGUMENT

I. The offer to reinstate service credit was available to former members after they became reemployed; it was not a right offered to members of the State's retirement systems.

Article XII, Section 7 protects the accrued benefits of the State's employee retirement systems. "Membership" in these systems results in a contractual relationship and the "*retirement benefits* are 'regarded as an element of the bargained-for consideration given in exchange for an employee's assumption and performance of the duties of his employment."[22] "This means that system benefits *offered to retirees* when an employee is first employed and as improved during the employee's tenure may not be 'diminished or impaired.'"[23] This Court has clarified that "system benefits" mean the

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20 Former AS 39.35.680(19), (21) (1981); *see* Sec. 54, ch. 128 SLA 1977.

21 *See ConocoPhillips Alaska, Inc. v. Williams Alaska Petroleum, Inc.*, 322 P.3d 114, 122 (Alaska 2014) ("We review rulings on motions for summary judgment de novo."); *State v. Ketchikan Gateway Borough*, 366 P.3d 86, 90 (Alaska 2016) ("Questions of constitutional and statutory interpretation, including the constitutionality of a statute, are questions of law to which we apply our independent judgment.").

22 *Duncan v. Retired Public Employees' of Alaska, Inc.*, 71 P.3d 882, 886 (Alaska 2003) (quoting *Hammond v. Hoffbeck*, 627 P.2d 1052, 1056 (Alaska 1981)) (emphasis added)).

23 *Id.* (emphasis added).

"whole complex of provisions" that comprise the retirement benefit package, whether the benefit was granted via statute or regulation.[24]

As with any other constitutional or statutory interpretation question, the Court must begin with the plain language of the provision it is interpreting. Article XII, Section 7 protects members. It does not say that *offers to join* the State's retirement system shall not be diminished or impaired. Rather it states that "membership in employee retirement systems . . . shall constitute a contractual relationship." The class members are not members of the retirement systems.[25] They gave up their membership when they left state service and cashed out their contribution. Unlike "inactive members"—members that left state service but did not cash out their contribution[26]—former members have no ties to the system. The State has paid the former members all of the compensation they are owed for their service, and it does not have access to the former members' contributions for purposes of investment and planning.

Alaska Statute 39.35.350 offered the class a way to reinstate PERS benefits once

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24 *Sheffield v. Alaska Public Employees' Ass'n, Inc.*, 732 P.3d 1083, 1087 (Alaska 1987) (relying on *Opinion of the Justices*, 364 Mass. 847 (1973) (emphasis omitted)).

25 A "member" is a "person eligible to participate in the plan and who is covered by the plan." AS 39.35.680(22)(A); *see also* AS 14.25.220(44) ("'teacher' and 'member are used interchangeably under AS 14.25.009–14.25.220 and mean a person eligible to participate in the plan and who is covered by the plan"). A "member" does not include "former members." AS 39.35.680(22)(C)(i); *see* AS 14.25.220(44)(A)–(C).

26 An "inactive member" is defined as "an employee who is terminated and who has not received a refund from the plan or an employee on leave-without-pay status or layoff status." AS 39.35.680(21); *see also* AS 14.25.220(20) ("'inactive teacher or member' means a member who is terminated and who has not received a refund from the plan or a member who is on leave of absence and who is not making contributions under AS 14.20.345").

they rejoined PERS, but this buy-back offer was not a benefit of their "membership" in PERS. Instead, it was an employment benefit. It was a way for the State to entice individuals with state experience to return to public service. For example, AS 39.35.350(b) provided that an "employee may reinstate credited service associated with a refund by repaying the total amount of the refund." This was not something a member of the retirement system could take advantage of, nor was it something that the employee could take advantage of when they first became an employee of the State. This offer only applied to reemployed employees of the State, and the benefits offered to reemployed employees can be changed prior to those employees returning to state service.

The class asks this Court to look past the plain language of the constitution and relevant statutes and instead focus on language in its decisions that state the diminishment clause protects the "whole complex of provisions" related to the retirement system. As the class argues, because the State offered reinstatement when the class members were state employees, the ability to be reinstated was a right of the benefit system—an eligibility requirement—and is therefore an "accrued benefit." But in making this argument the class ignores important aspects of the Court's prior decisions. This Court has protected benefits offered to members *during their retirement*. As it stated in *Duncan*, it is the "system benefits *offered to retirees*" that may not be diminished or impaired.[27] Reinstatement of service credit is not a benefit that would be exercised by a

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27 71 P.3d at 886.

retiree during her retirement.[28] The statute was intended to entice former employees to return to state employment. But former members do not possess retirement rights and could not accept the offer to reinstate service credit without first becoming employed.

Reinstatement is different from benefits protected by the diminishment clause, and a case from the Nebraska Supreme Court helps illustrate this difference. In *Livingston v. Metropolitan Utilities District*, the Nebraska Supreme Court held that the Metropolitan Utilities District ("MUD") had the right to modify the long-term disability ("LTD") policy it offered as optional coverage to its employees.[29] Livingston argued "that at the time he was offered and accepted employment with MUD, he was promised that he would have the option to obtain lifetime LTD coverage."[30] And, similar to this Court's diminishment clause jurisprudence, "Nebraska has long recognized that pensions are not gratuities."[31] Previously, the Nebraska Supreme Court "held that a pension plan offered to officers of the Nebraska State Patrol . . . was 'deferred compensation, earned in exchange for services rendered [and created] in the employees reasonable expectations entitled to legal protection.'"[32]

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28 The fact that AS 39.35.350 was part of the PERS Act does not automatically make it a retirement right protected from diminishment. The PERS Act contains other provisions that are not retirement benefits or rights. For example, AS 39.35.180 is a voluntary employee savings plan—it is not a retirement right or benefit.

29 692 N.W.2d 475, 477 & 479 (2005).

30 *Id.* at 479.

31 *Id.* at 480.

32 *Id.* (quoting *Haplin v. Nebraska State Patrolmen's Retirement Sys.*, 20 N.W.2d 910 (Neb. 2000)).

Nevertheless, despite its previous decision, the Nebraska Supreme Court held that optional coverage under the LTD plan is not a pension benefit protected by the Contracts Clause.[33] Deferred compensation is "compensation which is earned in exchange for services rendered."[34] The optional coverage offered by Nebraska was not deferred compensation because enrollment in the "LTD plan was purely voluntary[,] and the accrual of coverage under this policy was not contingent upon the rendering of services, but instead depended upon the payment of premiums and the occurrence of an injury."[35]

By leaving state employment and cashing out of PERS, every individual in the represented class is a "former member."[36] As former Chief Justice Fabe recognized in her dissent from the Court's last decision, the Court "has never held that article XII, section 7 applies to non-members of PERS."[37] Similarly, the Court has limited diminishment

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33 *Id.*

34 *Id.*

35 *Id.* This case also presents a similar situation to what the New Jersey court discussed in *Cookson v. Board of Trustees, Public Employees' Retirement System*, 2010 WL 816790 (N.J.Super.A.D.) (unreported) (affirming New Jersey PERS Board's decision that employee's membership had ended two years after she left PERS employment and that the reinstatement statutes she relied upon merely provided an avenue to resume membership and did not provide that she was a member continuously during the time that she could seek reinstatement of her membership).

36 AS 39.35.680(20).

37 *Metcalfe*, 382 P.3d at 1178 (Fabe, J., dissenting); *see also id.* at 1178 n.8 (citing the following cases: *Alford v. State, Dep't of Admin., Div. of Ret. & Benefits*, 195 P.3d 118 (Alaska 2008) (addressing the State's recapture of early retirement benefits after members retired, retained PERS membership and then re-entered public employment); *Bd. of Trs., Anchorage Police & Fire Ret. Sys. v. Municipality of Anchorage*, 144 P.3d 439 (Alaska 2006) (regarding "surplus benefits" for current members of the municipality's retirement system); *McMullen v. Bell*, 128 P.3d 186 (Alaska 2006) (reviewing the calculation of a specific PERS member's benefits); *Duncan*, 71 P.3d at

clause protection to *retirement* benefits that amount to deferred compensation.[38] The class members are not in the same position as the retirees in any of the Court's diminishment clause cases to date. They left state employment and abandoned the State's retirement systems. This Court should not expand its jurisprudence to grant constitutional protection to employment benefits.

II. A contract for reinstatement did not exist until the former member returned to public employment and began the reinstatement process.

Article XII, Section 7 provides that "[m]embership in employee retirement systems . . . shall constitute a contractual relationship." "Formation of a contract requires an offer, encompassing all essential terms, an unequivocal acceptance by the offeree of all terms of the offer, consideration, and intent to be bound by the offer."[39] Ordinarily, a promise contained within an offer becomes enforceable only when the offer is accepted.[40]

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882 (regarding PERS and TRS members' health insurance benefits); *Municipality of Anchorage v. Gallion*, 944 P.2d 436 (Alaska 1997) (reviewing a change to the "accrued benefits" of some members of a municipal retirement plan); *Municipality of Anchorage v. Gentile*, 922 P.2d 248, 260 n.13 (Alaska 1996) (declining to consider the constitutional claim brought by members of a municipal retirement plan); *Sheffield*, 732 P.2d at 1083 (regarding a change in calculating PERS members' accrued benefits); *State ex rel. Hammond v. Allen*, 625 P.2d 844 (Alaska 1981) (reviewing the repeal of benefits for members of the Elected Public Officers' Retirement System); *Hammond*, 627 P.2d at 1052 (reviewing a change in benefits as applied to PERS members who were adversely affected and employed on the date of the change)).

38 *Duncan*, 71 P.3d at 888–89 (holding that the State cannot diminish or impair the major medical insurance coverage promised to retirees during their retirement); *Sheffield*, 732 P.2d at 1089 (protecting the actuarial factors used to calculate an employee's early retirement); *Hammond*, 627 P.2d at 1058 (stating that requirements to determine eligibility for occupational disability and death benefits are an accrued benefit).

39 *Hall v. Add-Ventures, Ltd.*, 695 P.2d 1081, 1087 n.9 (Alaska 1985).

40 *Moro*, 351 P.3d at 20 (citing Restatement (Second) of Contracts § 24 comment a ("In the normal case, . . . the offer itself is a promise[.]") and Richard A. Lord, *1 Williston*

There are two types of contracts, bilateral contracts and unilateral contracts. "An offer for a bilateral contract invites the other party to accept with a return promise—that is, by *promising* some future performance."[41] "An offer for a unilateral contract invites the other party to accept with performance—that is, by actually *doing* the performance that the offering party seeks."[42] In other words, a unilateral contract is formed once the accepting party has fully performed its obligation under the contract.[43] The accepting party will therefore owe no future obligation to the offering party.[44]

These basic rules of contract formation apply to all contracts, including PERS contracts.[45] Before an employer's promise of PERS benefits becomes a contract, it is merely an offer that the prospective employee may accept or reject.[46] And, because the State's offer of PERS benefits invites employees "to accept by providing current service

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on Contracts § 4.7, 449 (4th ed. 2007) (defining an ordinary offer as a "conditional promise")); *see also Kodiak Island Borough v. Large*, 622 P.2d 440, 447 (Alaska 1981) (describing an offer as an "invitation to contract").

41 *Moro*, 351 P.3d at 21 (emphasis in original) (citing *Corbin on Contracts* § 1.23).

42 *Id.* (emphasis in original) (citing *Corbin on Contracts* § 1.23).

43 *Id.*

44 *Id.*

45 *See id.* (stating that a PERS contract is a unilateral contract); *see also Williams v. Cordis Corp.*, 30 F.3d 1429, 1432 (11th Cir. 1994) ("[A] pension plan is a unilateral contract which creates a vested right in those employees who accept the offer it contains by continuing in employment for the requisite number of years." (internal quotation marks omitted)).

46 *Moro*, 351 P.3d at 21.

for the employer—rather than by promising to provide some service in the future—the resulting PERS contract is a unilateral contract."[47]

Normally, an offeror may withdraw an offer for a unilateral contract at any time until the offeree has completed performance.[48] However, to prevent injustice, some contracts have "an implied term" preventing the employer from "revoking the employee's opportunity to vest those benefits."[49] "[A]n offer is impliedly irrevocable if the invited form of acceptance takes time to complete and the accepting party is attempting to complete the acceptance."[50]

These basic principles are important because they refine the nature and the scope of the contracts protected by the diminishment clause in Article XII, Section 7. In *Duncan*, this Court held that the diminishment clause protects "all retirement benefits that make up the retirement benefit package that becomes *part of the contract of employment when the public employee is hired.*"[51] This includes major medical insurance because "medical insurance is . . . part of an employee's benefit package and the whole package is an element of the consideration that the state contracts to tender in exchange for services rendered by the employee."[52] It is a form of "deferred compensation"—the State offers

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47 *Id.*

48 *Id.* at 35 & n.32 (citing Lord, *1 Williston on Contracts* § 5:13 at 987).

49 *Id.* at 35.

50 *Id.*

51 71 P.3d at 888 (emphasis added).

52 *Id.* at 887.

major medical insurance in exchange for the employees' public service, and the PERS members accept this offer by accepting employment and beginning work.[53]

Although the Court did not use these explicit words, it essentially held that the offer for major medical insurance was an offer to the prospective state employee to enter into a unilateral contract that the prospective employee could accept by entering employment. Once an employee is eligible to receive payment of those benefits that employee has fully performed her obligation under the contract and owes no future performance. The diminishment clause makes the offer irrevocable while the employee is attempting to complete the acceptance. The Court applied similar reasoning in other cases when it held that Article XII, Section 7 protects (1) occupational disability and death benefits;[54] (2) the standard of eligibility for these benefits;[55] and (3) how the monetary benefit calculations are made.[56] These are all benefits offered to the employee as a unilateral contract through the PERS system and accepted by the employee when the employee enters employment with the State.

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53 *Hammond*, 627 P.2d at 1056.

54 *Id.* at 1059–60 (stating that death benefits—which are essentially a life insurance policy—are an element of consideration offered to public employees in exchange for their services).

55 *Id.* at 1058 (concluding that the standard by which eligibility for benefits is determined is protected by the diminishment clause).

56 *Sheffield*, 732 P.2d at 1084 (holding that Article XII, Section 7 protects how the monetary value of the benefits are calculated, prohibiting the State from using factors that would reduce the amount of early retirement benefits the employee would receive compared to payments calculated under the system in place at the time of his employment).

At issue in *Sheffield v. Alaska Public Employees' Ass'n, Inc.*, was how to calculate state employees' early retirement benefits.[57] Prior to an amendment effective in 1986, the PERS Act provided that state employees' with at least five years of credited service could elect early retirement, subject to an actuarial adjustment of the amount of PERS benefits the employees would have received upon normal retirement.[58] The Court held that the diminishment clause prohibited a change in the actuarial tables that would result in the employees receiving less in early retirement than they would have received through the tables in place at the time of their employment.[59] Again, under the contract they accepted at the time of employment, these employees relied on the fact that they could choose early retirement and that the benefits they would receive during early retirement would be calculated a certain way.[60] The Court explained:

> [T]o hold that employees have a right only to early retirement benefits which are subject to actuarial changes until retirement would vitiate Alaska's constitutional protection of accrued benefits for those employees who anticipate early retirement: they could not count on any particular amount of pension but only that they will each receive one.[61]

Simply put, reinstatement under AS 39.35.350 is not like the benefits at issue in *Sheffield* or *Duncan* because it does not serve as "deferred compensation" to former members. The possibility of a PERS reinstatement after a future exit from and

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57 732 P.2d at 1084.

58 *Id.* (citing AS 39.35.370(a)–(c)).

59 *Id.*

60 *Id.* at 1089.

61 *Id.*

hypothetical re-entry into state employment was not a piece of "deferred compensation" that was part of the class' "retirement benefits package." Although one might speak of one's "retirement benefits package" as including a pension and health insurance at age 60, one would not say that one's "retirement benefits package" includes a latent option to quit, cash out one's employee contributions, return to state employment decades later, and buy back into the retirement system. Once a former member left state employment the former member had received all compensation—deferred or otherwise—that the former member was entitled to receive.

Similarly, even though an "accrued benefit" under Article XII, Section 7 includes "requirements for eligibility" in addition to "the dollar amount of the benefits payable,"[62] the PERS buy-back offer is categorically different from a benefit eligibility requirement. The concept of "accrued benefits" must be read to include benefit eligibility requirements to encompass situations that are readily recognizable as diminishments of benefits. For example, if the State were to increase the age at which a retiree would become eligible for a pension from 60 to 70, that would be a diminishment even if the dollar amount of the pension remained the same. Likewise, if the State were to eliminate mental conditions from the disability criteria that could qualify an employee for disability benefits, that would again be a diminishment even if the dollar amount of the benefits remained the same. But these examples are changes to the criteria that a member of the benefit system must meet in order to access benefits within the benefit system. The buy-back statute, by contrast, was a means by which a non-member could *enter the benefit system*—not a

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62 *Hammond*, 627 P.2d at 1058.

requirement that a member had to satisfy to access benefits *within the benefit system*. Just as all of the Court's diminishment clause cases involve members in the State's retirement systems, they also all involve benefits (or conditions for accessing benefits) *within those systems*—not ways in which to *enter those systems*.

Because reinstatement was not offered as a PERS benefit, the Court must separately consider when a contract was formed between the State and the former member. A contract requires an offer, acceptance, consideration, and intent to be bound by the offer. For reinstatement under AS 39.35.350, acceptance did not occur at the time the former member first entered public employment; instead, it occurred only when the former member returned to public employment after leaving, and elected to begin the reinstatement process. This is a classic bilateral contract. The employee accepts the contract with a return promise—that is, promising to pay back his or her contributions. Until that time, the State had only offered reinstatement and that "offer" could be revoked or amended.

III. The diminishment clause does not prevent the State from revoking or modifying its offer of reinstatement.

The contractual relationship between the State and PERS members does not become static once a contract is formed—it continues to change.[63] For unilateral contracts such as the PERS contract, "[a]s long as the [State] continues offering PERS benefits, PERS members can continue accepting that offer and, thereby, earn additional

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63 *Moro*, 351 P.3d at 22.

contractual rights to additional PERS benefits."[64] A PERS member may therefore accept improvements to the benefits offered by continuing employment, but Article XII, Section 7 prevents those benefits from being "diminished or impaired."[65]

Bilateral contracts, such as those formed when a former member returned to public employment and repaid his contributions, work differently. The State's offer for reinstatement was a continuing offer. The contract reaches only as far as a former member has accepted the offer, and the former member's acceptance reaches only as far as the former member's performance.[66] As long as the offer was available, a former member could choose to accept the State's offer and repay his or her contributions. However, the State could also choose to change or revoke an unaccepted offer of reinstatement. This occurred in 2010 with the implementation of SB 141. None of these class members had accepted the State's offer. They had not returned to public employment and they had not elected to seek reinstatement by repaying their contribution. The State lawfully revoked that offer as it was under no obligation to keep its offer of reinstatement open indefinitely.

In the superior court proceedings, the class argued that the offer of reinstatement amounted to an "option contract." An option contract is essentially an irrevocable offer.[67]

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64 *Id.*

65 *Duncan*, 71 P.3d at 886 ("This means that system benefits offered to retirees when an employee is first employed and as improved during the employee's tenure may not be 'diminished or impaired.'").

66 *See Moro*, 351 P.3d at 22–23.

67 Restatement (Second) of Contracts § 25.

It has two elements: (1) the underlying contract is not binding until accepted; and (2) there is an agreement to hold open the offer to contract for a period of time.[68] Although not yet a contract, it has the "requirements for the formation of a contract"[69] because consideration is needed to require an offeree to keep an offer open.[70]

The class argued that Article XII, Section 7 made the offer of reinstatement a contractual right that could not be diminished or impaired, and the offer became an option contract that limited the State's power to revoke the offer to reinstate credited service. This assumes that the diminishment clause protects offers to contract, which the State argues it does not. Reinstatement of service credit was not a part of that contractual relationship—it was not something the state employee promised to do during the course of her employment, and it was not something the State offered to the employee in return for her service. Rather it was an enticement intended to attract previous employees back to state service, which required reemployment and the repayment of contributions with interest.

This interpretation not only supports the objective of the diminishment clause—to protect the compensation earned by retirees but deferred until retirement—it is consistent with how the State treats "inactive members." An "inactive member" is "an employee who is terminated and who has not received a refund from the plan or an employee on

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68 *Plantation Key Developers, Inc. v. Colonial Mtg. Co. of Ind.*, 589 F.2d 164, 168 (5th Cir. 1979).

69 Restatement (Second) of Contracts § 25.

70 *Donahue v. Davis*, 68 So.2d 163, 170 (Fla. 1953); *Coulter & Smith, Ltd v. Russell*, 966 P.2d 852, 859 (Utah 1998) ("The contract to leave the option open for a specified time must be supported by consideration; without it the promisor is not bound.").

leave-without-pay status or layoff status."[71] An inactive member is a member of the retirement system.[72] If an inactive member returns to state service, she will return to the same package of retirement benefits that she had when she was first employed with the State.[73] In other words, by leaving her contributions in the retirement system when she departed state employment, that inactive member provided sufficient consideration to support an irrevocable offer that allowed her to maintain her position in the retirement system.

The class failed to meet its burden of proving an option contract because the former members provided no consideration to support an irrevocable offer.[74] This consideration must be separate and distinct from the service the class members provided during the course of their employment.[75] Because the offer of reinstatement was not supported by consideration, the State's offer was not an irrevocable option contract but simply an offer—an offer that the State lawfully revoked five years after it repealed AS 39.35.350 and AS 14.25.062.

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71 AS 39.35.680(21).

72 AS 39.35.680(22)(B).

73 *See* AS 39.35.720 (defining membership in the defined contribution plan to include "[a]n employee who becomes a member on or after July 1, 2006").

74 *See Donahue*, 68 So.2d at 170.

75 *See Polk v. BHRGU Avon Properties, LLC*, 946 So.2d 1120, 1122 (Fla. Dist. Ct. App. 2006) (stating that "consideration for the option contract is separate and distinct from the consideration for the real estate sales contract").

IV. Even assuming the class provided sufficient consideration to support an irrevocable offer, they failed to exercise the option within a reasonable period of time.

If the parties fail to specify a time for performance in an option contract, a reasonable time will be implied.[76] "Whether the length of time to exercise an option contract is 'reasonable' depends on the particular facts and circumstances of a given case."[77]

In this case, Metcalfe left state employment in 1981. The Legislature provided notice of its intent to revoke the offer of reinstatement in 2005. Metcalfe had 24 years to take action from the time he left state employment to the time he knew the State would revoke the offer, yet he chose not to act. Recognizing that not all former members had 24 years to decide whether to return to state employment, the Legislature delayed the repeal of AS 39.35.350 and AS 14.25.062 for five years. That means that every class member had at least five years to exercise the option, but failed to do so. In Metcalfe's case, he had 29 years to accept the offer. Even if a valid option contract existed, the class members were given a reasonable length of time to exercise the option, and they are not entitled to a longer option period.

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76 *South Carolina Elec. & Gas Co. v. Hartough*, 654 S.E.2d 87, 90 (S.C. Ct. App. 2007).

77 *Id.* (*see, e.g. Wall v. Huguenin*, 305 S.C. 100, 103 (1991) (holding that a delay of thirteen years in exercising an option to repurchase family land was not unreasonable, considering the fact that the land was subject to two lawsuits and the option indicated it could be exercised when "convenient" for the optionee); *Carroll v. Page*, 264 S.C. 345, 351 (1975) (noting that where the option for lessee to purchase the property if the lessor decided to sell it fixed no time for lessee's acceptance of the offer to sell, the delay of one year after lessee indicated he only wanted "a few days" to consider the option did not constitute the exercise of the option within a reasonable time)).

V. The State may make reasonable changes to the retirement systems.

"[T]he prohibition on diminishment or impairment of retirement benefits does not mean that retirement benefits are unchangeable."[78] A benefit can be modified as long as the modification is reasonable.[79] In *Hammond v. Hoffbeck*, this Court adopted the "limited vesting" approach applied by the California courts.[80] That approach is described as follows:

> An employee's vested contractual pension rights may be modified prior to retirement for the purpose of keeping a pension system flexible to permit adjustments in accord with changing conditions and at the same time maintain the integrity of the system. Such modifications must be reasonable, and it is for the courts to determine upon the facts of each case what constitutes a permissible change. To be sustained as reasonable, alterations of employees' pension rights must bear some material relation to the theory of a pension system and its successful operation, and changes in a pension plan which result in disadvantage to employees should be accompanied by comparable new advantages.[81]

The California Court of Appeals recently emphasized that, even in the limited vesting approach, retirees do not have a right to any fixed or definite benefit—they only have a right to a "reasonable pension."[82] And simply because the California courts have

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78 *Duncan*, 71 P.3d at 889.

79 *Id.*

80 627 P.2d at 1057 (citing *Betts v. Bd. of Admin. of Public Employees' Ret. Sys.*, 21 Cal.3d 859 (1978) and *Allen v. City of Long Beach*, 287 P.2d 765 (Cal. 1955)).

81 *Id.* (quoting *Allen*, 287 P.2d at 767).

82 *Marin Ass'n of Public Employees v. Marin County Employees' Ret. Ass'n*, 206 Cal. Rptr.3d 365, 388 (Cal. Ct. App. 2016), *review granted*, 383 P.3d 1105 (Cal. 2016) ("[T]he guiding principle is still . . . the governing body may make *reasonable* modifications and changes before the pension becomes payable and that until that time

previously stated that a disadvantage to employees *should* be accompanied by a comparable new advantage, there is no "imperative obligation" to do so.[83] In other words, a reasonable modification can encompass a reduction in promised benefits.[84] The fundamental question is not whether there are comparable new advantages. Rather, the question is whether the change was reasonable and whether the retirees will continue to receive a "substantial" or "reasonable" pension.[85]

Under the class' theory, the State made an offer of reinstatement that the State cannot revoke without a comparable new advantage. The class would require the State to either reopen the defined benefit plan or create a completely new plan that offers benefits of comparable value. If this Court finds the diminishment clause applies, it should follow the lead taken by the California Court of Appeals in *Marin Association of Public Employees v. Marin County Employees Retirement Association*[86] and consider whether this change was reasonable and whether former members that return to state employment

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the employee does not have a right to any fixed or definite benefits but only to a substantial or *reasonable* pension." (internal quotation marks omitted)).

83 *Id.* at 385 (stating that "'should' does not convey imperative obligation, no more compulsion than 'ought'").

84 *Id.* at 387–88.

85 *Id.* at 392 (stating that the change at issue did not deprive the employees of a "substantial" or "reasonable" pension); *id.* ("Unfortunately, the exercise of that power can be a harsh reminder to employees that "'a public pension system is subject to the implied qualification that the governing body may make reasonable modification and changes before the pension becomes payable and that until that time the employee does not have a right to any fixed or definite benefits.'" (quoting *Miller v. State of Alaska*, 557 P.2d 970, 975 (Cal. 1977) (en banc))).

86 206 Cal. Rptr.3d at 388.

will continue to receive a "substantial" or "reasonable" pension even in light of the change.

Although the State ultimately revoked its offer of reinstatement, this modification was reasonable under the facts and circumstances. This Court has adopted California's approach in stating that an employee's vested benefits may be modified prior to retirement "for the purpose of keeping a pension system flexible to permit adjustments in accord with changing conditions and at the same time maintain the integrity of the system."[87] Here, there is no question why the Legislature closed the option period. The legislative history of Senate Bill 141 documents the Legislature's concern about maintaining the integrity of the retirement system.

> The intent of the repeal [wa]s to relieve the "off book" liability of hundreds of millions of dollars represented by more than 77,000 people who have refunded out of the State's retirement system but who could return to work and be restored to the tier status they held prior to termination by repaying the amount refunded plus interest. In medical premiums alone, this amount stands at greater than $107 million for one year in today's dollars.[88]

Yet, despite these concerns, the Legislature did not revoke the offer to reinstate credited service immediately. It gave the former employees another five years to decide whether they wanted to return to state employment and accept the offer of reinstatement.

The former members had a reasonable length of time to seek reinstatement.[89] Any expectation on their part that the offer would be kept open indefinitely was unreasonable

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87 *Hammond*, 627 P.2d at 1057 (internal quotation marks omitted).

88 Senate Finance Comm., Sectional Analysis, CSSB 141, 24th Legis.

and not supported by Article XII, Section 7. Although the class members would be unable to rejoin the defined benefit plan if they returned to state service now, they would be a member of the defined contribution plan, which offers a "substantial" and "reasonable" retirement benefit.

CONCLUSION

Article XII, Section 7 protects PERS members from losing benefits they contracted for in return for their public service. But reinstatement is not a benefit offered to members as consideration for their state service. It is something that the State offers to former members separate from their employment contract, and their employment was not conditioned on the members' accepting an offer of reinstatement. For the reasons stated, the State asks that the Court affirm the superior court's order granting summary judgment.

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[89] In this case, where the terms of the offer were established by statute, the State believes the Court can determine that, as a matter of law, the five additional years offered by the State to exercise the option was reasonable.