

COMMONWEALTH OF KENTUCKY
FRANKLIN CIRCUIT COURT
DIVISION I
CASE NO. 18-CI-379
ELECTRONICALLY FILED

COMMONWEALTH OF KENTUCKY,
ex rel. ANDY BESHEAR, ATTORNEY GENERAL, *et al.*

PLAINTIFFS

v.

MATTHEW G. BEVIN, in his official capacity
as Governor of the Commonwealth of Kentucky, *et al.*

DEFENDANTS

**DEFENDANT'S MOTION TO DISQUALIFY THE ATTORNEY GENERAL AND
THE OFFICE OF THE ATTORNEY GENERAL**

NOTICE

Please take notice that the undersigned counsel will appear in the courtroom of the above-referenced Court and present the following Motion on Wednesday, April 25, 2018, at the hour of 9:00 a.m., or as soon thereafter as counsel may be heard.

MOTION

Defendant Governor Bevin hereby moves to disqualify the Attorney General and the Office of the Attorney General because their prosecution of this action violates the Kentucky Rules of Professional Conduct. A Memorandum of Law is submitted herewith and incorporated herein by reference.

Respectfully submitted,

/s/ M. Stephen Pitt

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CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing were served via email this 17th day of April, 2018, to Andy Beshear, J. Michael Brown, La Tasha Buckner, S. Travis Mayo, Marc G. Farris, Samuel Flynn, Office of the Attorney General, 700 Capitol Avenue, Suite 118, Frankfort, Kentucky 40601, Jeffrey Walther, Walther, Gay & Mack, 163 E. Main St., Suite 200, Lexington, KY 40588, David Leightty, Priddy, Cutler, Naake, Meade, 2303 River Road, Suite 300, Louisville, KY 40206, David Fleenor, Capitol Annex, Room 236, Frankfort, KY 40601, Eric Lycan, Office of the Speaker, Capitol Annex, Room 332, Frankfort, KY 40601, Mark Blackwell, 1260 Louisville Road, Frankfort, KY 40601.

/s/ M. Stephen Pitt

Counsel for Governor Bevin

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MATTHEW G. BEVIN, in his official capacity
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DEFENDANTS

DEFENDANT'S MEMORANDUM OF LAW IN SUPPORT OF MOTION TO
DISQUALIFY THE ATTORNEY GENERAL AND THE OFFICE OF THE
ATTORNEY GENERAL

Yet again, the Attorney General has sued Governor Bevin. This time, however, the Attorney General sued the Governor, both chambers of the General Assembly, and two executive-branch agencies. And he did this after deliberately providing the defendants legal advice in his capacity as the Commonwealth's chief legal advisor. *See* KRS 15.020. The Attorney General, in other words, is suing his own clients over the very matters on which he advised them. To make matters worse, he is using this lawsuit as political cannon fodder in speeches and rallies around the state.

The conflicts of interest created by the Attorney General's conduct are not difficult to understand—the only question is whether the law will be fairly applied here as it would in any other case. The Attorney General's decision to sue his own clients and political opponents violates the Rules of Professional Conduct. He does

not get a pass on the law simply because he is the Attorney General or because this lawsuit is over issues of important public policy. In fact, the opposite should be true. If the rules and laws governing conflicts of interest should apply to anyone, they should apply to the chief law officer of the Commonwealth. And for those reasons, the Attorney General should be disqualified from representing himself or any other individual in this suit.

BACKGROUND

On April 2, 2018, Governor Matt Bevin signed SB 151 into law, putting into place several much-needed reforms to Kentucky's ailing pension system.¹ But the Attorney General's involvement began much earlier than April 2. The substance of SB 151 originated in SB 1, which was filed by Senator Joe Bowen on February 20, 2018. The bill was assigned to the Senate Committee on State & Local Government the next day, and from there it went through several weeks of review and public comment. One part of that review came from the Attorney General, who drafted a legal memorandum regarding the provisions of SB 1 eight days after the bill was filed. [Ex. A]. In his legal memorandum, the Attorney General laid out what he believed were twenty-one different reasons the bill violated Kentucky law.

¹ It is now common knowledge that Kentucky's pension system is the worst funded in the nation. *See* "U.S. State Pensions: Weak Market Returns Will Contribute To Rise In Expense," Global Credit Report, Sept. 12, 2016 (S&P Global) (online at https://www.globalcreditportal.com/ratingsdirect/renderArticle.do?articleId=1708443&SctArtId=400468&from=CM&nsl_code=LIME&sourceObjectId=9778524&sourceRevId=1&fee_ind=N&exp_date=20260912-20%3A30%3A04) (last visited April 16, 2018).

Critically, the Attorney General drafted this memorandum in his role as the chief law officer of the Commonwealth, and he addressed it to every single member of the General Assembly. It was not an op-ed or a letter to the editor. Rather, it was a memorandum containing legal advice addressed to legislators—those to whom he is obligated to provide legal advice under Kentucky law. KRS 15.020 provides that the Attorney General is the Commonwealth’s chief legal officer and “legal advisor of all state officers, departments, commissions, and agencies,” and it requires him to provide legal advice to state agencies as needed. The Attorney General’s legal memorandum makes clear that he is providing legal advice pursuant to his statutory duty, establishing an attorney-client relationship with the recipients. He urged every member of the General Assembly to continue to consult with him regarding the legality of the bill, and he followed up with a second legal memorandum on March 6 after the legislature implemented several revisions to the bill.

Approximately one month later, the General Assembly moved the provisions of SB 1 into SB 151, and in doing so adopted several of the revisions recommended by the Attorney General’s legal-advice memorandum. The Attorney General, for example, advised the General Assembly that he believed reducing the cost of living adjustments for retired teachers violated the Commonwealth’s inviolable contract, and this provision was eliminated in SB 151. While the General Assembly did not adopt every suggestion by the Attorney General, it is rare to find a client that agrees with every opinion of his attorney.

After SB 151 passed the General Assembly, the Attorney General continued to provide legal advice to the members of the legislature. On March 30, 2018, the day after SB 151 passed, the Attorney General met with the Democratic Party leaders of the Kentucky House of Representatives and the Kentucky Senate “to discuss legal options on [the] pension bill.” [See Figure 1].²



Figure 1

While the existence of his meeting with these legislative leaders was public, the actual discussions between the parties is unknown. What is known is that the Attorney General apparently took his role as the Commonwealth’s chief legal advisor seriously as he counseled legislators regarding SB 151.

But the Attorney General’s next steps are inexplicable and indefensible. Three days later, the Attorney General appeared at a political rally protesting the bill’s

² See <https://twitter.com/KYHouseDems/status/979734685063331840> (last visited April 16, 2018).

passage. He gave an impassioned speech to a group of protestors and called for them to vote against any legislator who supported SB 151 and to defeat Governor Bevin in the 2019 gubernatorial election. In the video from this rally, the Attorney General is seen repeatedly nodding his head as the crowd cheers along.³

Most troubling, however, is that the Attorney General deliberately drew a link between his yet-filed-to-be-filed lawsuit over SB 151 and his collective efforts with the political protestors to defeat their political opponents in the 2018 and 2019 elections. He declared, to a roaring crowd:

[They] broke their promise, but I'm going to keep mine. **We will sue.**
[APPLAUSE] And to this Governor. To this Governor who calls you disgusting. **I call him one and done.**

(emphasis added). All of this was done while standing in front of a sign that read, "CAN YOU SMELL WHAT BEVIN IS COOKING." [See Figure 2].



Figure 2

³ See "Kentucky Attorney General Andy Beshear speaks at teachers rally," Courier Journal, April 2, 2018, online at <https://www.courier-journal.com/videos/news/politics/2018/04/02/kentucky-attorney-general-andy-beshear-speaks-teachers-rally/33474561/> (last visited April 16, 2018).

The Attorney General further implored the crowd to tell the legislators that they will either repeal SB 151 “or you will not reelect them.” [Video at 1:15]. At the end of the video, the Attorney General is seen shaking hands of the protestors while they chant, “Vote them out! Vote them out!” [Video at 1:40].

Nine days later the Attorney General filed this suit *against the very legislators who were recipients of—and who heeded*—his legal advice regarding the legality of the bill. The Attorney General named the Governor, the President of the Kentucky Senate, and the Speaker Pro Tempore of the Kentucky House of Representatives as defendants, as well as two other executive agencies that could participate in implementing the law. The President and Speaker Pro Tempore, of course, oversaw passage of SB 151 as the two presiding officers of their respective legislative chambers. The Governor signed the bill and is constitutionally charged with executing it. All three individuals are officers of the Commonwealth and statutory clients of the Attorney General. Yet all three have been sued by their own lawyer.

ARGUMENT

The Attorney General must be disqualified from prosecuting this case because he and his office are prohibited by the Kentucky Rules of Professional Conduct from bringing suit against the Commonwealth regarding the passage and execution of SB 151. The bottom line here is that the Attorney General provided legal advice to the Defendants regarding these exact issues. As a result, he is ethically prohibited from suing the Defendants over this same issue.

Under the Rules of Professional Conduct, attorneys cannot engage in representation that creates certain conflicts of interest. An impermissible conflict of

interest typically arises when an attorney undertakes a representation adverse to another client without consent. *See* SCR 3.130(1.7). Rule 1.7 states that “a lawyer shall not represent a client if the representation involves a concurrent conflict of interest,” which exists if the representation “will be directly adverse to another client[.]” Likewise, Rule 1.9 states that “[a] lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same or substantially related matter in which that person’s interests are materially adverse to the interests of the former client” SCR 3.130(1.9)(a). Both rules embody the same common-sense principle that a lawyer cannot provide a client with legal advice only to turn around and sue that same client the next week.

That is exactly what has happened here. The Attorney General is the chief law officer and advisor of the Commonwealth and has a statutory duty to provide every state agency and officer with legal advice. *See* KRS 15.020. Pursuant to that duty, on February 28, 2018, the Attorney General in fact provided a six-page legal memorandum to the members of the legislature regarding the legal issues he perceives with the pension-reform measures debated by the General Assembly. [Ex. A]. One week later, he followed up with a second legal memorandum, again reiterating that he was providing advice to legislators in his capacity as the Commonwealth’s chief legal officer. [Ex. B]. The Attorney General then met with Democratic Party legislative leaders in the General Assembly after SB 151 passed specifically “to discuss legal options on [the] pension bill.” [See Figure 1, *supra*]. He repeatedly reached out pursuant to his statutory duties under KRS 15.020 to provide

legal advice to the General Assembly regarding SB 151. And the legislators accepted some of his advice, omitting from SB 151 some of the provisions that the Attorney General had advised them to delete. Yet, the Attorney General has now filed suit against those same legislators, as well as against the executive branch agencies lawfully obligated to execute the laws passed by the General Assembly. This is a blatant violation of both Rule 1.7 and Rule 1.9 of the Professional Rules of Conduct.

A similar issue arose in *People ex rel. Deukmejian v. Brown*, a case in which the Supreme Court of California held that the Attorney General was ethically prohibited from bringing suit against a public official or agency after providing legal advice to the state on the same issue. 624 P.2d 1206, 1207 (Cal. 1981). As here, the issue was whether the Attorney General of California could file suit against the Governor regarding the constitutionality of a law passed by the state legislature. This presented the same question now before this Court: “whether the Attorney General may represent clients one day, give them legal advice with regard to pending litigation, withdraw, and then sue the same clients the next day on a purported cause of action arising out of the identical controversy.” *Id.* The Supreme Court of California correctly held that this violated an attorney’s ethical duties and that there was “no . . . ethical authority for such conduct by the Attorney General.” *Id.*

Here, the Attorney General provided legal advice to the General Assembly and all of its members regarding the exact controversy he has now filed suit over. He is, according to KRS 15.020, the chief legal advisor for the Commonwealth, and he entered into an attorney-client relationship the moment he offered his advice.

Moreover, the General Assembly followed at least part of the legal guidance he provided. He cannot now turn around and sue those to whom he has provided legal advice regarding the same issues he advised them on. Doing so violates the Rules of Professional Conduct, and any other attorney would be immediately disqualified for such action. The Attorney General should be treated no differently, and he and his office must be prohibited from continuing this suit.⁴ The Attorney General might be an elected official, but that does not relieve him of the obligation to follow the ethics rules that govern all lawyers.⁵

CONCLUSION

Conflicts of interest do not disappear simply because the Attorney General says that a case is a matter of great public importance. Kentucky has adopted strict rules regarding conflicts for its attorneys. The Attorney General's suit violates those rules, and therefore, this Court must disqualify him and his office from this action to protect

⁴ If the Attorney General and his office are disqualified, the remaining Plaintiffs will be in position to ably prosecute their claims through competent legal counsel of their own.

⁵ His conduct here also appears to be inconsistent with the Executive Branch Ethics Code. The Ethics Code requires that “a public servant shall work for the benefit of the people of the commonwealth” and not his own private interests. See KRS 11A.005(1). More specifically, it provides that the Attorney General cannot “[u]se or attempt to use his influence in any matter which involves a substantial conflict of interest between his personal or private interest and his duties in the public interest[.]” KRS 11A.020(1)(a). Given the nakedly partisan rhetoric that the Attorney General has employed with respect to this lawsuit, it is abundantly clear that he is using his public office to further his private political interests. After all, the Attorney General appeared at a political rally on April 2 at which he promised protestors that he would file suit over SB 151, and then—*in his very next breath*—referred to Governor Bevin as “one and done.” The intersection between the Attorney General's public duties and his own private political interests could not be clearer.

the integrity of the judicial system. The Attorney General's Office is a serious office that ought to be used for the good of the Commonwealth; it is not a blunt instrument to be used by hyper-partisan, overly ambitious politicians to bludgeon their enemies so they can climb to the next rung of the political ladder.

Respectfully submitted,

/s/ M. Stephen Pitt

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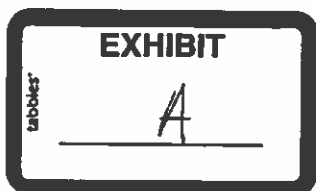
Counsel for Governor Bevin

CERTIFICATE OF SERVICE

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/s/ M. Stephen Pitt

Counsel for Governor Bevin



COMMONWEALTH OF KENTUCKY
OFFICE OF THE ATTORNEY GENERAL

ANDY BESHEAR
ATTORNEY GENERAL

February 28, 2018

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Kentucky Legislators
702 Capitol Ave
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Frankfort KY 40601

Re: Senate Bill 1

Dear Legislators:

Last week, Senate Bill 1 ("SB 1") was filed in the General Assembly. SB 1 seeks to substantially alter and ultimately reduce the retirement benefits for current and future state, city, and county retirees including teachers, police officers, firefighters, and social workers. The Attorney General's Office was not provided any advanced copy of SB 1. This letter is therefore our first opportunity to advise you on the multiple legal violations that we have thus far identified within the bill's 289 pages.

As you know, you – the General Assembly – created an inviolable contract between the Commonwealth and its public employees. You passed this contract into law as KRS 21.480, KRS 61.692, KRS 78.852, and KRS 161.714. Under those laws, you promised Kentucky's public employees that, in exchange for their public service, they would be guaranteed certain retirement benefits. You declared these promises to be inviolable, meaning that you could not later break them.¹

The Commonwealth's public employees have upheld their end of the contract, working for decades on behalf of our Kentucky families. The General Assembly, on the other hand, will violate the contract if it passes the current version of SB 1 into law, as it would materially reduce, alter, or impair the contract's guaranteed benefits. For teachers, SB 1 unlawfully reduces cost of living adjustments, caps the use of sick time, extends years of service to qualify for some benefits, and forces teachers to contribute significantly more of their salaries to their retirement. For state police officers, state employees, and county employees, the bill unlawfully changes how public employees' retirement is calculated, reduces or caps sick leave benefits, and imposes new deductions on already strapped salaries.

Below, I have provided an initial description of some of the most serious violations:

1. **Kentucky Teachers**

The General Assembly created an inviolable contract with public educators under KRS Chapter 161. The contract protects benefits provided between KRS 161.220 and KRS 161.710. *See* KRS 161.714. SB 1 amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to KTRS members. Violations include:

¹ *Inviolable*, Black's Law Dictionary (10th ed. 2014) *adj.*: Safe from violation; incapable of being violated. *Inviolable*, The American Heritage Dictionary (2d ed. 1985) *adj.*: Secure from violation or profanation.

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- **Reduction of Cost of Living Adjustments:** The inviolable contract guarantees teacher retirees a 1.5% annual COLA. *See* KRS 161.620(2). SB 1, Section 73 reduces the annual member COLA from 1.5% to 0.75%. This reduction may reduce retirement benefits by up to \$73,000. As such, it materially impairs the rights and benefits due to retirees, and therefore violates the inviolable contract. *See e.g.*, OAG 17-031.
- **Mandatory Annual Contribution Increases:** Under the inviolable contract, teachers are required to contribute a defined amount of their annual compensation to the retirement system's health fund. *See* KRS 161.540. SB 1, Section 57 mandates that the KTRS governing board increase member contributions by up to one percent (1%) annually under certain conditions. This increase materially impairs the rights guaranteed to KTRS members and therefore violates the inviolable contract.
- **Cap of Sick Time Used to Increase Service Credit:** The inviolable contract does not cap the amount of accrued sick leave that teachers who started before July 1, 2008, may convert to additional service credit for purposes of their retirement. *See* KRS 161.623. SB 1, Section 74 caps the amount of accrued sick leave that members may convert to the amount accrued as of July 31, 2018. This limitation materially alters and impairs the rights and benefits due to employees who started before July 1, 2008, and therefore violates the inviolable contract.
- **Increase of Years of Service Requirement For 3% Benefit Factor:** The KTRS pension plan guarantees a 3% benefit factor for calculating retirees' retirement allowances, if the member has 30 years of service. *See* KRS 161.620. SB 1, Section 73 increases the service years required for this 3% benefit factor, limiting it to employees retiring with thirty (30) years of service, who have at least twenty (20) years of that service as of July 1, 2018. While members without twenty (20) years of service may still receive the 3% benefit factor, they are forced to work thirty-five (35) years and be at least age sixty (60) upon retirement to receive the factor. Because this increase materially alters the contractual service requirements and guaranteed benefits related thereto, it violates the inviolable contract.

2. Kentucky Employees

The Kentucky Employees Retirement System ("KERS") pension rights and benefits are located at KRS Chapter 61, with the inviolable contract found in KRS 61.510-61.705. *See* KRS 61.692. SB 1 amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to KERS members. Violations include:

- **Excludes Compensatory Time Payments From Creditable Compensation:** The inviolable contract allows lump-sum payments for compensatory time to be included in the creditable compensation of Tier I nonhazardous employees.² *See* KRS 61.510. SB 1, Section 14 expressly excludes lump-sum payments from creditable compensation for non-hazardous, Tier I employees, retiring after July 1, 2023. This exclusion materially alters and impairs the ultimate calculation of KERS members' retirement allowances, and therefore violates the inviolable contract.
- **Eliminates Uniform and Equipment Allowances From Creditable Compensation:** Under the inviolable contract, uniform and equipment allowances may be included in KERS members'

² Tier I employees began their employment prior to September 1, 2008. Tier II employees began their employment on or after September 1, 2008 but prior to January 1, 2014.

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creditable compensation. *See* KRS 61.510. SB 1, Section 14 expressly excludes such allowances, paid on or after January 1, 2019, from creditable compensation. This exclusion materially alters and impairs the ultimate calculation of KERS members' retirement allowances, and therefore violates the inviolable contract.

- **Caps Service Credit For Accumulated Sick Leave:** Under the inviolable contract, KERS Tier I employees are not limited in the amount of service credit they may receive for their accrued, unused sick leave. *See* KRS 61.546. SB 1, Section 16, caps service credit for sick leave for Tier I members who retire on or after August 1, 2018. Effective August 1, 2018, for any KERS member retiring on or after August 1, 2018, the maximum amount of service credited for sick leave would be set by – and could not exceed – the amount credited for balance on July 31, 2018. Because this cap materially impairs the sick leave conversion rights and benefits guaranteed to members, it violates the inviolable contract.
- **Prohibits Use of Sick Leave For Determination of Retirement Eligibility:** The inviolable contract guarantees KERS Tier I members may use accumulated, unused sick leave to determine retirement eligibility. *See* KRS 61.546. SB 1, Section 16 prohibits KERS Tier I employees from using sick leave service credit for retirement eligibility, if they retire on or after August 1, 2018. Because this prohibition materially impairs the rights and benefits due to members, it violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions in any amount from KERS Tier I members' creditable compensation for hospital and medical insurance. *See* KRS 61.702(2)(b). SB 1, Section 30 requires an employer of a KERS Tier I member employed after July 1, 2003 to deduct up to 3% of the member's creditable compensation for purposes of hospital and medical insurance under the plan. Because this provision alters and impairs the ultimate calculation of KERS members' retirement allowances, it violates the inviolable contract.
- **Alters Final Compensation Calculation:** The inviolable contract requires Tier I hazardous employees' final compensation be calculated using the creditable compensation from the three (3) fiscal years the employee was paid the highest average monthly rate. It requires the highest five (5) years for Tier I nonhazardous employees. *See* KRS 61.510. SB 1, Section 14 requires, after January 1, 2019, that Tier I hazardous employees' final compensation be calculated using the creditable compensation from their highest three (3) *complete* fiscal years, and that the highest five (5) *complete* fiscal years be used to calculate for Tier I nonhazardous employees' final compensation. Because SB 1 alters and impairs the final compensation calculation guaranteed to hazardous and nonhazardous Tier I employees, it violates the inviolable contract.
- **Eliminates Guaranteed Annual Interest For Hybrid Cash Balance Plan Participants:** KERS Tier I and Tier II employees who opted into the current hybrid cash balance plan are guaranteed an annual interest credit of at least 4%. *See* KRS 61.597. SB 1, Section 19 removes this guarantee. Because this change materially impairs the rights of these employees, it violates the inviolable contract.

3. Kentucky State Police

The State Police Retirement System ("SPRS") pension rights and benefits are located at KRS Chapter 16, with the inviolable contract found in KRS 16.510-16.645. *See* KRS 16.652. SB 1 amends or

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repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to SPRS members. Violations include:

- **Caps Service Credit For Accumulated Sick Leave:** The inviolable contract guarantees Tier I employees are not limited in the amount of service credit they may receive for their accrued, unused sick leave. *See* KRS 16.645; KRS 61.546. SB 1, Section 16, caps service credit for sick leave for Tier I members who retire on or after August 1, 2018, requiring that the maximum amount of service credited for sick leave be set by – and could not exceed – the amount credited for balance on July 31, 2018. This cap materially impairs rights and benefits due to members, and therefore violates the inviolable contract.
- **Prohibits Use of Sick Leave For Determination of Retirement Eligibility:** The inviolable contract guarantees SPRS Tier I members may use accumulated, unused sick leave to determine retirement eligibility. *See* KRS 16.645; KRS 61.546. SB 1, Section 16 prohibits SPRS Tier I employees from using sick leave service credit for retirement eligibility, if they retire on or after August 1, 2018. This prohibition materially impairs rights and benefits due to members, and therefore violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions in any amount from SPRS Tier I members' creditable compensation for hospital and medical insurance. *See* KRS 16.645; KRS 61.702(2)(b). SB 1, Section 30 requires an employer of a SPRS Tier I member, employed after July 1, 2003, to deduct up to 3% of the member's creditable compensation for purposes of hospital and medical insurance under the plan. Because this provision alters and impairs the ultimate calculation of SPRS members' retirement allowances, it violates the inviolable contract.

4. County Employees

The County Employees Retirement System ("CERS") pension rights and benefits are located at KRS Chapter 78, with the inviolable contract found in KRS 78.510-78.852. *See* KRS 78.852. SB 1 amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to CERS members. Violations include:

- **Excludes Compensatory Time Payments From Creditable Compensation:** The inviolable contract allows lump-sum payments for compensatory time to be included in the creditable compensation of Tier I nonhazardous employees. *See* KRS 78.510. SB 1, Section 15 expressly excludes lump-sum payments from creditable compensation for non-hazardous, Tier I employees, retiring after July 1, 2023. This exclusion materially alters and impairs the ultimate calculation of CERS members' retirement allowances and therefore violates the inviolable contract.
- **Eliminates Uniform and Equipment Allowances From Creditable Compensation:** Currently, uniform and equipment allowances may be included in CERS members' creditable compensation. *See* KRS 78.510. SB 1, Section 15 expressly excludes uniform and equipment allowances, paid on or after January 1, 2019, from creditable compensation. This exclusion materially alters and impairs the ultimate calculation of CERS members' retirement allowances, and therefore violates the inviolable contract.
- **Caps Service Credit For Accumulated Sick Leave:** The inviolable contract guarantees that CERS Tier I employees are not limited to the amount of service credit they may receive for his or

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her accrued, unused sick leave. Tier II employees can receive up to twelve (12) months of service credit. *See* KRS 78.616. SB 1, Section 17, caps service credit for sick leave for CERS members who retire on or after August 1, 2018, requiring the maximum amount of service credited for sick leave be set by – and not exceed – the amount credited for balance on July 31, 2018. Because the cap materially impairs the sick leave rights and benefits due to CERS members, it violates the inviolable contract.

- **Prohibits Use of Sick Leave For Determination of Retirement Eligibility:** The inviolable contract guarantees CERS members may use accumulated, unused sick leave to determine retirement eligibility. *See* KRS 78.616. SB 1, Section 17 prohibits CERS employees from using sick leave service credit for retirement eligibility, if they retire on or after August 1, 2018. This prohibition materially impairs rights and benefits guaranteed to CERS members, and therefore violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions, in any amount, from CERS Tier I members' creditable compensation for hospital and medical insurance. *See* KRS 78.545; KRS 61.702(2)(b). SB 1, Section 30 requires an employer of a CERS Tier I member, employed after July 1, 2003, to deduct up to 3% of the member's creditable compensation for purposes of hospital and medical insurance under the plan. As this provision alters and impairs the ultimate calculation of CERS members' retirement allowances, it violates the inviolable contract.
- **Alters Final Compensation Calculation:** The inviolable contract requires CERS Tier I hazardous employees' final compensation to be calculated using the creditable compensation from the three (3) fiscal years the employee was paid the highest average monthly rate. It requires the highest five (5) years for CERS Tier I nonhazardous employees. *See* KRS 78.510. SB 1, Section 15 requires, after January 1, 2019, that CERS Tier I hazardous employees' final compensation be calculated using the creditable compensation from their highest three (3) *complete* fiscal years, and that the highest five (5) *complete* fiscal years be used to calculate CERS Tier I nonhazardous employees' final compensation. Because this provision alters and impairs the ultimate calculation of CERS members' retirement allowances, it violates the inviolable contract.
- **Eliminates Guaranteed Annual Interest For Hybrid Cash Balance Plan Participants:** CERS Tier I and Tier II employees who opted into the current hybrid cash balance plan are guaranteed an annual interest credit of at least 4%. *See* KRS 61.597; *see also*, KRS 78.545. SB 1, Section 19 removes this guarantee. Because this change materially impairs the rights of these employees, it violates the inviolable contract.

Based on the above, if passed into law, SB 1 would unquestionably breach the inviolable contract. Additional violations of the contract likely exist, as this analysis is limited to our initial review of the 289 page bill. However, at this time it is clear that if you pass SB 1 into law, you should expect numerous lawsuits, which the Commonwealth will lose.

Specifically, should you pass SB 1 and thereby break the inviolable contract, a court must determine whether that breach violates the Contracts Clause of the United States Constitution and Section 19 of the Kentucky Constitution. However, the Kentucky Supreme Court has held: “[a]ny reduction or demonstrable threat to those promised benefits might well run afoul of” Kentucky’s Constitution. *Jones v. Bd. of Trustees of Kentucky Ret. Sys.*, 910 S.W.2d 710, 713 (Ky. 1995). It is our conclusion that a court will not uphold any of the violations in SB 1.

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As the chief law officer of the Commonwealth and the people's lawyer, I took an oath to protect the Constitution. You took that same oath. In that light, I urge you to take the necessary and appropriate steps to address these legal concerns and any others that might arise during the legislative process. If another agency is willing to provide its legal analysis, I would be happy to review it and provide additional comments.

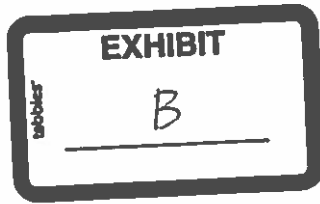
I would also strongly suggest that, instead of passing SB 1, you consider legalizing expanded gaming. By doing so, you can create a dedicated revenue stream that will begin to address the unfunded liability, and will do so without raising taxes.

If you would like to discuss the concerns I have raised, please feel free to contact me. I remain committed to working with you to protect Kentucky families and our valued public employees.

Sincerely,



Andy Beshear
Attorney General



COMMONWEALTH OF KENTUCKY
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March 6, 2018

Kentucky Legislators
702 Capitol Ave
Capitol Annex
Frankfort, KY 40601

Sent via Email

Re: Proposed Senate Substitute for Senate Bill 1

Dear Legislators:

Last week, I provided you a letter stating Senate Bill 1 ("SB 1"), if passed, would violate the inviolable contract that you, the General Assembly, made with Kentucky's public employees. My office's initial review of SB 1 identified at least twenty-one (21) such violations of the inviolable contract. Since that time, a Proposed Senate Substitute ("PSS") has been published.¹ As with the initial bill, the Office of the Attorney General was not provided with any advanced copy of the 293-page PSS for review.

Having now reviewed the PSS, we find that it fails to cure *any* of the twenty-one (21) violations identified in SB 1, including unlawful reductions in cost of living adjustments for teachers, caps on the use of sick time, and alterations to retirement allowance calculations.

As you know, the General Assembly promised Kentucky's public employees that, in exchange for their public service, they would be guaranteed certain retirement benefits. This promise was made in the form of a contract, which was passed into law. *See* KRS 21.480; KRS 61.692; KRS 78.852; KRS 161.714. The statutes passed by the General Assembly declared this contract to be "inviolable," meaning the General Assembly could not later break it.

If passed into law the PSS would breach the inviolable contract, resulting in numerous lawsuits against the Commonwealth – lawsuits the Commonwealth will lose. Like my previous letter, I have provided a description of some of the PSS's violations below:²

¹ As of this date and time of this letter, the Senate Standing Committee for State and Local Government has not adopted the Proposed Senate Substitute, but it is available at <http://www.lrc.ky.gov/SB1PSS.PDF>.

² For a comparison of my review of SB 1 and the Proposed Senate Substitute, please see my letter of February 28, 2018, available at https://ag.ky.gov/pdf_news/20180228_KY-Legislators.pdf.

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1. Kentucky Teachers

The General Assembly created an inviolable contract with public educators under KRS Chapter 161. The contract protects benefits provided between KRS 161.220 and KRS 161.710. *See* KRS 161.714. The PSS amends or repeals these statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to KTRS members. Violations include:

- **Reduction of Cost of Living Adjustments:** The inviolable contract guarantees teacher retirees a 1.5% annual COLA. *See* KRS 161.620(2). Section 73 of the PSS indefinitely reduces the annual member COLA from 1.5% to 1.00%. This reduction significantly reduces guaranteed retirement benefits. As such, the PSS materially impairs the rights and benefits due to retirees, and therefore violates the inviolable contract. *See e.g.*, OAG 17-031.
- **Mandatory Annual Contribution Increases:** Under the inviolable contract, teachers are required to contribute a defined amount of their annual compensation to the retirement system's health fund. *See* KRS 161.540. Section 57 of the PSS mandates that the KTRS governing board increase member contributions by up to one percent (1%) annually under certain conditions. This increase materially impairs the rights guaranteed to KTRS members and therefore violates the inviolable contract.
- **Cap of Sick Time Used to Increase Service Credit:** The inviolable contract does not cap the amount of accrued sick leave that teachers who started before July 1, 2008, may convert to additional service credit for purposes of their retirement. *See* KRS 161.623. Section 74 of the PSS caps the amount of accrued sick leave that members may convert to the amount accrued as of December 31, 2018. This limitation materially alters and impairs the rights and benefits due to employees who started before July 1, 2008, and therefore violates the inviolable contract.
- **Increase of Years of Service Requirement for 3% Benefit Factor:** The KTRS pension plan guarantees a 3% benefit factor for calculating retirees' retirement allowances, if the member has 30 years of service. *See* KRS 161.620. Section 73 of the PSS increases the service years required for this 3% benefit factor, limiting it to employees retiring with thirty (30) years of service, who have at least twenty (20) years of that service as of July 1, 2018. While members without twenty (20) years of service may still receive the 3% benefit factor, they are forced to work thirty-five (35) years and be at least age sixty (60) upon retirement to receive the factor. Because this increase materially alters the contractual service requirements and guaranteed benefits related thereto, it violates the inviolable contract.

2. Kentucky Employees

The Kentucky Employees Retirement System ("KERS") pension rights and benefits are located at KRS Chapter 61, with the inviolable contract found in KRS 61.510-61.705. *See* KRS 61.692. The PSS amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to KERS members. Violations include:

- **Excludes Compensatory Time Payments from Creditable Compensation:** The inviolable contract allows lump-sum payments for compensatory time to be included in the creditable

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compensation of Tier I nonhazardous employees.³ See KRS 61.510. Section 14 of the PSS expressly excludes lump-sum payments from creditable compensation for non-hazardous, Tier I employees, retiring after July 1, 2023. This exclusion materially alters and impairs the ultimate calculation of KERS members' retirement allowances, and therefore violates the inviolable contract.

- **Eliminates Uniform and Equipment Allowances from Creditable Compensation:** Under the inviolable contract, uniform and equipment allowances may be included in KERS members' creditable compensation. See KRS 61.510. Section 14 of the PSS expressly excludes such allowances as well as undefined "other expense allowances," paid on or after January 1, 2019, from creditable compensation. This exclusion materially alters and impairs the ultimate calculation of KERS members' retirement allowances, and therefore violates the inviolable contract.
- **Caps Service Credit for Accumulated Sick Leave:** Under the inviolable contract, KERS Tier I employees are not limited in the amount of service credit they may receive for their accrued, unused sick leave. See KRS 61.546. Section 16 of the PSS caps service credit for sick leave for Tier I members who retire on or after January 1, 2019. Effective January 1, 2019, for any KERS member retiring on or after January 1, 2019, the maximum amount of service credited for sick leave would be set by – and could not exceed – the amount credited for balance on December 31, 2018. Because this cap materially impairs the sick leave conversion rights and benefits guaranteed to members, it violates the inviolable contract.
- **Prohibits Use of Sick Leave for Determination of Retirement Eligibility:** The inviolable contract guarantees KERS Tier I members may use accumulated, unused sick leave to determine retirement eligibility. See KRS 61.546. Section 16 of the PSS prohibits KERS Tier I employees from using sick leave service credit for retirement eligibility, if they retire on or after January 1, 2019. Because this prohibition materially impairs the rights and benefits due to members, it violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions in any amount from KERS Tier I members' creditable compensation for hospital and medical insurance. See KRS 61.702(2)(b). Section 30 of the PSS requires an employer of a KERS Tier I member employed after July 1, 2003 to deduct up to 1% of the member's creditable compensation for purposes of hospital and medical insurance under the plan. Because this provision alters and impairs the ultimate calculation of KERS members' retirement allowances, it violates the inviolable contract.
- **Alters Final Compensation Calculation:** The inviolable contract requires Tier I hazardous employees' final compensation be calculated using the creditable compensation from the three (3) fiscal years the employee was paid the highest average monthly rate. It requires the highest five (5) years for Tier I nonhazardous employees. See KRS 61.510. Section 14 of the PSS requires, after January 1, 2019, that Tier I hazardous employees' final compensation be calculated using the creditable compensation from their highest three (3) *complete* fiscal years, and that the highest five (5) *complete* fiscal years be used to calculate for Tier I nonhazardous employees' final compensation. Because the PSS alters and impairs the final compensation calculation guaranteed to hazardous and nonhazardous Tier I employees, it violates the inviolable contract.

³ Tier I employees began their employment prior to September 1, 2008. Tier II employees began their employment on or after September 1, 2008 but prior to January 1, 2014.

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- **Eliminates Guaranteed Annual Interest for Hybrid Cash Balance Plan Participants:** KERS Tier I and Tier II employees who opted into the current hybrid cash balance plan are guaranteed an annual interest credit of at least 4%. *See* KRS 61.597. Section 19 of the PSS removes this guarantee. Because this change materially impairs the rights of these employees, it violates the inviolable contract.

3. Kentucky State Police

The State Police Retirement System (“SPRS”) pension rights and benefits are located at KRS Chapter 16, with the inviolable contract found in KRS 16.510-16.645. *See* KRS 16.652. The PSS amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to SPRS members. Violations include:

- **Caps Service Credit for Accumulated Sick Leave:** The inviolable contract guarantees Tier I employees are not limited in the amount of service credit they may receive for their accrued, unused sick leave. *See* KRS 16.645; KRS 61.546. Section 16 of the PSS caps service credit for sick leave for Tier I members who retire on or after January 1, 2019, requiring that the maximum amount of service credited for sick leave be set by – and could not exceed – the amount credited for balance on December 31, 2018. This cap materially impairs rights and benefits due to members, and therefore violates the inviolable contract.
- **Prohibits Use of Sick Leave for Determination of Retirement Eligibility:** The inviolable contract guarantees SPRS Tier I members may use accumulated, unused sick leave to determine retirement eligibility. *See* KRS 16.645; KRS 61.546. Section 16 of the PSS prohibits SPRS Tier I employees from using sick leave service credit for retirement eligibility, if they retire on or after January 1, 2019. This prohibition materially impairs rights and benefits due to members, and therefore violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions in any amount from SPRS Tier I members’ creditable compensation for hospital and medical insurance. *See* KRS 16.645; KRS 61.702(2)(b). Section 30 of the PSS requires an employer of a SPRS Tier I member, employed after July 1, 2003, to deduct up to 1% of the member’s creditable compensation for purposes of hospital and medical insurance under the plan. Because this provision alters and impairs the ultimate calculation of SPRS members’ retirement allowances, it violates the inviolable contract.

4. County Employees

The County Employees Retirement System (“CERS”) pension rights and benefits are located at KRS Chapter 78, with the inviolable contract found in KRS 78.510-78.852. *See* KRS 78.852. The PSS amends or repeals these very statutes, thereby unlawfully and materially reducing, altering, or impairing pension benefits due to CERS members. Violations include:

- **Excludes Compensatory Time Payments from Creditable Compensation:** The inviolable contract allows lump-sum payments for compensatory time to be included in the creditable compensation of Tier I nonhazardous employees. *See* KRS 78.510. Section 15 of the PSS expressly excludes lump-sum payments from creditable compensation for non-hazardous, Tier I employees, retiring after July 1, 2023. This exclusion materially alters and impairs the ultimate calculation of CERS members’ retirement allowances and therefore violates the inviolable contract.

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- **Eliminates Uniform and Equipment Allowances from Creditable Compensation:** Currently, uniform and equipment allowances may be included in CERS members' creditable compensation. *See* KRS 78.510. Section 15 of the PSS expressly excludes uniform and equipment allowances as well as undefined "other expense allowances," paid on or after January 1, 2019, from creditable compensation. This exclusion materially alters and impairs the ultimate calculation of CERS members' retirement allowances, and therefore violates the inviolable contract.
- **Caps Service Credit for Accumulated Sick Leave:** The inviolable contract guarantees that CERS Tier I employees are not limited to the amount of service credit they may receive for their accrued, unused sick leave. Tier II employees can receive up to twelve (12) months of service credit. *See* KRS 78.616. Section 17 of the PSS caps service credit for sick leave for CERS members who retire on or after January 1, 2019, requiring the maximum amount of service credited for sick leave be set by – and not exceed – the amount credited for balance on December 31, 2018. Because the cap materially impairs the sick leave rights and benefits due to CERS members, it violates the inviolable contract.
- **Prohibits Use of Sick Leave for Determination of Retirement Eligibility:** The inviolable contract guarantees CERS members may use accumulated, unused sick leave to determine retirement eligibility. *See* KRS 78.616. Section 17 of the PSS prohibits CERS employees from using sick leave service credit for retirement eligibility, if they retire on or after January 1, 2019. This prohibition materially impairs rights and benefits guaranteed to CERS members, and therefore violates the inviolable contract.
- **Imposes Deductions from Creditable Compensation for Group Hospital and Medical Insurance:** The inviolable contract does not include deductions, in any amount, from CERS Tier I members' creditable compensation for hospital and medical insurance. *See* KRS 78.545; KRS 61.702(2)(b). Section 30 of the PSS requires an employer of a CERS Tier I member, employed after July 1, 2003, to deduct up to 1% of the member's creditable compensation for purposes of hospital and medical insurance under the plan. As this provision alters and impairs the ultimate calculation of CERS members' retirement allowances, it violates the inviolable contract.
- **Alters Final Compensation Calculation:** The inviolable contract requires CERS Tier I hazardous employees' final compensation to be calculated using the creditable compensation from the three (3) fiscal years the employee was paid the highest average monthly rate. It requires the highest five (5) years for CERS Tier I nonhazardous employees. *See* KRS 78.510. Section 15 of the PSS requires, after January 1, 2019, that CERS Tier I hazardous employees' final compensation be calculated using the creditable compensation from their highest three (3) *complete* fiscal years, and that the highest five (5) *complete* fiscal years be used to calculate CERS Tier I nonhazardous employees' final compensation. Because this provision alters and impairs the ultimate calculation of CERS members' retirement allowances, it violates the inviolable contract.
- **Eliminates Guaranteed Annual Interest for Hybrid Cash Balance Plan Participants:** CERS Tier I and Tier II employees who opted into the current hybrid cash balance plan are guaranteed an annual interest credit of at least 4%. *See* KRS 61.597; KRS 78.545. Section 19 of the PSS removes this guarantee. Because this change materially impairs the rights of these employees, it violates the inviolable contract.

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The provisions of the PSS would undeniably breach the guarantees of the inviolable contract by significantly reducing the benefits and rights of retirees. The Kentucky Supreme Court has held that even a "...threat to those promised benefits might well run afoul of" Kentucky's Constitution. *Jones v. Bd. of Trustees of Kentucky Ret. Sys.*, 910 S.W.2d 710, 713 (Ky. 1995). For these reasons, it is our conclusion that a court will not uphold these violations.

As the chief law officer of the Commonwealth and the people's lawyer, I urge that you not break the inviolable contract you made with Kentucky state employees, teachers, firefighters, social workers, police officers, and other hardworking members of these systems.

Sincerely,



Andy Beshear
Attorney General