5-13-2011

CDA Dairy Queen, Inc. v. State Ins. Fund Augmentaion Record Dckt. 38492

In the Supreme Court of the State of Idaho

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE, LLC OF SALMON, Plaintiffs-Appellants, v. STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN, and MAX BLACK, and STEVE LANDON, in their capacity as members of the Board of Directors of the State Insurance Fund, Defendants-Respondents.	)	ORDER GRANTING PLAINTIFFS' MOTION TO AUGMENT THE RECORD Supreme Court Docket No. 38492-2011 Canyon County Docket No. 2009-13607

PLAINTIFFS' MOTION TO AUGMENT THE RECORD was filed by counsel for Appellants on May 11, 2011. Therefore, good cause appearing,

IT HEREBY IS ORDERED that PLAINTIFFS' MOTION TO AUGMENT THE RECORD be, and hereby is, GRANTED and the augmentation record shall include the documents listed below, file stamped copies of which accompanied this Motion:

1. Amended Memorandum in Support of Plaintiffs' Motion for Partial Summary Judgment, file-stamped October 12, 2010;
2. Memorandum in Support of Defendants' Motion for Summary Judgment, file-stamped October 26, 2010;
3. Defendants' Notice of Erratum Re: Memorandum in Support of Defendants' Motion for Summary Judgment, file-stamped October 29, 2010;
4. Memorandum in Opposition to Defendants' Motion for Summary Judgment, file-stamped November 30, 2010;
5. Opposition to Plaintiffs' Motion for Partial Summary Judgment, file-stamped November 22, 2010;

6. Defendants' Notice of Errata Re: Pending Motions, file-stamped December 8, 2010; and
7. Motion to Strike the Affidavit of James M. Alcorn and Selected Exhibits Attached to the Affidavit of Counsel Both of Which Were Filed in Support of Defendants' Motion for Summary Judgment, file-stamped November 22, 2010

DATED this 13th day of May, 2011.

For the Supreme Court

Stephen W. Kenyon

Stephen W. Kenyon, Clerk

cc: Counsel of Record

LAW CLERK

AUGMENTATION RECORD

In the Supreme Court of the State of Idaho

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE, LLC OF SALMON, Plaintiffs-Appellants, v. STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN, and MAX BLACK, and STEVE LANDON, in their capacity as members of the Board of Directors of the State Insurance Fund, Defendants-Respondents.	ORDER GRANTING PLAINTIFFS' MOTION TO AUGMENT THE RECORD Supreme Court Docket No. 38492-2011 Canyon County Docket No. 2009-13607

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DATED this 13th day of May, 2011.

For the Supreme Court

Stephen Kenyon

Stephen W. Kenyon, Clerk

cc: Counsel of Record

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Attorneys for Plaintiffs and the Class

IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT OF THE STATE OF IDAHO, IN AND FOR THE COUNTY OF CANYON

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE LLC OF SALMON,

Plaintiffs,

vs.

THE IDAHO STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its Manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN AND MAX BLACK AND STEVE LANDON in their capacity as member's of the Board of Directors of the State Insurance Fund,

Defendants.

CASE NO. CV 09-13607-C

AMENDED MEMORANDUM IN SUPPORT OF PLAINTIFFS' MOTION FOR PARTIAL SUMMARY JUDGMENT

COME NOW THE PLAINTIFFS, and the members of the class, by and through undersigned counsel, and hereby provide the Court with the following Memorandum in Support of their Motion for Partial Summary Judgment. The basis and grounds for this Motion is the contention that making the 2009 repeal of Idaho Code §72-915 retroactive to January 1st, 2003 is clearly unconstitutional because it unquestionably impairs the obligations of a contract. In so doing it violates Article I, Section 16 of the Constitution of Idaho. ("No bill of attainder, ex post facto law, or law impairing the obligations of contracts shall ever be passed.")

PART I.: STATEMENT OF FACTS

A. INTRODUCTION:

The Idaho State Insurance Fund (hereafter "the Fund") was established by the Idaho Legislature in 1917. *See,* Idaho Code, Title 72, Chapter 9. For the first 92 years of the Fund's existence, its sole authority to pay dividends derived from a single statute, namely I.C. § 72-915, which read as follows:

> **72-915. Dividends.** – At the end of every year, and as such other times as the manager in his discretion may determine, a readjustment of the rate shall be made for each of the several classes of employments or industries. If at any time there is an aggregate balance remaining to the credit of any class of employment or industry which the manager deems may be safely and properly divided, he may in his discretion, credit to each individual member of such class who shall have been a subscriber to the state insurance fund for a period of six (6) months or more, prior to the time of such readjustment, such proportion of such balance as he is properly entitled to, having regard to his prior paid premiums since the last readjustment of rates.

This statute allowed the Fund's Manager the discretion to determine whether to declare a dividend and to determine the total amount of the dividend corpus to be distributed among the Fund's policyholders. Thereafter, the manner of distributing the dividend corpus among the Fund's policyholders is outside of the Manager's discretion. As will be demonstrated below, the

express provisions of the Fund's contract with its policyholders mandates that the dividend corpus will be distributed on a *pro rata* basis. The Fund did not adhere to the provisions of the contract requiring it to distribute any relevant dividend corpus on a *pro rata* basis and it is this failure which underlies the damage claims made in this case.

B. THE HISTORICAL SETTING:

In 1998, the Idaho Legislature passed House Bill 774, which contained a series of changes to Title 72, Chapter 9. Specifically, that legislation amended I.C. §§ 72-901; 902 and 906, and repealed I.C. § 72-911. No mention of I.C. § 72-915 was then made, either by the Bill's sponsor, or by any member of the House or Senate State Affairs Committees, and no version of this legislation contained any reference to I.C. § 72-915. *See Doc # 000001 to Doc # 000077, Affidavit of Philip Gordon In Support of Plaintiffs' Motion for Partial Summary Judgment ¶ 2* (hereinafter "Aff. Gordon").

For the first two policy years following the passage of HB 774 (July 1, 1998 to June 30, 1999, and July 1, 1999 to June 30, 2000 [1]) the State Insurance Fund, acting through its manager and Board of Directors paid dividends using a formula which did not make a *pro rata* allocation of the dividend corpus but which did allow for a distribution of dividend to even its smallest policyholders. *See Doc # 000088 to Doc# 000099 ¶ 3 Aff. Gordon.* In allocating dividends, the formula used the amount of "billed premiums" as a starting point. This amount was then reduced

1. Each of the Fund's dividend distributions is made in respect to a policy period commencing on the July 1st approximately 30 months prior to such distribution, and ending on the following June 30th, i.e. approximately 18 months in advance of such distribution. Thus, the dividends allocated in December 2000, and distributed in January, 2001 pertained to the policies with inception dates falling on or before July 1st 1998 and on or before June 30th 1999. Similarly, the dividends allocated in December 2002, and distributed in January, 2003 -the first distribution to exclude the smaller policyholders- were made in reference to the policy year July 1st 2000 to June 30th 2001.

for retention (to cover underwriting expenses) based upon a percentage of the billed premium paid which percentage was decreased as the amount of billed premium increased. The remaining amount was then reduced by a "loss factor" (1.18 times any losses on the policy). The remaining amount, if any, was multiplied by a "rate of return" (dividend rate) which increased as the amount of billed premium increased. *See Doc # 000088 to Doc# 000099 and Doc # 0000 91 ¶3 & ¶4 Aff. Gordon.*

At its regularly scheduled Board meeting in November, 2002, the Manager and the Board made the decision that, commencing with the dividend corpus which the Fund would distribute in January, 2003, it would no longer pay any dividends to a class of policyholders which had historically been receiving dividends. Specifically, the Board and Manager determined that no dividends whatsoever would be paid to any policyholder whose premium for the applicable period was $2,500.00 or less (hereafter "the smaller policyholders"), and that the entirety of the dividend corpus would be divided only among employers whose annual premiums exceeded $2,500.00 (hereafter "the larger policy holders"). *See Docs #000092 to #000099, ¶ 6 Aff. Gordon.*

In July, 2006, in response to the Fund's decision to deny dividends to those of its policyholders whose premiums were at or under $2,500.00, a class action lawsuit was filed in this Court against the Fund by three named businesses, each of whom was a policyholder of the Fund for one or more years of the designated class period. *See, Farber v. The Idaho State Insurance Fund,* Third Judicial District Court, Canyon County, CV06-7877. The gravamen of that action was a claim that since the named Plaintiffs had not received any dividends for the years of the class period the Fund was in violation of I.C. § 72-915. *See, Farber v. Idaho State Insurance Fund,* 147 Idaho 307, 208 P. 3d 289 (2009) (initial opinion issued 3/5/2009, replacement opinion

following petition for rehearing filed 5/5/2009). In both of its decisions, the Supreme Court determined that Idaho Code § 72-915 clearly and unambiguously required that, for any policy period in respect to which the Fund elected to pay a dividend, the dividend corpus had to be divided among all time-qualified policyholders (those who held their policy for at least six months) *pro rata* based solely upon the amount of the premium which they had paid. Id.147 Idaho 311-312, 208 P. 3d 293-294.

In the two-month interval between the issuance of the two *Farber* opinions, a Bill which attempted to legislatively reverse the decision in *Farber* was introduced in the Idaho Legislature. State Senator John Goedde, a member of the Fund's Board and also a named Defendant in the *Farber* case, presented SB 1166 to the Senate Commerce and Human Resources Committee with the explanation that it would "serve to offset an adverse decision of the Idaho Supreme Court regarding the interpretation of *Idaho Code,* Section 72-915..." *See Doc #000102 to Doc #000109, ¶7 Aff Gordon.* Senate Bill 1166, in its original form, acknowledged the Supreme Court's decision, set out the purported legislative intention in amending the laws relating to the Fund in 1998 and, on the basis that an emergency existed, provided for a repeal Idaho Code 72-915 retroactive to April, 1998. *Doc # 000100 ¶7 Aff Gordon.* When the SB 1166 was presented to the Senate Commerce and Human Resources Committee on April 7, 2010, testimony challenged it as an attempt to impair the rights of contract and a majority of the members voted to hold the Bill in Committee. *Doc #000102 to #000109 ¶7 Aff Gordon* . On April 14, 2010, the Bill came back before the Committee with representations that agreements had been reached to amend the Bill and at that time it was sent to the Senate Amending Order. *Doc #000110 to #000113 ¶7 Aff Gordon* After SB 1166 was amended to be 1) retroactive to January 1, 2003, and 2) to specifically

provide that the Bill was not in any way intended to apply to any claims made in *Farber v. State Insurance Fund*, the Bill (thereafter SB 1166aa. *See Doc #000119 Aff. Philip Gordon*) passed through both the Senate and the House and was signed by the Governor on May 6th, 2009.

Since May, 2009, the Fund issued its Annual Statement for the year ended December 31, 2009. In pertinent part, this Statement showed the following:

a. The "Net Admitted Assets" of the Fund rose by more than 2.5 million dollars from the prior year (Doc # 000117 ; line 26).

b. The unallocated surplus of the Fund ["Unassigned funds (surplus)] grew by more than seven million dollars from that on hand at the end of the prior year (Doc # 000118, lines 33 and 34.2).

c. The amount of "declared and unpaid" dividends to policyholders was the sum of $14,045,136 (Doc #000118, lines 11 and 11.2).

See Doc #000114 to #000118, ¶ 8 Aff Gordon.

C. BACKDROP TO THE INSTANT ACTION:

In the course of pre-trial discovery proceedings in the *Farber* case, it became clear that the Fund had, at least since 2002, violated the terms and conditions of Idaho Code § 72-915 in not simply one, but in three ways. First, the Fund totally excluded from any share of the dividend pool any and all policyholders whose billed premium was $2,500.00 or less (i.e. the Plaintiff class in *Farber).*[2] Second, the Fund computed the dividends to be paid to the larger policy holders (i.e.

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2. During the pendency of the *Farber* case, the Fund lowered its threshold minimum premium for the receipt of some portion of the dividend from $2,500.00 to $1,500.00. Commencing with the first dividend distributed thereafter, policyholders whose premiums exceeded that lower number received **some** dividend. Thus, there may be some members of the class who were members of the class in *Farber,* as to those years in respect to which they received no dividend whatsoever, who will also be

those whose billed premiums exceeded $2,500.00 -or, for some years in the class period, $1,500.00- and who therefore shared in the dividend corpus) not on a flat percentage basis, whereby each qualifying policyholder would receive a *pro rata* share of the total dividend based solely on the size of their billed premium but, instead, using two sliding scales (one for percentage of premium "retained" and one for "return percentage"). The effect of these adjustments was that a policy issued between July 1, 2001 and June 30, 2002 with a billed premium of $5000 (and no losses) would have received a dividend of $187.50 ($0.0375/dollar) and a policy issued during the same period with a $200,000 billed premium (and no losses) would have received a dividend of $40,500 ($.20/dollar) *See e.g. Doc #000097.* Third, as to all policyholders who had losses due to injured employees, the Fund first reduced their billed premiums based upon the amount to be "retained", then the remainder was further reduced by a multiple of 1.18 of the losses paid and then paid them a dividend based upon any portion of the billed premium that was left after these reductions. *See Doc #000091.* All three of these practices violated Idaho Code § 72-915, as interpreted by our Supreme Court in *Farber, supra.*

Each of the named Plaintiffs and all of the members of the class in this cause are Idaho employers who purchased contracts of workers compensation insurance with the Fund for one or more years commencing on July 1st, 2002, and continuing up to January 1st, 2009, i.e. six months prior to the effective date of the act repealing Idaho Code 72-915. *First Amended Complaint ¶¶ 7 and 8.* The Plaintiffs and the members of the class, as a result of the formula used by the Fund, received less than a *pro rata* share of the dividend which the Fund allocated and distributed in one

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members of the Plaintiff class in the instant action, for any year in which they received a dividend, albeit one which was less than their *pro rata* share. In no instance will any person or entity be a member of both classes for the same premium period.

or more of the years during the Class Period. *First Amended Complaint ¶13.*

In consequence of the fact that the dividends which are paid by the Fund relate back to a policy period commencing 30 months prior to payment and concluding 18 months prior to payment *(see FN 1, supra)*, each and every dividend which the Fund has paid during the class period, including the dividend of approximately $14 million dollars paid in January, 2010 (on policies issued on or after July 1, 2007 and on or before June 30, 2008), related to contracts of insurance which were written and had remained in force for more than six months prior to May 6th, 2009, the date on which the Governor signed the enactment repealing Idaho Code § 72-915.[3] In other words, the rights of the Plaintiffs and the members of the class to receive their *pro rata* share of these dividends, and the obligation of the Fund to pay those dividends in accordance with the clear and unambiguous language of I.C.§ 72-915, for each year of the class period, had fully vested prior to the effective date of the repeal of this statute.

Furthermore, another full batch of premiums have been billed for policies issued July 1, 2008 to June 30, 2009. It is reasonable to expect based upon history in late 2010 or early 2011 the Fund will declare, allocate and distribute a dividend relative to these policies. Many of these policyholders will have a claim that their right to a dividend vested before the repeal became effective and others will have a claim that their contractual right to share in the dividend was agreed upon before the Bill became effective.[4] These claims while they may arise and have to be

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[3] Indeed, policies which were issued between July 1, 2008, and November 26, 2010 ,(which will receive a dividend in January 2011, if one is distributed) will also all have been in force for more than 6 months by the time that I.C. 72-915 was repealed (assume the law is effective at all or on May 26, 2010).

[4] If the emergency driven retroactive repeal of I.C. 72-915 is not effective the Court will be later called upon to determine if the repeal is wholly ineffective, if the repeal is effective but that the effective date is July 1, 2009, or if the repeal is effective when the Governor signed the Bill on May 6, 2009. These questions are not, however relevant, to the issues raised in this motion.

addressed in the future do not need to be addressed at this time and are mentioned only so that it will not appear that Plaintiffs' have intended to waive them.

It is clear therefore that the Plaintiffs, and the Class they seek to represent:

1. Had contracts of insurance with the Fund;

2. Were entitled pursuant to the terms of those contracts to receive a *pro rata* share of any dividend corpus that the Fund elected to distribute among policyholders;

3 Have the benefit of a Idaho Supreme Court decision requiring that they be paid a *pro rata* share of any dividend corpus that the Fund elected to distribute, *Farber v. The Idaho State Insurance Fund, supra.*;

4 Will recover a *pro rata* share of the dividend corpus that was distributed only if the legislative repeal of I.C. ¶72-915 is held to be unconstitutional.

PART II.: THE APPLICABLE LAW

A. INTRODUCTION:

The Plaintiffs have moved for Partial Summary Judgment on the limited question of whether or not the Idaho Legislature could make the repeal Idaho Code § 72-915 **retroactive to January 1st, 2003,** without running afoul of Article 1, § 16 of the Constitution of Idaho. Plaintiffs contend that the retroactivity aspect of the statute. *See, Engrossed SB 1166aa, Doc #000119 Aff. Philip Gordon,* is unconstitutional as a matter of law, given that the Idaho Legislature is expressly forbidden by Article 1, §16 of the Idaho Constitution from passing any law which, *inter alia,* impairs the obligations of contracts. That model of categorical brevity reads in full as follows:

> No bill of attainder, ex post facto law, or law impairing the obligation of contracts shall ever be passed.

The repeal of Idaho Code § 72-915, insofar as it affects, or purportedly affects, any contract of insurance which was entered into on or prior to January 1st, 2009, and held for at least 180 days, impairs the obligations of those insurance contracts in violation of this very succinct Constitutional provision.

B. The Idaho Statutes creating the Fund and governing its actions, which are in force at the time the Fund issues any policy of insurance, constitute terms and conditions of such policy. A violation of any of these statutes is, therefore, a breach of the Fund's contract of insurance.

The policies of workers' compensation insurance which the Plaintiffs and the members of the Class purchased from the Defendant Fund are contracts for the provision of insurance coverage. Indeed, Paragraph A of the contract which the Fund supplied to its insureds *(see Exhibit "A" Affidavit of Donald W. Lojek in Support of Plaintiffs' Motion for Partial Summary Judgment, hereinafter Aff Lojek*). The Fund is specifically empowered by statute to enter into contracts to provide insurance and services related to that insurance. Idaho Code § 72-905.

At all times during the class period, the terms and conditions of the contracts between the Fund and its policyholders included not only the provisions of its written policy (*Exhibit "A", Aff Lojek*) but also the Idaho Statutes creating and governing the Fund which are in effect during the policy period.

In 2000, the Idaho Supreme Court decided the case of *Kelso & Irwin, P.A. v. State Insurance Fund; and Drew Forney, Manager of the State Insurance Fund,* 134 Idaho 130; 997 P. 2d 591. Among the various rulings made by the *Kelso* Court was this seminal formulation:

> It is undisputed that Kelso has a contract for worker's compensation insurance with the SIF. Any violation of the provisions of that contract would constitute a breach of contract by the SIF. **Additionally, the contract necessarily incorporates the statutory framework which both created the SIF and governs the actions that**

> **can be taken by the SIF with regard to the SIF's funds.** When Kelso contracted with the SIF it was entitled to rely on the statutes creating and regulating the SIF....Consequently, any act taken by the SIF beyond its statutory authority would also be a breach of the SIF's contract with Kelso. *134 Idaho 130 at 138, 997 P. 2d 591 at 599.* (emphasis added).

Our Supreme Court in *Hayden Lake Fire Protection District v. Alcorn,* 141 Idaho, 388, 111 P. 3d 73 (2005), reiterated this principle and specifically extended it to the statute governing the declaring and distribution of dividends:

> In *Kelso* this Court held that the SIF's governing statutes were incorporated in its contracts with its policyholders. [citation omitted]. *Kelso* also held that policyholders "had a right to rely on the statutes creating and regulating the SIF, and the limits those statutes place on how the SIF can invest its policyholders" premiums.[citation omitted] **This covenant reaches to the SIF's statutory obligations that are incorporated into its contracts. The SIF has duties to its policyholders regarding surplus and dividends by virtue of the fact that the implied covenant of good faith and fair dealing extends the statutes that are incorporated in the policyholders' contracts.** 141 Idaho, 388, 399; 111 P. 3d 73, 84 (emphasis added).

At all times material and relevant to this class action, Idaho Code § 72-915 was one of the statutes governing the actions of the Fund. A breach by the Fund of its duty to distribute the dividend corpus according to the statutory method set forth in Idaho Code § 72-915 thus constituted a breach of the contracts of insurance which the Fund entered into with the Plaintiffs and the members of the Class.

The concept that the laws which create and govern an entity which is a creature of statute (and the Fund is of course such an entity; *See, Kelso, supra)* comprise terms and conditions of the contracts entered into by that entity is not limited to the Fund. Rather, it has been applied by our Idaho Appellate Courts to a variety of governmental and quasi-governmental entities which trace their existence to specific statutes. Thus, in the context of a drainage district ("....we feel certain

that a drainage district is a local improvement district..." *Straus and Nicholson v. Ketchen*, 54 Idaho 56 at 67; 28 P.2d 824 at 828 [Idaho Supreme Court 1933]), our Supreme Court, drawing on precedent from Federal law, concluded that:

> The law is so well settled that the statutes of this state and decisions of the courts, that were in force at the time of the issuance of the bonds in question, became a part of the contract, as between the bondholders and the property owners, that citation of authority is deemed hardly necessary.

C. There is no question that the Idaho Legislature intended the repeal of Idaho Code § 72-915 to have retroactive effect and be applied retroactively.

The very wording of the Bill repealing Idaho Code § 72-915 permits no doubt that the Idaho Legislature intended the repeal to have retroactive effect and be applied retroactively so that certain of the Fund's contractual obligations would be impaired. Making the repeal retroactive to January 1, 2003, as the enactment states, would, were it constitutional, affect the rights of all persons who purchased policies of insurance from the Fund at any time on or after July 1st of the year 2000,[5] up to and including six months prior to the purported effective date of the repeal.[6]

D. The attempt to make the repeal of Idaho Code § 72-915 apply retroactively would operate to eliminate the obligations of the Fund to pay dividends in the manner mandated by the *Farber* Court in respect to the contracts of insurance which the Plaintiffs and the Members of the Class purchased from the fund prior to six months before the purported effective date of the repeal.

Absent retroactive application of the repeal of Idaho Code § 72-915, and given the Idaho

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[5] See FN 1., supra, wherein it is explained that dividends are paid for a policy period commencing approximately 30 months and ending approximately 18 months prior to the payment date of such dividends.

[6] This date represents the last date on which an employer could purchase a policy of worker's compensation insurance from the Fund, and have it be in effect for the six months needed to qualify for a dividend prior to the effective date of the repeal. Since their rights to a dividend would have vested prior to the repeal of the dividend statute, this would represent the last day on which persons who purchased policies with the Fund would have their rights compromised by the attempt to repeal the statute retroactively.

Supreme Court's holding in *Farber, supra,* the Plaintiffs and the Members of the Class, once they held their policies of workers compensation insurance with the Fund for six months prior to the effect date of the repeal, would have a vested right to receive, and the Fund would have an obligation to pay to them, for each year in the class period, a *pro rata* share of the total dividend corpus paid out, based solely on the amount of the premiums they paid.[7]

As the *Farber* Court explained the obligatory method of allocating the dividend corpus:

> The statute contemplates dividing the aggregate balance *proportionately* according to the policyholder's *prior paid premiums* relative to all paid premiums. To argue that this language could be construed to somehow grant discretion regarding how to calculate the distribution makes no sense, and would require this Court to stretch the plain language beyond its obvious meaning. 208 P. 3d 294.

Implementation of *Farber* with respect to the Plaintiffs and the Class in the instant matter would thus unquestionably result in the Fund having to meet its financial obligations to the Plaintiffs and the members of the Class. Should, however, the repeal of § 72-915 be allowed to be applied retroactively to one or more of the years in the class period, the first and most crucial corollary to such a ruling would be that the Plaintiffs and the members of the Class would have no contractual basis on which to claim their *pro rata* share of the dividends distributed in each of the years in the class period. Rather, they would have to content themselves with the receipt of a dividend less than they would have been entitled to had the Fund properly applied I.C. § 72-915, or, in some cases, no dividend whatsoever. Therefore, by definition, the obligation of the Fund to pay dividends to the

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[7] This Memorandum does not intend to adopt any position with regard to what might be the effective date of the repeal of I.C. § 72-915 if, as is argued here, the Court finds that making that repeal retroactive is unconstitutional. Should the Court adopt Plaintiffs' position regarding the constitutionality of retroactive application, the repeal may well only become effective on July 1, 2009, along with all other legislative enactments from the 2009 legislature, which have not been defined by the legislature as having some other or different effective date.

Plaintiffs and the members of the Class, *pro rata*, as spelled out in *Farber, supra,* and the vested right of the Plaintiffs and the members of the Class to receive such dividends would, for each year of the class period, be impaired by this unconstitutional exercise of legislative power.

E. The attempt to make the repeal of Idaho Code § 72-915 retroactive violates Article 1, § 16 of the Idaho Constitution.

Article 1, Section 16 of the Idaho Constitution, quoted above, has been uniformly and consistently construed by the Idaho Supreme Court in a manner which supports Plaintiffs' Motion for Partial Summary Judgment. By making the 2009 repeal of Idaho Code § 72-915 retroactive to January 1st, 2003, the vested contractual entitlement of the Plaintiffs (and the Class which they represent) to receive a *pro rata* share of the dividend corpus distributed by the State Insurance Fund during each year of the class period has been totally eliminated. If this is not an "impairment" of a contractual right, then it beggars the imagination to construct a more egregious example. Because the policies of insurance written by the Fund have, over the years involved in this litigation, incorporated the terms of I.C. § 72-915 and made those terms a part of each contract, the retroactive repeal of the statute will clearly operate to deprive Plaintiffs of property to which they would have otherwise been entitled. This attempt by the legislature is plainly a violation of Idaho's constitutional ban on legislation which impairs the obligations of contracts.

Plaintiffs are not taking any position on the **prospective** effect of the repeal of I.C. § 72-915. However, the retroactive effect unquestionably deprives them of their vested contractual rights to the receipt of certain additional dividend payments and eliminates the Funds' obligations to make those payments, and thus violates the Idaho Constitution.

In *Fidelity State Bank v. North Fork Highway District*, 35 Idaho 797, 209 P. 449 (1922), the

Highway District brought suit to enforce a trust on the general funds and estate of the insolvent Bank. The case was tried on a set of stipulated facts, which are set forth in great detail at 35 Idaho 803-805. In essence, the District kept a portion of its money on deposit in the Bank. The money had been deposited in the Bank by the Highway District's Treasurer, as a "general deposit", with the result that the District's funds were in danger of being regarding as commingled with the bank's general funds. At the time all of the deposits were made by the District Treasurer, an Idaho law forbade such officials "from depositing the funds of a highway district in banks other than upon special deposit." 35 Idaho 807. Prior to the enactment of that law, the Idaho Supreme Court:

> held that although public moneys were deposited other than upon special deposit, they remained nevertheless a trust fund, and in case of the insolvency of the bank it was the duty of the receiver to treat such funds as a trust fund and the property of the true owner, and that creditors of such bank were not to share *pro rata* in the public money. (Citation omitted.) And again in the case of *First National Bank v. C. Bunting & Co., 7 Idaho 27, 59 P. 929,* it was held that public monies deposited in a bank in violation of law are trust funds and do not become the property or assets of such bank, and remain trust funds, with the title in the true owner after the appointment of a receiver of the insolvent bank, and that a county whose funds have been unlawfully deposited in a bank is not estopped from claiming such funds..... Prior to the enactment of [the new statute] the moneys of the district, illegally deposited in the bank upon general deposit, remained the property of the district, and the title did not pass to the bank, neither did the relationship of debtor and creditor arise between the bank and the district. 35 Idaho 807-8.

After all of the District's deposits were made, and before the Bank was taken over on April 8th, 1921, Chapter 42 of the Session Laws of 1921 went into effect. 35 Idaho 806. This law, quoted in full at 35 Idaho 810, would have had the effect of abrogating the *de jure* contract of special deposit between the Highway District and the Bank, by lumping the deposited funds of the Highway District together with all of the Bank's general deposits. This would have meant that the debt owing to the District had the same priority as debts due all other depositors. *Ibid.* The new law had a retroactive

effect. If the Court permitted the law to be applied retroactively, the District would have lost its deposited funds because they would have lost their "trust fund" character, and would instead have been treated as general deposits.

The Court found that allowing the new enactment to control the nature, character and priority of the District's funds would impair the obligation of the contracts made when the District deposited its money in the Bank. The holding was that the law in existence when the deposits were made, as quoted above, would control the characterization of these public funds, with the result that the Highway District would be in a first position to get its money back. The Court's ruling prevented the *de jure* status of these public funds from being altered retroactively.

Our Supreme Court then cited with approval a U.S. Supreme Court case *Von Hoffman v. Quincy*, 4 Wall (U.S.) 535, 18 L.Ed. 403 which stated "it is also settled that the laws which subsist at the time and place of the making of a contract, and where it is to be performed, enter into and form a part of it, as if they were expressly referred to or incorporated in its terms. This principle embraces alike those which affect its validity, constructions, discharge, and enforcement."

The *Fidelity* opinion goes on to address the constitutional implications involved in attempting to apply the new statute retroactively in the following terms:

> Any enactment of a legislative character is said to "impair" the obligation of a contract which attempts to take from a party a right to which he is entitled by its terms or which deprives him of the means of enforcing such a right. *35 Idaho 797, 810.*
>
> A law enacted subsequent to a contract which, if valid, will have the effect of annulling the contract constitutes the most palpable form of legislative impairment, and such an enactment is clearly unconstitutional. *Id.*
>
> Legislation that attempts to make material alterations in the character,

> terms, or legal effect of existing contracts is clearly void. Of this character are statutes which attempt to add a material condition or provision to a contract, and those which attempt to release material stipulations contained therein. *Id.*

The Supreme Court then concluded that the legislation in question "interfered" with the contract between the Bank and the Highway District and was therefore unconstitutional, stating:

> It is a well-known fundamental rule of law that a state by the act of its legislature cannot alter the nature or legal effect of an existing contract to the prejudice of either party, nor can the legislature make a law for a particular case between two contracting parties contrary to the existing law and require the courts to enforce it. This rule is founded on two distinct principles of constitutional law, one prohibiting the assumption of judicial power by the legislative department, and the other inhibiting the impairment by a state of the obligation of contracts. The obligation of a contract is impaired by a statute which alters its terms, by imposing new conditions or dispensing with conditions, or which adds new duties or releases or lessens any part of the contract obligation or substantially defeats its ends. . .*35 Idaho 797 at 812-813.*

This reading of the Idaho Constitution and the "fundamental rule of law" announced therein have remained intact from 1922 to the present day.

Penrose v. Commercial Traveler's Insurance Co., 75 Idaho 524, 275 P.2d 969 (1954), was an insurance case which directly implicated Article 1, Section 16. The Idaho Supreme Court once again found that legislation retroactively affecting existing contracts was in violation of the "impairment of the obligations of contracts" provision of the Idaho Constitution. There, the offending statute provided that if an insurance company failed to pay an insured whatever was justly due under the policy then attorney's fees could be awarded by the court. In the case, a farmer obtained a policy of disability insurance with the defendant insurance company and, after a period of time, he became ill. The insurance company questioned whether or not he was totally disabled and therefore eligible for benefits under the policy. The Supreme Court affirmed the district court

and allowed coverage. Because the new attorneys fees law passed while the contract was in force, the district court also awarded attorney's fees against the insurer. The Supreme Court reversed that part of the District Court's decision allowing attorney's fees. Three separate opinions were written.

While the majority opinion on the issue of retroactive legislation and its unconstitutionality when affecting contracts in existence is remarkably short, the three justices comprising the majority buttress their opinion that the retrospective application of attorneys' fee statutes is unconstitutional by referring to the plethora of cases cited in the lead opinion at *75 Idaho 538*, which support their holding. In reliance on those cases, they conclude: ". . . to apply the statute enacted after the insurance policy was written impairs the obligation of contract." *75 Idaho 540.* So, too, here.

The lead opinion on the coverage issue also addressed the retroactive effect of attorney's fees, and its author observed that a retroactive statute "is not unconstitutional merely because it is retrospective. . . . It is rendered unconstitutional if it impairs contractual obligations, violates due process or disturbs vested rights." 75 Idaho 524, 537.

The majority concluded that the new law contravened Article 1, § 16 of the Constitution of Idaho insofar as it acted on or affected an existing contract of insurance .

Other cases decided in Idaho similarly lend support to the position taken by the Plaintiffs in their Motion for Partial Summary Judgment. See, e.g., *Agricultural Products Corp. v. Utah Power and Light*, 98 Idaho 23, 557 P.2d 617 (1976), *City of Hayden v. Washington Water Power*, 108 Idaho 467 (Ct. App. 1985) and *Steward v. Nelson*, 54 Idaho 437 (1934). In the latter case, the legislature passed a law stating that a mortgage could not be effective as a secured interest more than ten years after the due date of the underlying debt. The Supreme Court did not uphold the statute in the face of a "contracts clause" challenge, because it operated to deprive the mortgagor of

a remedy which had been available to them when they accepted the mortgage as security for money owed to them. The Court stated simply: "Any law which in its operation amounts to a denial or obstruction of the rights accruing by a contract, though professing to act only on the remedy, is directly obnoxious to the prohibition of the Constitution." (citing *Brine v. Hartford Fire Ins. Co.*, 96 U.S. 627.) 54 Idaho 437, 443.

The Idaho Supreme Court in *Steward* then cites from the *Fidelity Bank* case and repeats "any enactment of a legislative character is said to 'impair' the obligation of a contract which attempts to take from a party a right to which he is entitled by its terms, or which deprives him of the means of enforcing such a right.. . ." *Id.*

Although *Steward* addresses itself to a remedy, it is very clear that the Idaho Supreme Court still found this to constitute an impairment of the obligation of the contracts involved, thus violative of the categorical ban on enactments "impairing the obligation of contracts" found in our state constitution.

In *Curtis v. Firth*, 123 Idaho 598, 850 P. 2d 749 (1993), the Supreme Court struck down and refused to give application to a statute which affected a trust deed entered into before the statute was enacted. *Steward v. Nelson, supra,* was cited here with approval. "The Court noted that '[i]t is well settled that the law existing when a mortgage is made enters into and becomes a part of the contract.' 54 Idaho 441, 32 P. 2d at 845. Further, a law which in its operation denies or obstructs any rights accruing under a contract is a violation of the Idaho's constitutional provision prohibiting any laws which impair the "obligation of contract." Id. at 444, 32 P. 2d at 846, *quoted at 123 Idaho 598, 610.*

Tanner v. Shearmire, is another trust deed case where *Steward v. Nelson, supra,* is cited

with approval. "However, a trust deed is governed by the law in existence at the time of its execution, and the parties' rights thereunder are not affected by subsequent legislative enactments." 115 Idaho 1060, 1063, fn. 3 (Ct App. 1989).

Curr v. Curr, 124 Idaho 686 (1993) is yet another case applying the constitutional prohibition regarding laws or rules which by seeking retroactive application operate to impair the obligations of contracts. It involved attorneys who were shorted as to their attorneys' fees by virtue of a clumsy amendment which the Industrial Commission made to its rules, and sought to apply retroactively. The Supreme Court took a dim view of this stating that the "Commission has waded into regulatory conduct with an indifference to constitutional requirements that adhere to rights fixed by a private contract. . . It is clear that, in Idaho, parties to a contract have a property interest in the subject matter of the contract that is protectable both under the contract clause and the due process clause of the United States Constitution." 124 Idaho 686, 691-2. In Footnote 3, *Steward v. Nelson, supra,* is again cited with approval, as is the Idaho Constitution, Art. 1, Sec. 16. *Id.*

The foregoing cases indicate that the application of the Idaho Constitution's certain and unconditional prohibition against laws of the type struck down in *Steward* and in the *Fidelity Bank* case has remained unchanged.

The attempted repeal of I.C. § 72-915 on a retroactive basis is clearly unconstitutional, as being in violation of Art. 1, Sec. 16 of the Constitution of Idaho. It not only impairs but absolutely destroys a vested contractual right which existed prior to the attempted legislative frustration of the Supreme Court's final opinion in *Farber*. Whether the legislature can destroy I.C. § 72-915 prospectively from May 6, 2009 forward or whether the statute has prospective application commencing May 6th, 2009 or July 1, 2009 are not issues brought before the Court. However, the

retroactive application of this statute cannot be allowed and Plaintiffs have asked for partial summary judgment on this point.

III. CONCLUSION

The provision of Section 1 of S.L. 2009, chapter 294 (which is the number assigned to the enacted law repealing Idaho Code § 72-915 *retroactively)* violates the Contract Clause of the Idaho Constitution. There can be no doubt that, under *Farber, supra,* the Plaintiffs and the members of the Class have vested rights to receive a *pro rata* share of the total dividend paid by the Fund in each year of the class period. Nor can it seriously be doubted that, absent the retroactivity provision of the legislation, the Fund would have been obligated to pay to the Plaintiffs and the members of the Class such sums as would result in their receiving their *pro rata* share of the total dividends paid. It therefore follows inexorably that the retroactive repeal of I.C. § 72-915 impairs the Fund's obligation to allocate such dividends as the Manager declares to all time-qualified policyholders *pro rata,* based solely on the size of their premium, for all policies purchased up to six months prior to the effective date of the repeal.

For all of the reasons set forth above, this Court should grant Plaintiffs' Motion For Partial Summary Judgment, and enter an order declaring that the repeal of Idaho Code § 72-915 is unconstitutional insofar as it is declared to be retroactive for the simple reason that it impairs the Fund's obligation to honor the vested rights of the Plaintiffs and the members of the Class to the receipt of a *pro rata* portion of the dividend corpus.

Respectfully submitted this 8th day of October, 2010.

GORDON LAW OFFICES, CHTD.

Philip Gordon

Donald W. Lojek

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 8th day of October, 2010, a true and correct copy of the foregoing instrument was served on the following by the method indicated below, and addressed as follows:

[ ] Hand Delivery
[ ] U.S. Mail, postage paid
[ ] Overnight Express Mail
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Attorneys for Defendants

IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT OF THE STATE OF IDAHO, IN AND FOR THE COUNTY OF CANYON

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE, LLC OF SALMON,

Plaintiffs,

vs.

THE IDAHO STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its Manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN and MAX BLACK and STEVE LANDON, in their capacity as members of the Board of Directors of the State Insurance Fund,

Defendants.

Case No. CV 09-13607-C

MEMORANDUM IN SUPPORT OF DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

COME NOW defendants, The Idaho State Insurance Fund, James M. Alcorn in his official capacity as its Manager, and William Deal, Wayne Meyer, Gerald Geddes, John Goedde, Elaine Martin, Mark Snodgrass, Rodney A. Higgins, Terry Gestrin, Max Black, and Steve

Landon in their capacity as members of the Board of Directors of the State Insurance Fund (collectively, "SIF"), by and through their counsel of record Hall, Farley, Oberrecht & Blanton, P.A., and hereby submit their Memorandum of Law in Support of Defendants' Motion for Partial Summary Judgment. For the reasons stated herein, Defendants' Motion should be granted.

SUMMARY OF ARGUMENT

The dispute in this action generally regards Plaintiffs' allegation that the SIF failed to pay them certain dividend payments for prior years in which Plaintiffs paid premiums as policyholders of workers' compensation policies issued by SIF. Specifically, Plaintiffs allege I.C. § 72-915 requires payment of dividends according to a specific mathematical formula based upon a premium surplus declared by SIF.

However, the Idaho Legislature voted to repeal I.C. § 72-915 – the statute under which Plaintiffs seek to enforce their claim for dividends – on April 29, 2009, as S.L. 2009, ch. 294, § 2. It was then signed by the Governor on May 6, 2009. Such repeal was expressly made retroactive to January 1, 2003.

Nevertheless, Plaintiffs' First Amended Class Action Complaint and Demand for Jury Trial seeks, in relevant part, a declaration: "That the repeal of I.C. § 72-915 by the 2009 legislature be deemed to be unconstitutional, void and of no effect as to all policies issued prior to July 1, 2009. *Id.* at p. 15. The request for such declaration reflects Plaintiffs' need to first bypass the repeal by the Idaho Legislature that, at present, leaves them no right of action.

There is no issue of material fact precluding summary judgment as a matter of law in favor of Defendants on this issue. The repeal of I.C. § 72-915 bars Plaintiffs' action because legislation is effective when the Legislature so defines, and the emergency repeal of I.C. § 72-915 was signed May 6, 2009, and was made retroactive to January 1, 2003, thereby barring

Plaintiffs' action. Furthermore, contrary to Plaintiffs' position, the repeal of I.C. § 72-915 is constitutional under both the U.S. and Idaho constitutions.

Plaintiffs have the burden of proving that the repeal is unconstitutional, and the test of whether the repeal violates the Contract Clause is a demanding one. According to RUI One Corp. v. City of Berkeley, 371 F.3d 1137, 1147 (9th Cir. 2004), in order to prevail on their claim that the repeal violates the Contract Clause, Plaintiffs must show that:

- the state law has, in fact, operated as a substantial impairment of a contractual relationship;
- the State does not have a significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem; and
- the adjustment of the rights and responsibilities of contracting parties is not based upon reasonable conditions and is not of a character appropriate to the public purpose justifying the legislation's adoption.

As a matter of law, plaintiffs are unable to meet their burden under this test.

First, the Idaho Legislature has not operated a substantial impairment of a contractual relationship because there is no contractual right to dividends in the SIF workers' compensation policies. In addition, even assuming a right of contract existed, the repeal cannot be considered to have substantially impaired it. The purpose behind the Legislature's creation of SIF was to ensure the well-being of the public's wage-earners through insurance for employers who may have to pay workers' compensation, and this core function of the policies held by Plaintiffs remains unchanged by application of the repeal. What is more, reading the repeal as unconstitutional would enhance, rather than impair, the rights of some policyholders.

Second, the SIF and the workers' compensation coverage it provides are creatures of statute and, when the Legislature created them, it did not prevent itself from using its police powers to shepherd the SIF, a quasi-public entity, and run it efficiently.

Third, the repeal merely conforms to the law to the way the Manager has paid dividends for years. Therefore, the only expectations the policyholders may have had for dividends to be paid otherwise would have been attributable to the *Farber* litigation and would have been uncertain and quickly quashed by the Legislature's repeal.

Fourth, the Legislature, recognizing the vitality of the SIF is necessary to the vitality of the public welfare, repealed I.C. § 72-915 so the Manager would have the authority to make the decisions necessary to the economic health and competitiveness of the entity in today's market.

Finally, the repeal is based upon reasonable conditions and is of a character appropriate to the public purpose justifying the action.

In short, Defendants are entitled to summary judgment on this issue because there is no factual question preventing the Court from determining that, as a matter of law, Plaintiffs have failed to meet their burden of showing that the repeal of I.C. § 72-915 was unconstitutional.

BACKGROUND

A. The SIF.

By way of background to understand the creation, purpose, and governance of the SIF, a brief summary of the SIF is appropriate.

1. The Purpose of the SIF is to Provide Worker's Compensation Insurance to Idaho Employers and to Ensure the Existence of a Solvent Source From Which Workers Entitled to Compensation May Collect.

In 1917, the Idaho legislature enacted a comprehensive statutory scheme, now codified as Idaho Code §§ 72-901 et seq., creating the SIF "for the purpose of insuring employers against liability for compensation under this worker's compensation law ... and of securing to the persons entitled thereto the compensation provided by said laws." Idaho Code § 72-901(1).

Since its enactment, the SIF has fulfilled its public purpose by providing worker's compensation coverage to thousands of Idaho employers who have relied on such service being available.[1]

While Idaho employers are not required to procure insurance with the SIF, if an employer is declined coverage by two private carriers and the SIF, then coverage may be obtained through the assigned risk pool.[2] In an effort to fulfill one of its principal purposes—providing worker's compensation insurance to Idaho employers—the SIF maintains an underwriting policy that seeks to insure all Idaho employers, regardless of size, so the majority of Idaho employers who could not otherwise obtain coverage through a private carrier could obtain coverage with the SIF, and therefore avoid the extra costs associated with acquiring an insurance contract through the assigned risk pool.[3]

In structuring the SIF, the Legislature determined it should be "created as an independent body corporate politic" and derive its financial well-being from "premiums and penalties received," "property and securities acquired," and "of interest earned" thereon. Idaho Code § 72-901(1). The money generated is deposited with the state treasurer, who acts as custodian for the SIF; however, "[t]he money in the fund does not belong to the state . . . [the money is held by the treasurer] . . . for the contributing employers and the beneficiaries of the compensation law, and for the payment of the costs of the operation of the fund." State ex rel. Williams v. Musgrave, 84 Idaho 77, 84, 370 P.2d 778, 782 (1962).

Moreover, the SIF is to "be administered without liability on the part of the state." Idaho Code § 72-901(1). Yet, per I.C. §72-901(4), the SIF is subject to the provisions of the Idaho insurance code, but is not allowed to be a member of the Idaho Insurance Guaranty Association

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[1] *See* Affidavit of Jim Alcorn in Support of Defendants' Motion for Summary Judgment, at ¶ 13.("Alcorn Aff.").
[2] *See* Alcorn Aff., ¶ 12. The assigned risk pool insures Idaho employers who cannot otherwise secure worker's compensation coverage, but they are generally required to pay a fifty percent (50%) higher premium than if they were insured through the SIF or a private carrier. *See* Alcorn Aff., ¶ 11.
[3] *See* Alcorn Aff., ¶ 13.

("IIGA"). The IIGA offers security for those insurers who are unable to make payments on a claim, and guarantees the payment of insurance benefits if an insurance carrier becomes insolvent.[4] Likewise, the IIGA offers security for those individuals insured by insurers unable to pay; however, by statute, this protection does not extend to the SIF.[5]

Unlike other insurance carriers which rely on the IIGA to pay benefits in the event of insolvency, the SIF must be managed such that is maintains sufficient surplus and reserve totals to provide a stable and ongoing source of worker's compensation insurance to protect Idaho workers.[6] As a result, it remains even more critical that the SIF's financial integrity remain intact, for if it is compromised, the availability of worker's compensation insurance in Idaho would be critically jeopardized; this is especially true in light of the fact that the SIF insures approximately 70% of the market, including policyholders unable to obtain coverage from other private insurers.[7]

2. The Idaho Legislature Charged the Manager with the Primary Responsibility of Conducting the Business and Administration of the SIF.

The duty to ensure the SIF maintains its financial integrity is left to the Board of Directors and the Manager. Idaho Code §§ 72-901(3), 72-902. In many ways they share a symbiotic relationship in that their collective decisions determine whether the SIF is able to fulfill its public purpose.[8] For the majority of its existence, the SIF has been directed by a Manager, charged with the duty of conducting the business and administration of the SIF.[9] To accomplish these demanding tasks, the Manager, by statute, has been granted full power and/or discretion over a number of critical business and administrative decisions involving the operation

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[4] *See* Alcorn Aff., ¶ 16.
[5] Idaho Code § 72-901(4); *see also* Alcorn Aff., ¶ 15.
[6] *See* Alcorn Aff., ¶ 18.
[7] *See* Alcorn Aff., ¶ 19.
[8] *See* Alcorn Aff., ¶ 19.
[9] *See* Alcorn Aff., ¶ 20.

of the SIF, including, but not limited to, directing the investment of surplus funds generated from premiums and interest, the power to sue and to enter into insurance contracts, setting appropriate reserve totals to meet unexpected losses, and declaring a dividend should the proper conditions be present. *See generally* Idaho Code § 72-901 *et seq.*

Despite the extent of power and discretion invested in the Manager, the Board of Directors plays an integral role through its duty to "direct the policies and operations of the state insurance fund to assure that [it] is run as an efficient insurance company, remains actuarially sound and maintains the public purposes for which [it] was created." Idaho Code § 72-901(3). Although this duty is enacted through the decisions and guidance of the Manager, the two entities work in conjunction to satisfy the SIF's purpose as mandated by statute.[10]

3. As Part of His Duties, the Manager Has Been Charged With the Discretion of Determining Whether a Dividend Will Be Paid Each Year.

The SIF surplus fund is considered an asset of the fund and dividends, if any, are paid from what the Manager determines to be surplus available for a dividend distribution after evaluating a myriad of factors, including, but not limited to, present and future SIF operating expenses, the required reserves, investment income, market forces, and industry trends.[11] The declaration of a dividend is a multi-step process that ultimately boils down to determining how much surplus is available to declare as a dividend, followed by determining how it is to be divided, taking into account such factors as the costs associated with writing the insurance contract, and any losses that may have been incurred on the insurance contract.[12]

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[10] *See* Alcorn Aff., ¶ 19.
[11] *See* Alcorn Aff., ¶ 21.
[12] *See* Alcorn Aff., ¶ 24.

4. Policyholders Are Not Entitled to the Payment of a Dividend Each Year.

Idaho employers who purchase their worker's compensation insurance from the SIF receive a contract of insurance which sets forth the parameters of their coverage.[13] The contract of insurance does not provide for the payment of a dividend to the policyholders.[14] The governing statutes for the SIF do not guaranty payments of dividends to policyholders, nor do they set forth that the policyholders have a property interest in the surplus or assets of the SIF. *See generally* Idaho Code §72-901 *et seq.* In fact, the Idaho Supreme Court previously concluded the SIF's statutory framework does not create any property rights in the SIF's policyholders. Kelso & Irwin, P.A. v. State Insurance Fund, 134 Idaho 130, 135, 997 P.2d 591, 596 (2000). An SIF policyholder has no vested right in the surplus and assets of the SIF; rather, the assets and surplus belong to the SIF in order to meet its statutory purpose provided in I.C. §72-901(1). *Id.*

B. The prior *Farber* litigation and Idaho Supreme Court's decision therein.

Prior to this litigation, a group of plaintiffs filed a lawsuit, entitled *Randolph E. Farber, et al. v. The Idaho State Insurance Fund*, in the District Court for the Third District of Idaho, Canyon County, Case No. CV06-7877 (Judge Morfitt and Judge Ryan, presiding)("*Farber*"). In the *Farber* action, the plaintiffs contended that they, as policyholders paying annual premiums of $2,500 or less, were improperly denied a pro rata share of dividends declared by the SIF for certain years at issue, relying upon the now-repealed Idaho Code §72-915. In response thereto, the SIF argued that, per the language of I.C. §72-915, the Manager exercised the authority given to him by the Legislature in determining that during such certain policy years, dividends would

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[13] *See* Alcorn Aff., ¶ 25.
[14] See Affidavit of Donald W. Lojek filed on January 6, 2007, Ex. 1 (State Insurance Fund Workers Compensation and Employers Liability Insurance Policy).

not be issued to SIF policyholders who paid premiums of $2,500 or less during the respective dividend year.

The statute at issue in the *Farber* litigation and which forms the basis for this action, I.C. § 72-915, stated:

> At the end of every year, and at such other times as the manager in his discretion may determine, a readjustment of the rate shall be made for each of the several classes of employments or industries. If at any time there is an aggregate balance remaining to the credit of any class of employment or industry which the manager deems may be safely and properly divided, he may in his discretion, credit to each individual member of such class who shall have been a subscriber to the state insurance fund for a period of six (6) months or more, prior to the time of such readjustment, such proportion of such balance as he is properly entitled to, having regard to his prior paid premiums since the last readjustment of rates.

Particularly at issue in the *Farber* litigation was the question of whether Idaho Code §72-915 mandated that, if the SIF Manager made a dividend declaration as is his discretion to do, the dividend would require distribution of the dividend on a strictly pro-rata basis to eligible policyholders who paid less than $2,500 in annual premiums.

Presented the question on motion for summary judgment, the District Court sided with the SIF. In analyzing I.C. §72-915, the District Court held that I.C. § 72-915 was ambiguous. (Counsel Aff., Exh. A.) In so holding, the District Court stated that:

> The use of the term "class of employment" in 72-915 by its phrasing "any class of employment **or** industry" is ambiguous. By the use of "or", this Court is not convinced that plaintiffs' proposed interpretation that it refers to grouping classes based solely on type of industry is the only reasonable interpretation. That phrase could reasonably be interpreted to mean that the classes could be determined by industry, by size of employer, by premium amounts paid by employer, etc. As the term is ambiguous, this Court is free to examine not only the literal words of the statute, but the reasonableness of the proposed interpretations, the policy behind the statute, and the legislative history.

(*Id.*, at pp. 11-12.) The District Court, in amending its concluding paragraph, later added the following:

> [I]t is this Court's conclusion that, as a matter of law, the language of I.C. §72-915, in context with the directives of other statutes set forth in the Act, the laws of our sister states, and the decisions of our Supreme Court, allows the fund manager, with the

> approval of the board of directors, to use his discretion to distribute dividends to policyholders in a manner that is consistent with the legislative purpose and directives set forth in Article 72, Chapter 9, Idaho Code, which establishes the State Insurance Fund. Specifically, to assure that the State Insurance Fund is run as an efficient insurance company, remains actuarially sound, and maintains the public purposes for which the Fund was created.

(Counsel Aff., Exh. B, at p. 2.)

However, on appeal, the Idaho Supreme Court issued its Opinion in the *Farber* matter, reversing the District Court's grant of summary judgment to SIF.[15] In particular, the Court found that the statute at issue on appeal, I.C. §72-915, was unambiguous and that "the distribution of dividends must be done on a pro rata basis." Farber v. Idaho State Ins. Fund, 147 Idaho 307, 311, 208 P.3d 289, 293 (2009). However, in rejecting the SIF's arguments regarding the basis of SIF's dividend methodology – to wit, its efforts to distribute dividends in a fashion to comply with the statutorily-obligated mandate that SIF "is run as an efficient insurance company, remains actuarially sound and maintains the public purposes for which the state insurance fund was created" (Idaho Code §72-901(3)) - the *Farber* Court recognized the authority of the Legislature to change the law:

> Because the statute is unambiguous, there is no need to consider the plethora of evidence and testimony provided by the Fund to support its argument that the Manager acted reasonably in choosing to distribute a dividend only to those policyholders who paid more than $2,500.00 in annual premiums. The arguments, evidence, and testimony provided to this Court would be better targeted at the Legislature, which is empowered to change existing law. . . . If, in the intervening time, it has become prudent to alter the statutory language related to the requirements for distribution of dividends, **the proper remedy is to approach the Legislature to change the law.**

Id. at 313 (emphasis added).

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[15] The Idaho Supreme Court's initial opinion was issued on March 5, 2009, which was later withdrawn and replaced by a Substitute Opinion on May 5, 2009.

C. **The repeal of I.C. §72-915.**

While the *Farber* litigation was still pending before the Idaho Supreme Court, the Idaho Legislature voted to repeal I.C. §72-915. (Counsel Aff., Exh. C.) The repeal specifically provided that: "An emergency existing therefor, which emergency is hereby declared to exist, Section 1 of this act shall be in full force and effect on and after passage and approval, and Section 2 of this act shall be in full force and effect retroactively to January 1, 2003." (*Id.* at §3.). The repeal was approved in the Legislature, and advanced to the Governor, who signed it on May 6, 2009. *Id.*

Thereafter, the Idaho Supreme Court denied Respondent's Petition for Rehearing on May 12, 2009, and issued its Remittitur to the District Court on May 27, 2009. (Counsel Aff., Exh. D.)

D. **Summary of this action.**

Later that year, on December 24, 2009, the plaintiffs in this action filed their Class Action Complaint and Demand for Jury Trial; plaintiffs later filed, on June 10, 2010, their First Amended Class Action Complaint and Demand for Jury Trial ("Amended Complaint"). Plaintiffs generally allege:

13.

> For some or all of the Dividend Periods falling within the Class Period, the Plaintiffs and the members of the Class purchased a worker's compensation insurance policy from the Fund, were billed annual premiums which were in excess of $2,500.00, retained each such policy for at least 6 months, and, for each such Dividend Period, did not receive an amount which was equal to or greater than a *pro rata* share of the dividend distributed by the Fund. In each such instance, the Plaintiffs and the members of the Class did not receive a dividend because the Manager and/or the Board arbitrarily, capriciously, and without any lawful authority, violated the terms of the contract and the law by determining that such amounts which were distributed as dividends would not be allocated among policyholders on a *pro rata* basis.

Amended Complaint, p. 8.[16] This alleged failure by SIF to pay dividends was based upon I.C. §72-915:

10.

As of June 30, 2009, Idaho Code § 72-915 provided as follows:

> At the end of every year, and at such other times as the manager in his discretion may determine, a readjustment of the rate shall be made for each of the several classes of employments or industries. If at any time there is an aggregate balance remaining to the credit of any class of employment or industry which the manager deems may be safely and properly divided, he may in his discretion, credit to each individual member of such class who shall have been a subscriber to the state insurance fund for a period of six (6) months or more, prior to the time of such readjustment, such proportion of such balance as he is properly entitled to, having regard to his prior paid premiums since the last readjustment of rates.

This term of contract between the parties requires that any dividend which the Fund elects to distribute must be distributed among all "Qualified Policyholders" (those who had entered into a contract for a policy during the period covered by any dividend being distributed and who held that policy in effect for at least six months). The term of the contract requires that total amount of the dividend be allocated into shares based upon the ratio between the amount of annual premiums billed to each Qualified Policyholder during the Dividend Period and the total annual premiums billed to all Qualified Policyholders during the same period. Neither this term of the contract nor any other term of the contract or any applicable law provides the Manager any authority whatsoever to distribute the dividend based upon any other allocation formula.

Amended Complaint, p. 6. However, plaintiffs recognized the repeal of I.C. §72-915 presented a bar to their entire action; thus, plaintiffs seek, in conjunction with declaratory, injunctive, and breach of contract relief, a ruling from the Court that the repeal of I.C. §72-915 was unconstitutional which declares:

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[16] The Amended Complaint defines "Dividend Period" as "a twelve month period ... between the July 1 which falls about 30 months prior to the distribution and the June 30 which falls about 18 months prior to the distribution." (Amended Complaint at p. 7.) In turn, the "Class Period" is defined as "some or all of the Dividend Periods beginning on July 1, 2002 and including all Dividend Periods ending on or before June 30, 2009[.]" (*Id.*) More simply, plaintiffs also state that "this action pertains to any dividends distributed after December 24, 2004[.]" (*Id.*)

> That the repeal of I.C. § 72-915 by the 2009 legislature be deemed to be unconstitutional, void and of no effect as to all policies issued prior to July 1, 2009.

Id. at p. 15. The basis for such is stated to be that

> such attempted repeal is, pursuant to Article I, Section 16 of the Idaho Constitution and Article 1, Section 10 of the United States Constitution, unconstitutional, null, void and of no effect as to contracts of insurance in existence prior to the effective date of the repeal.

Id. at p. 8.

STANDARD OF REVIEW

A. The Summary Judgment Standard.

Rule 56(c) of the Idaho Rules of Civil Procedure allows that summary judgment "shall be rendered forthwith if the pleadings, depositions and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Smith v. Meridian Joint School District No. 2, 128 Idaho 714, 718, 918 P.2d 583, 587 (1996) (quoting I.R.C.P. 56(c)); *see also* Idaho Building Contractors Association v. City of Coeur d'Alene, 126 Idaho 740, 890 P.2d 326 (1995); Avila v. Wahlquist, 126 Idaho 745, 890 P.2d 331 (1995). If the evidence reveals no disputed issues of material fact, then summary judgment should be granted. *Id.* at 718-19, 918 P.2d at 587-88 (citing Loomis v. City of Hailey, 119 Idaho 434, 437, 807 P.2d 1272 (1991)). If the moving party challenges an element of the nonmoving party's case on the basis that no genuine issue of material fact exists, the burden then shifts to the nonmoving party to come forward with sufficient evidence to create a genuine issue of fact. *Id.* at 719, 918 P.2d at 588 (citing Tingley v. Harrison, 125 Idaho 86, 89, 867 P.2d 960, 963 (1994)).

Summary judgment is properly granted in favor of the moving party when the nonmoving party fails to establish the existence of an element essential to that party's case upon which that party bears the burden of proof at trial. *Id.* (citing Thomson v. Idaho Ins. Agency, Inc., 126

Idaho 527, 530-31, 887 P.2d 1034, 1037-38 (1994), and Badell v. Beeks, 115 Idaho 101, 102, 765 P.2d 126 (1988)). The party opposing the summary judgment motion "may not rest upon the mere allegations or denials of that party's pleadings, but the party's response, by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue for trial." *Id.* (quoting I.R.C.P. 56(c)). The nonmoving party's case must be anchored in something more than speculation, and a mere scintilla of evidence is not enough to create a genuine issue of fact. Tuttle v. Sudenga Industries, Inc., 125 Idaho 145, 868 P.2d 473 (1994) (plaintiff who produces mere scintilla of evidence, or otherwise raises only slight doubt as to facts, will not withstand summary judgment); Nelson v. Steer, 118 Idaho 409, 797 P.2d 117 (1990). If the nonmoving party does not come forward as provided in the rule, then summary judgment should be entered against that party. State v. Shama Resources Ltd. Partnership, 127 Idaho 267, 270, 899 P.2d 977, 980 (1995).

B. The Standard Applicable to Declaring a Statute Unconstitutional.

Idaho law is clear that legislative acts are presumed to be constitutional: "[a] legislative act is presumed to be constitutional and all reasonable doubt as to its constitutionality must be resolved in favor of its validity." Oneida County Fair Bd. v. Smylie, 86 Idaho 341, 346, 386 P.2d 374, 376 (1963). The burden of proving that a legislative act rests squarely on the challenger:

> There is a presumption in favor of the constitutionality of the challenged statute or regulation, and the burden of establishing that the statute or regulation is unconstitutional rests upon the challengers. An appellate court is obligated to seek an interpretation of a statute that upholds it [sic] constitutionality. The judicial power to declare legislative action unconstitutional should be exercised **only in clear cases.**

Stuart v. State, 149 Idaho 35, ___, 232 P.3d 813, 818 (2010)(quoting Am. Falls Reservoir Dist. No. 2 v. Idaho Dep't of Water Res., 143 Idaho 862, 154 P.3d 443 (2007)(emphasis added).

ARGUMENT

A. The repeal of I.C. § 72-915 bars Plaintiffs' action.

1. Legislation is effective when the Legislature so defines.

Article III, §22 of the Idaho State Constitution provides that:

> When acts take effect.-No act shall take effect until sixty days from the end of the session at which the same shall have been passed, except in the case of emergency, which emergency shall be declared in the preamble or in the body of the law.

In turn, Article IV, §10 of the Idaho State Constitution provides, in relevant part, that:

> Veto power. -Every bill passed by the legislature shall, before it becomes a law, be presented to the governor. If he approves, he shall sign it, and thereupon it shall become a law[.]

The Idaho Supreme Court has further explained it is solely within the province of the Legislature to determine the effective date of legislation, including in the context of declaring an emergency:

> Legislative discretion in declaring emergencies was recognized in *Johnson v. Diefendorf*, 56 Idaho 620, 635, 57 P.2d 1068, 1083 (1936), which stated, "it is left to the discretion of the legislature to fix the time when [the act] shall go into effect." *Johnson* did not raise the issue of whether a court could review the legislature's declaration that an emergency existed. That issue was resolved in *Idaho State AFL-CIO v. Leroy*, 110 Idaho 691, 718 P.2d 1129 (1986). The Court stated: "we hold that the legislature's determination of an emergency in an act is a policy decision *exclusively* within the ambit of legislative authority and the judiciary cannot second-guess that decision." *Id.* at 698, 718 P.2d at 1136 (emphasis added). The Petitioners argue that this statement is inapplicable if the repeal infringes a constitutional right but they do not identify a constitutional right that is infringed by the declaration of an emergency in this case.
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> In *Leroy,* this Court concluded that *Johnson* must be read in conjunction with *Diefendorf v. Gallet*, 51 Idaho 619, 10 P.2d 307 (1932). In *Gallet* this Court held that the judiciary could not review the governor's determination that an emergency existed to justify calling an extraordinary session of the legislature, and that the Court could not review the legislature's determination that an emergency existed to justify dispensing with the constitutional requirement that before an act could be passed, it must be printed and read on three separate days in each house. 51 Idaho at 638-39, 10 P.2d at 314-15. The Court stated, "[t]he determination as to whether facts exist such as to constitute 'an extraordinary occasion' is for him [the governor] alone to determine." *Id.*

> The justification for legislative discretion in this area is that the decision to declare an emergency is "a decision-making function that is uniquely legislative. The courts are ill equipped to make such policy decisions." *Leroy*, 110 Idaho at 695, 718 P.2d at 1133. "The respect due to the co-equal and independent legislative branch of state government and the need for finality and certainty about the status of a duly enacted statute contribute to the reluctance of the courts to inquire into whether the legislature's determination of an effective date is justified." *Id.* Justice Shepherd, concurring in *Assoc. Taxpayers of Idaho, Inc. v. Cenarrusa*, 111 Idaho 502, 725 P.2d 526 (1986), stated that "[i]n my view it is exceedingly dangerous for this Court, or any court, to interfere with the legislative *process.* Within the duties of this Court is the determination of the constitutionality of actions of other branches of government but only when the time and circumstances are appropriate." *Assoc. Taxpayers*, 111 Idaho at 503, 725 P.2d at 527 (emphasis in original). In this case the Petitioners are asking the Court to interfere with the legislative process, and this Court has held repeatedly that it is not proper to do so.

Gibbons v. Cenarrusa, 140 Idaho 316, 320-21, 92 P.3d 1063, 1067-68 (2002).

Finally, I.C. § 73-101 provides that "No part of these compiled laws is retroactive, unless expressly so declared." The Idaho Supreme Court has confirmed that "a statute will be applied retroactively where there is a clear legislative intent to that effect." Union Warehouse and Supply Co., Inc. v. Illinois R.B. Jones, Inc., 128 Idaho 660, 669, 917 P.2d 1300, 1309 (1996) (citing Gailey v. Jerome County, 113 Idaho 430, 745 P.2d 1051 (1987)).

2. The repeal of I.C. §72-915 was effective May 6, 2009, and the Legislature made it retroactive to January 1, 2003, thereby barring Plaintiffs' action.

In repealing I.C. §72-915, the Idaho Legislature was clear on the effective date, the emergency nature of the act, and the intent to make the legislation retroactive.

Section 3 of the repeal provides:

> An emergency existing therefore, which emergency is hereby declared to exist, Section 1 of this act shall be in full force and effect on and after passage and approval, and Section 2 of this act shall be in full force and effect retroactively to January 1, 2003.

After approval in the state Legislature, the repeal was forwarded to the Governor, who signed the repeal on May 6, 2009. (Counsel Aff., Exh. C.) Accordingly, the act – declared an emergency

by the Legislature, which emergency was affirmed by the governor when he signed the bill – went into effect upon signature by the Governor, retroactive to January 1, 2003.

At plaintiffs' counsel's urging, the Legislature provided a limited carve-out to the retroactive effect of the repeal, that being for extant litigation (and, in particular, the *Farber* action), which is inapplicable to this litigation:

> (6) it is the intent of the Legislature that the provisions of this act shall not apply to any action filed in a state or federal court of law in the state of Idaho on or before December 31, 2008, and the provisions of this act shall not apply to the aforementioned case of *Farber v. Idaho State Insurance Fund* as currently pending with respect to those policy holders paying annual premiums of not more than two thousand five hundred dollars ($2,500).

(Counsel Aff., Exh. C.)

In the present case, the repeal of I.C. § 72-915 forecloses Plaintiffs' claims. Plaintiffs' action was filed on December 24, 2009, long after the effective date of the repeal, and long after the permitted repeal carve-out for existing litigation of December 31, 2008. Further, as this litigation is not the *Farber* litigation involving those policyholders paying not more than $2,500 in annual premiums, Plaintiffs do not fall within the other carve-out of the repeal. Thus, even accepting *arguendo* the allegation of Plaintiffs' Amended Complaint that "this action pertains to any dividends distributed after December 24, 2004" (Amended Complaint, ¶12),[17] the earliest date that Plaintiffs could claim a right to a particular dividend methodology, then, would be December 24, 2004, long after the effective date of the repeal (January 1, 2003).

As such, Plaintiffs' action is foreclosed by the repeal of I,C. § 72-915, and SIF should be granted summary judgment.

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[17] Plaintiffs' claim for a 5-year statute of limitation is based upon their contention that the dividend methodology is a contractual right. To the contrary, dividends are governed by statute, and thus are subject to a 3-year statute of limitation. This question has been definitively resolved by the Hayden Lake decision and the District Court's ruling in the *Farber* litigation, and will be the subject of a motion to dismiss by SIF. However, for purposes of this motion, a 5-year statute of limitation is utilized for argument, to illustrate that even under Plaintiffs' demanded statute of limitation, Plaintiffs' action is still foreclosed by the repeal of Idaho Code §72-915.

B. The repeal of I.C. § 72-915 is constitutional under both the U.S. and Idaho constitutions.

1. Plaintiffs' arguments and the applicable tests under the Contract Clause.

Recognizing that the repeal of I.C. § 72-915 is fatal to their claims, Plaintiffs attempt, instead, to have the repeal declared unconstitutional. Plaintiffs' Amended Complaint seeks, in relevant part, a declaration:

> That the repeal of I.C. § 72-915 by the 2009 legislature be deemed to be unconstitutional, void and of no effect as to all policies issued prior to July 1, 2009.

Id. at p. 15. The basis for such is stated to be that

> such attempted repeal is, pursuant to Article I, Section 16 of the Idaho Constitution and Article 1, Section 10 of the United States Constitution, unconstitutional, null, void and of no effect as to contracts of insurance in existence prior to the effective date of the repeal.

Id. at p. 8.

The United States Constitution, Article 1, Section 10 and the Idaho Constitution, Article 1, Section 16, both provide that there shall be no "law impairing the obligations of contracts" (the "Contract Clause"). The Contract Clause only applies to contractual obligations in existence at the time the law is enacted. Lindstrom v. Dist. Bd. of Health Panhandle, 109 Idaho 956, 961, 712 P.2d 657, 662 (1985).

Whether there is a violation of the Contract Clause requires a three-step analysis: (1) "whether the state law has, in fact, operated as a substantial impairment of a contractual relationship[;]" (2) "whether the State . . . [has] a significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem[;]" and (3) "whether the adjustment of the rights and responsibilities of contracting parties is based upon reasonable conditions and is of a character appropriate to the public

purpose justifying the legislation's adoption." RUI One Corp. v. City of Berkeley, 371 F.3d 1137, 1147 (9th Cir. 2004) (internal quotations omitted).

In Los Quatros, Inc. v. State Farm Life Ins. Co., 800 P.2d 184 (1990), the Supreme Court of New Mexico outlined the modern parameters of the test for whether the legislation violates the Contract Clause once it has been established there is indeed a contractual relationship. A mortgagor sued for declaratory judgment that a law allowing for early payment applied to its mortgage, despite the contract's language to the contrary. The mortgagee relied on Von Hoffman v. City of Quincy, 71 U.S. (4 Wall.) 535, 18 L.Ed. 403 (1866), for the proposition that states cannot constitutionally reduce a party's existing rights under a contract; however, the *Quatros* court pointed out that "much water has flowed over the dam since *Von Hoffman,* and so we prefer to apply more modern Contract Clause analysis in deciding whether or not to invalidate this statute in this case." Quatros, 800 P.2d at 192. The mortgagor relied upon Home Building & Loan Association v. Blaisdell, 290 U.S. 398, 54 S.Ct. 231, 78 L.Ed. 413 (1934), in which the Court held that "[The Contract Clause] prohibition is not an absolute one and is not to be read with literal exactness like a mathematical formula . . . . The economic interests of the state may justify the exercise of its continuing and dominant protective power notwithstanding interference with contracts." 290 U.S. at 428, 437, 54 S.Ct. at 236, 239. The *Quatros* court went on to explain that different Contract Clause cases had different factors present, for example in *Blaisdell* there was an emergency and the legislative relief was tailored to that emergency. 800 P.2d at 192. The Court pointed out that in National R.R. Passenger Corp., 470 U.S. 451, 472, (1985) (see discussion below) "the impairing statute was a federal one, and so judicial scrutiny of the legislation was minimal, which doubtless reflects a federal court's concern with principles of federalism lacking here." 800 P.2d at 192. The *Quatros* court found these cases to be nevertheless applicable to the case at bar:

> Perhaps the case providing the best overview of the appropriate methodology is *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, [459 U.S. 400 (1983)]. There the Court reviewed a Kansas statute regulating the price of natural gas sold intrastate between a producer and a public utility, and held that it was not invalid under the Contract Clause. The Court noted, first, that "[t]he threshold inquiry is 'whether the state law has, in fact, operated as a substantial impairment of a contractual relationship.'" It went on to say that "[t]he severity of the impairment is said to increase the level of scrutiny to which the legislation will be subjected," or "the height of the hurdle the state legislation must clear." In determining the extent of the impairment, it is relevant that the industry which the complaining party has entered has or has not been regulated in the past.
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> If the answer to the threshold inquiry is that the state regulation does indeed constitute a substantial impairment, the state "must have a significant and legitimate public purpose behind the regulation," so that there is some guarantee that the state "is exercising its police power, rather than providing a benefit to special interests." Finally, once a legitimate public purpose has been identified, the reviewing court must determine "whether the adjustment of 'the rights and responsibilities of contracting parties [is based] upon reasonable conditions and [is] of a character appropriate to the public purpose justifying [the legislation's] adoption.'"

Quatros, 800 P.2d at 192 (citations omitted). The *Quatros* court allowed the legislation to stand, because it did not effect the underlying debt and because the banking industry is highly regulated, thus the impairment was slight. Even though the impairment was slight, the court still found it necessary to evaluate the public purpose, though it need not be too pressing; the court concluded that promoting the alienability of land was a public purpose, and that the legislation was appropriately tailored to that end. *Id.*

Moreover, although plaintiffs have pled violations of both the state and federal constitutions, the examination conducted by this Court will be the same. The Idaho Supreme Court has held that "we seriously consider federal law in determining the parameters of our own constitutional provisions, and we may adopt federal precedent under the state constitution but only to the extent that we believe the federal law is not inconsistent with the protections afforded by our state constitution." State v. Guzman, 122 Idaho 981, 988, 842 P.2d 660, 667 (1992). The Idaho Supreme Court has clearly not been persuaded that federal law is inconsistent with the

protections under the contract clause in the Idaho Constitution. To the contrary, the Idaho Supreme Court recently addressed a federal and state constitutional argument with a single, dispositive analysis. *See* State v. Korn, 148 Idaho 413, 224 P.3d 480, 482 (2009). In Korn, the defendant argued that a city violated his rights under "the contract clauses found in the Idaho and U.S. constitutions." The Korn Court, without making a distinction between the two constitutions, engaged in a single analysis, relying on federal law (Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 241 (1978)) to hold that the city's ordinance did not violate his rights under either constitution. *Id.* at 483. *Cf.* State v. Newman, 108 Idaho 5, 16 n.6, 696 P.2d 856, 867 n.6 (1985) (holding that while defendants sued under federal constitution and "did not also argue that the due process clause of art. 1, § 13 of Idaho's Constitution invalidates the Act in question, had they done so, we do not think that the result would have been different, for we are convinced that the rules we set down for facial challenges to the constitutionality of a statute, although derived from federal sources, are also sound and proper under Idaho's Constitution.")

Plaintiffs have a tough row to hoe in making the argument that the repeal of I.C. § 72-915 is unconstitutional, in that Idaho law is clear that legislative acts are presumed to be constitutional: "[a] legislative act is presumed to be constitutional and all reasonable doubt as to its constitutionality must be resolved in favor of its validity." Oneida County Fair Bd. v. Smylie, 86 Idaho 341, 346, 386 P.2d 374, 376 (1963). As discussed herein, Plaintiffs' argument that the repeal of I.C. § 72-915 is unconstitutional fails, as the repeal of I.C.§72-915 is constitutionally valid under both the U.S. and Idaho constitutions.

2. The Idaho Legislature has not operated a substantial impairment of a contractual relationship.

In analyzing a claim that the Contract Clause has been violated, "[t]he threshold inquiry is 'whether the state has, in fact, operated a substantial impairment of a contractual relationship." RUI One Corp. v. City of Berkeley, 371 F.3d at 1147; *accord,* Quatros, 800 P.2d at 192 ("[t]he

threshold inquiry is 'whether the state law has, in fact, operated as a **substantial** impairment of a contractual relationship.'")(emphasis added)(quoting Energy Reserves Group, Inc. v. Kansas Power & Light Co., 459 U.S. 400 (1983)). "The threshold inquiry . . . itself has three components: 'whether there is a contractual relationship, whether a change in law impairs that contractual relationship, and whether the impairment is substantial." *Id.*

As discussed herein, Plaintiffs cannot even prevail on this threshold question.

a. ***There is no contractual right to dividends in the SIF workers' compensation policies.***

"The first sub-inquiry is not whether any contractual relationship whatsoever exists between the parties, but whether there was a 'contractual agreement regarding the specific . . . terms allegedly at issue." RUI One Corp. v. City of Berkeley, 371 F.3d at 1147. In the present case, there is no contractual right to a dividend under a SIF workers' compensation policy.

In National R.R. Passenger Corp. v. Atchison Topeka and Santa Fe Ry. Co., 470 U.S. 451, 105 S.Ct. 1441 (1985), the U.S. intervened on the side of Amtrak. Congress passed statutes relieving railroads of providing rail service to inter-city passengers; then later amended the statutes to require railroads to pay Amtrak for transporting its employees. In turn, the railroads sued, alleging that the amendment was unconstitutional under the Contract clause. The National R.R. Court explained that a presumption exists that it is the primary function of the legislature is to make laws that establish the policy of the state and not to make contracts:

> For many decades, this Court has maintained that absent some clear indication that the legislature intends to bind itself contractually, the presumption is that "a law is not intended to create private contractual or vested rights but merely declares a policy to be pursued until the legislature shall ordain otherwise." This well-established presumption is grounded in the elementary proposition that the principal function of a legislature is not to make contracts, but to make laws that establish the policy of the state. Policies, unlike contracts, are inherently subject to revision and repeal, and to construe laws as contracts when the obligation is not clearly and unequivocally expressed would be to limit drastically the essential powers of a legislative body. Indeed, "'[t]he continued existence of a government would be of no great value, if by implications and presumptions, it was disarmed

> of the powers necessary to accomplish the ends of its creation.'" Thus, the party asserting the creation of a contract must overcome this well-founded presumption and we proceed cautiously both in identifying a contract within the language of a regulatory statute and in defining the contours of any contractual obligation.

National R.R., 470 U.S. at 465-67. The Court went on to provide that it is critical to ascertain what gave rise to the contractual obligation being claimed in determining whether retroactive application of a statute violates the constitution:

> In determining whether a particular statute gives rise to a contractual obligation, "it is of first importance to examine the language of the statute." "If it provides for the execution of a written contract *on behalf of the state* the case for an obligation binding upon the state is clear." But absent "an adequate expression of an actual intent" of the State to bind itself, this Court simply will not lightly construe that which is undoubtedly a scheme of public regulation to be, in addition, a private contract to which the State is a party.

Id.

In this case, SIF is an "independent body corporate politic," and, thus, a quasi-public entity that is created by, and exists by, statutory grant of authority. *See generally*, Idaho Code §72-901 *et seq.* *See, e.g.,* Kelso, 134 Idaho at 136 (holding that SIF is not a private insurance company). Idaho employers who purchase their worker's compensation insurance from the SIF receive a contract of insurance which sets forth the parameters of their coverage. (*See* Affidavit of Donald W. Lojek in Support of Plaintiffs' Motion for Partial Summary Judgment, filed September 22, 2010, at Exh. A.) While plaintiffs will likely argue that "SIF's statutory provisions are necessarily part of [the insured's] contract with SIF," Kelso, 134 Idaho at 140, the contract of insurance does not provide for the payment of a dividend to the policyholders – in fact, nowhere does it even address dividends. Further, the governing statutes for the SIF do not guarantee payments of dividends to policyholders, nor do they set forth that the policyholders have a property interest in the surplus or assets of the SIF. *See generally* Idaho Code §72-901 *et seq.* In fact, this Court previously concluded the SIF's statutory framework does not create any property rights in the SIF's policyholders. Kelso, 134 Idaho at 135. An SIF policyholder has no

vested right in the surplus and assets of the SIF; rather, the assets and surplus belong to the SIF in order to meet its statutory purpose as provided in I.C. § 72-901(1). *Id.*

Moreover, plaintiffs cannot paint a right to a strict pro rata dividend distribution as some variety of expected or vested contractual right that has been disrupted by retroactive application because SIF dividends have not previously been paid that way, and, indeed, any change in the law created by *Farber* was promptly remedied by the Idaho legislature even before remittitur issued. *See* Southwestern Bell Tel. Co. v. Public Utility Commission of Texas, 615 S.W.2d 947, 956-57 (Texas Civ. App. 1981) ("In determining whether a retroactive statute impairs or destroys vested rights, the most important inquiries are (1) whether the public interest is advanced or retarded, (2) whether the retroactive provision gives effect to or defeats the bona fide intentions or reasonable expectations of affected persons, and (3) whether the statute surprises persons who have long relied on a contrary state of the law.").[18] Courts will look to whether a reasonable expectation in a particular 'right' has developed based upon past expectation; where no such expectation existed based upon contrary past practices, courts have been loath to find a reasonable expectation that is then disrupted by a change in the law.

In Boykin v. Boeing Co., 128 F.3d 1279 (9th Cir. 1997), the 9th Circuit addressed the question of disturbing of vested rights in the context of an overtime dispute. In Boykin, the Washington State Court of Appeals had held that payment of overtime on an hourly basis defeated a claim that an employee was exempt, in a decision named Tift. 128 F.3d at 1282. In response to Tift, the Washington Legislature passed retroactive, emergency legislation to state that "[t]he payment of compensation or provision of compensatory time off in addition to a

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[18] Note, too, that Idaho generally precludes insureds from claiming a "reasonable expectation" of some term not expressly provided for in their policy of insurance. *See generally* Ryals v. State Farm Mut. Auto. Ins. Co., 134 Idaho 302, 304, 1 P. 3d 803, 805 (2000).

salary shall not be a factor in determining whether a person is exempted[.]" *Id.* Employees involved in litigation regarding exempt status argued, in turn, that the legislature's retroactive legislation disturbed their vested rights as emanating from Tift. *Id.* The 9th Circuit rejected this argument finding that the retroactive application of the Senate Bill did not defeat any reasonable expectation of the plaintiffs in the lawsuit:

> The employees next argue that the retroactive application of Senate Bill 6029 impairs their vested rights under the Washington Constitution. A vested right is "an immediate, fixed right of present or future enjoyment." *Gillis v. King County*, 42 Wash.2d 373, 377, 255 P.2d 546 (1953) (quotation omitted). In order for a vested right to be entitled to protection from legislation, it "must be something more than a mere expectation based upon an anticipated continuance of the existing law." *Washington v. Hennings*, 129 Wash.2d 512, 528, 919 P.2d 580 (1996) (quotation and citation omitted). The proper inquiry in determining the constitutionality of retroactive legislation is "whether a party has changed position in reliance upon the previous law or whether the retroactive law defeats the reasonable expectations of the parties." *Id.* at 528-29, 919 P.2d 580.
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> The employees have not changed position in reliance upon *Tift*: As Boeing notes, at issue in this case are primarily the 1992-1994 compensation practices at Boeing; *Tift* was not announced until 1995. Further, retroactive application of Senate Bill 6029 does not defeat any reasonable expectations of the employees. The employees governed by the SPEEA collective bargaining agreement cannot claim any expectations from the terms of their contract, as it provides for overtime compensation at a rate less than time and one-half. Moreover, none of the employees had expectations, under the MWA, to overtime pay at a rate of time and one-half prior to *Tift*.

Id. at 1283.

In a Washington appellate case entitled In Re Marriage of Giroux, the court examined whether or not a "vested right" had been disturbed following a change in military pension law. *See* 704 P.2d 160 (Wash. App. 1985). Military retirement pensions were traditionally considered community property. However, the U.S. Supreme Court ruled, in McCarty v. McCarty, 453 U.S. 210 (1981), that federal law prohibited states from dividing military pensions as community property. The Girouxes' divorce was decided under McCarty, and Rose Giroux was denied any part of her husband's pension. In response, however, Congress passed the Services Former

Spouses' Protection Act, 10 U.S.C. § 1408, restoring courts' right to divide pensions as community property. Rose Giroux sued for relief from her divorce judgment. James Giroux argued that upsetting the divorce settlement by retroactive application of the Congress' change in the law would disturb his vested rights, an argument rejected by the Washington Court of Appeals because Mr. Giroux had no reasonable expectation that his military pension would not be treated as community property:

> James Giroux argues that even if Congress intended the Act to be retroactive, retroactive application deprives him, without due process of law, of his vested right to the pension payments. He claims that his right to the pension vested when the amended decree became final. However, to determine the constitutionality of retroactive legislation, the proper inquiry is not whether vested rights have been interfered with, but whether "settled expectations honestly arrived at with respect to substantial interests" will be defeated. 2 C. Sands, *Statutes and Statutory Construction* § 41.05, at 261 (4th ed. 1973).
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> An argument similar to James Giroux's was made to this court in *In re Santore*, 28 Wash.App. 319, 623 P.2d 702 (1981). After the unintentional repeal of a statute permitting adoption by written consent of natural parents, the Legislature passed former RCW 26.32.916 with provisions for retroactivity. The Santores then sought to regain custody after having consented to the adoption of their child. They argued that the statute retroactively interfere[d] with their "vested rights," in violation of the due process and contract clauses of the federal and state constitutions, by making effective Mrs. Santore's consent to adoption, which was ineffective under the law existing when the consent was executed . . . . *In re Santore*, *supra* at 324, 623 P.2d 702. The court held:
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> > The proper test of the constitutionality of retroactive legislation is whether a party has changed position in reliance upon the previous law or whether the retroactive law defeats the reasonable expectations of the parties, not whether the law abrogates a "vested right," which is merely a conclusory label. Curative laws, such as RCW 26.32.916, which implement the original intentions of affected parties are constitutional because there is no injustice in retroactively depriving a person of a right that was created contrary to his expectations at the time he entered into the transaction from which the right arose.
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> (Citations omitted.) *In re Santore*, *supra* at 324, 623 P.2d 702.
>
> Applying the test adopted in *Santore* to the case at bar, it is difficult to see how retroactive application of the Act would defeat the reasonable expectations of the parties. Throughout their marriage, and until the *McCarty* decision, the Girouxs could reasonably have expected that James Giroux's military pension would be

> treated as community property by the courts of this state. Only after the *McCarty* decision could the husband have reasonably expected to receive as his separate property what was formerly almost all of the couple's community property. Retroactive application of the Act cannot be said to be unfair or unreasonable. Recognizing the important contribution of the military spouse to our national defense, "that frequent change-of-station moves and the special pressures placed on the military spouse as a homemaker make it extremely difficult to pursue a career affording economic security, job skills and pension protection", Congress intended that the "status of the military spouse be acknowledged, supported and protected." 1982 U.S.Code Cong. and Ad.News, at 1601.

Id. at 162-63.

In the present case, SIF policyholders have also not changed any position in reliance upon an expectation of the payment of a pro rata dividend in every instance the SIF Manager declares a dividend. To the contrary, the dividend methodology employed by SIF has been employed for many years. (Alcorn Aff., ¶25.) Prior to the Farber decision, the SIF policyholders did not receive a strict pro rata share of the declared dividends. (Alcorn Aff., ¶25.) The Farber decision announced an interpretation of I.C. § 72-915 that the Legislature itself did not intend for the statute, as borne out by S.B. 1166a's Statement of Purpose. Indeed, even before the Idaho Supreme Court's Order Denying Petition for Rehearing (May 12, 2009) and subsequent Remittitur (May 27, 2009), the repeal of Idaho Code §72-915 was put into effect. (Counsel, Exhs. C & F.) Thus, even after the Farber decision, no expectation in pro rata distribution of declared dividends could reasonably have been contemplated by SIF policyholders, given that I.C. § 72-915 was repealed even before the Idaho Supreme Court had finished with the Farber appeal. Thus, here, an SIF policyholder could have only reasonably expected to receive dividends in pro rata fashion after the Farber decision – and even then, the law was immediately changed by the Idaho legislature before the remittitur was ever issued.

Accordingly, there is no contractual right to dividends, and a legislative change to the statute governing the methodology for distribution of dividends does not implicate a term of the SIF insurance policy.

b. The repeal of I.C. § 72-915 was not a change in law that impaired the contractual relationship between SIF and its policyholders.

A statutory right to a particular dividend methodology, even if found to be "necessarily part of [the insured's] contract with SIF," is expressly limited by the terms of the contract itself. The policy expressly provides:

> Terms of this insurance that conflict with the workers compensation law are changed by this statement to conform to this law.

(Alcorn Aff., Exh. A, at p. 2.) Thus, an SIF policyholder is on notice from the commencement of coverage that the terms of the policy are governed by statutes, and are subject to amendment at any time by a change in the law. Thus, even to the extent a dividend methodology may be a term of the contract by virtue of statute, that term expressly emanates from statute, and is subject to change at any time by the Legislature, which is expressly outlined in the policy. A repeal of I.C. § 72 -915 (or, more specifically, the lack of a statute mandating a particular dividend methodology), then, would be automatically incorporated into the policy, and no "impairment" would exist. Moreover, as discussed above, there is no expectation being impaired, as SIF policyholders had no expectation of a pro rata dividend under I.C. § 72 -915 given it was retroactively repealed before the *Farber* case was remitted to the district court.

Thus, no impairment to any contractual right is implicated by the change in the law – rather, only at best a statutory policy term wholly subject to Legislative change.

c. The SIF policies were not "substantially impaired."

Even assuming, *arguendo*, that the right to a particular dividend methodology is a statutory provision that becomes a term of a workers' compensation contract, and that the repeal effectuated some kind of impairment, a repeal of the statute governing such methodology would not constitute a "substantial" impairment to the SIF policy, a necessary showing under a Contract Clause analysis.

"The Contracts Clause provides protection against 'substantial' impairments of the obligation of contract only. A finding of minimal alteration of contractual obligations may end the court's inquiry." 16B Am. Jur. 2d Constitutional Law § 776 (2010). Similarly,

> [I]n determining the extent of the impairment, a reviewing court may also consider "whether the industry the complaining party has entered has been regulated in the past." *Id.* For, "where a complaining party enters a contractual relationship in a heavily regulated industry, expectations of further regulation of that industry may lessen the severity of a subsequent impairment of that party's contractual rights and obligations." *Segura [v. Frank], . . .* 630 So.2d [714,] 730.

State v. All Property and Cas. Ins. Carriers Authorized and Licensed To Do Business In State, 937 So.2d 313 (La. 2006); *see also* U.S. for Use and Benefit of Midwest Steel & Iron Words Co. v. Henly, 117 F. Supp. 928, 930-31 (D. Idaho 1954) (stating that "[a]s has been stated in numerous decisions, all contracts are entered into with the understanding that the reserve power of the state to pass laws for the general welfare may be invoked at any time and therefore if the legislature in the proper exercise of that power is convinced that the public good demands that an insurance company unsuccessfully resisting payment should pay attorneys' fees, there is no constitutional objection to their doing so."); *accord* Allstate Ins. Co. v. Kim, 829 A.2d 611, 625 (Md. 2003) (holding that retroactive abolition of child-parent immunity in tort action involving motor vehicle such that insurer was required to pay on mother's behalf did not impair insurance contract, since both insurance industry and field of tort law are heavily regulated, change was "in the wind" for some period of time, and there was no evidence of significant economic impact on Allstate or any other insurer); Hawkeye Commodity Promotions, Inc. v. Miller, 432 F.Supp.2d 822, 846-49 (Iowa 2006) (holding that statute making it illegal for retailers to offer certain gaming machines did not violate constitution because although the impairment was substantial, i.e., a total wipeout, the state had the right to terminate the contract at any time and the impairment was thus foreseeable).

In regard to workers' compensation policies issued by SIF, the overriding purpose of such policies is not to potentially allow a fractional return on paid premiums, depending on whether the SIF Manager, in his statutorily-authorized discretion, declares a dividend. Instead, the core, fundamental function and purpose of worker's compensation coverage is to provide unlimited coverage for worker injuries (and, under Part 2, additional coverage for employer liability in an amount as desired by the policyholder) to its policyholder regardless of the premium size. Thus, the SIF policy provides a $300 policyholder, and any policyholder under or above that amount with the same amount of upper coverage as a $500,000 policyholder. The repeal of I.C. § 72-915 does nothing to alter, in any way, the purpose of the workers' compensation policy; it merely grants the SIF Manager the discretion to pay declared discretionary dividends in a fashion that complies with the statutory directive that SIF be an "efficient insurance company, remain[. . .] actuarially sound and maintain[. . .] the public purposes for which the state insurance fund was created." I.C. § 72-901(3). Altering the way the SIF Manager pays out dividends to particular policyholders, then, does not constitute a "substantial" impairment to the parties' contract of insurance.[19]

Moreover, Plaintiffs cannot demonstrate that the repeal effectuated a "substantial impairment" on the insurance polices between SIF and the policyholders based upon the limitations of their own Amended Complaint. Plaintiffs do not, and cannot, contend that their claims in this action are applicable to all policyholders paying in excess of $2,500 in premiums for the years at issue. In years where SIF elected to not distribute dividends to those policyholders below a certain paid premium level ($2,500, as was the subject of the *Farber*

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[19] Indeed, even the amount declared as dividends, as a percentage of premiums, is not "substantial." For the 6 years in which dividends were declared between December 2003 and December 2008, the average dividend was only 5.8582% of paid premiums, ranging from 3.9191% to 9.0304%. Counsel Aff., at Exhs. D & E. Thus, a pro-rata share under Idaho Code §72-915 for the dividend declared in December 2003 for a policyholder paying $10,000.00 in annual premiums would have been $391.91.

action), the dividends declared were, instead, redirected to policyholders of more than $2,500 in premiums – thus, certain of those larger policyholders received dividends that were larger than what their pro rata share would have been under Idaho Code §72-915. In fact, Plaintiffs' own complaint even seeks to exclude those same certain policyholders from this action:

> For some or all of the Dividend Periods falling within the Class Period, the Plaintiffs and the members of the Class purchased a worker's compensation insurance policy from the Fund, were billed annual premiums which were in excess of $2,500.00, retained each such policy for at least 6 months, and for each such Dividend Period, did not receive an amount which was equal to or greater than a *pro rata* share of the dividend distributed by the Fund.
>
> . . . .
>
> The Class shall include, for each of the Dividend Periods during the Class Period as to which a dividend was or may be distributed, all Idaho employers who: . . . (d) did not or may not, with respect to the Dividend Period in which the policy was acquired, receive a dividend which was at least equal to a *pro rata* share of the total amount of dividend being distributed[.]

Amended Complaint at ¶¶13 & 15.

Plaintiffs' efforts to nullify the repeal of I.C. § 72-915, then, is not predicated on the claim that all policyholders' rights were "impaired" by the repeal, but only that certain policyholders were. In fact, a nullification of the repeal - whether its retroactive application, its prospective application, or both – would actually adversely impact dividend payments to certain policyholders, by either potentially creating a right in SIF for recoupment of dividend overpayments, or by restricting their ability to secure a larger dividend as the SIF Manager may, in his discretion, determine is appropriate for those policyholders based upon premium level and other factors, including individual policyholders' losses.

As such, given that the repeal of I.C. § 72-915 does not impact the purpose of the SIF's workers' compensation policies in the slightest, and given that plaintiffs cannot even contend that all policyholders are impacted by the change in the law (which some policyholders will, in

fact, benefit from), Plaintiffs cannot demonstrate that the repeal "substantially impaired" their contracts of insurance with SIF.

3. The State has a significant and legitimate public purpose behind the repeal of I.C. § 72-915.

Even if the threshold showing – a substantial impairment of contractual relationship – is met, the Court must then inquire "whether 'the State, in justification, [has] a significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem,' to guarantee that 'the State is exercising its police power, rather than providing a benefit to special interests.'" RUI, 371 F.3d at 1147. Thus, Plaintiffs must demonstrate that there lacked a legitimate public purpose behind the repeal of I.C. § 72-915.

Of course, the legitimate public purpose behind the repeal of I.C. § 72-915 is borne out by the Legislature's Statement of Purpose and Fiscal Note to S.B. 1166, as amended. (Counsel Aff., Exh. C.) There, the Legislature stated:

> Repeal of Idaho Code Section 72-915 will serve to offset an adverse decision of the Idaho Supreme Court regarding the interpretation of Idaho Code Section 72-915 which could subject the State Insurance Fund to pay dividends on policies that are not financially profitable, thereby restricting the Fund's ability to reduce premiums and pay dividends to profitable policyholders. The proposed repeal of Idaho Code 72-915 will clarify the law regarding the payment of dividends by the State Insurance Fund by making it clear that in passing House Bill 774aa in 1998, it was the intent of the legislature to have the State Insurance Fund operate like an efficient insurance company subject to regulation under Title 41, Idaho Code, including the dividend provision set forth in Title 41, Chapter 28, Idaho Code. Repeal of the law effective April 3, 1998 is necessary because on that date laws were enacted which subjected the State Insurance Fund to regulation under the Insurance Code, Title 41 of the Idaho Code. This legislation will allow the State Insurance Fund to issue dividends in the same manner as other insurance companies operating within the State of Idaho.

Id.[20] In turn, the repeal's Fiscal Note emphasized the financial uncertainly faced by SIF in light of the Court's ruling:

> The State of Idaho and public entities, which are insured by the State Insurance Fund, face losing all or part of their future dividends and deviations as a result of uncertainties as to the effect of a recent Supreme Court decision. Based on dividends and rate reduction deviations provided by the State Insurance Fund over the past two years, that number could exceed $5,000,000 annually. Private businesses may also, due to the same uncertainties, experience the loss of future dividends and deviations since, according to the Court's decision, the Fund has no option when distributing dividends, other than to use a pro rata formula.

Id.

The public purpose of the SIF is well-established. The SIF is a "creature of statute, . . . limited to the power and authority granted to it by the legislature." Kelso, 134 Idaho at 135. In particular, the SIF was created "for the purpose of insuring employers against liability for compensation under this worker's compensation law . . . and of securing to the persons entitled thereto the compensation provided by said laws." I.C. § 72-901(1). In structuring the SIF, the Legislature determined it should be "created as an independent body corporate politic" and derive its financial well-being from "premiums and penalties received," "property and securities acquired," and "of interest earned" thereon. I.C. § 72-901(1). The Board of the SIF[21] is instructed to "direct the policies and operations of the state insurance fund to assure that [it] is run as an efficient insurance company, remains actuarially sound and **maintains the public purposes for which [it] was created.**" I.C. § 72-901(3) (emphasis added). The money generated is deposited with the state treasurer, who acts as custodian for the SIF; however, "[t]he

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[20] Of course, even in the absence of such a legislative statement as to a particular decision by the Idaho Supreme Court: "[s]tatutes are construed under the assumption that the legislature was aware of all other statutes and legal precedn[t] at the time the statute was passed." State, ex rel. Wasden v. Maybee, 148 Idaho 520, ____, 224 P.3d 1109, 1118 (Idaho 2010)(quoting Druffel v. State, Dep't of Transp., 136 Idaho 853, 41 P.3d 739 (2002); *accord* Smith v. Washington County, ___ Idaho ___, ___ P.3d ____, 2010 WL 3895341 (Idaho, October 6, 2010)("We presume that when it amended §12-117(1), the Legislature was aware of the prevailing judicial interpretation of that statute and specifically chose to change that interpretation.").

money in the fund does not belong to the state . . . [the money is held by the treasurer] . . . for the contributing employers and the beneficiaries of the compensation law, and for the payment of the costs of the operation of the fund." State ex rel. Williams v. Musgrave, 84 Idaho at 84.

Additionally, I.C. § 72-913 directs that premiums be set "at the lowest possible rate consistent with the maintenance of a solvent state insurance fund and the creation of a reasonable surplus and reserve." Public corporations are required to first attempt to insure through the SIF, unless declined as a matter of risk or if they opt to self-insure. I.C. § 72-928(a); City of Boise v. Industrial Comm'n, 129 Idaho 906, 935 P.2d 169 (1997). SIF's own stated underwriting policy requires that "It is the policy of the Idaho State Insurance Fund (ISIF) to offer insurance coverage to **all Idaho employers** who are required, by Idaho Code, to obtain workers compensation insurance on their Idaho employees and who are willing to comply with reasonable business terms and conditions," subject to limited circumstances where an employer may be cancelled, non-renewed, or refused to quote. (Alcorn Aff., Exh. A.)(emphasis added).

Further, the SIF is also statutorily required to administer workers' compensation claims for the Idaho National Guard, but is forbidden from collecting premiums or otherwise charging for such administration – in effect, serving as the Idaho National Guard's third-party administrator for free. I.C. § 72-928(b). Thus, it is clear that the SIF "serves a 'public purpose.'" State ex rel. Williams v. Musgrave, 84 Idaho at 85; *accord* Board of County Com'rs of Twin Falls County v. Idaho Health Facilities Authority, 96 Idaho 498, 502, 531 P.2d 588, 592 (1974)("Thus, no entity created by the state can engage in activities that do not have primarily a public, rather than a private purpose, nor can it finance or aid any such activity.").

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[21] Note, again, that the SIF Board is comprised of individuals appointed by the Governor, two of whom are required to be sitting legislators. I.C. § 72-901(2).

Moreover, the very requirement of workers' compensation is, itself, an express exercise of the police power of the State:

> DECLARATION OF POLICE POWER. The common law system governing the remedy of workmen against employers for injuries received and occupational diseases contracted in industrial and public work is inconsistent with modern industrial conditions. The welfare of the state depends upon its industries and even more upon the welfare of its wageworkers. The state of Idaho, therefore, exercising herein its police and sovereign power, declares that all phases of the premises are withdrawn from private controversy, and sure and certain relief for injured workmen and their families and dependents is hereby provided regardless of questions of fault and to the exclusion of every other remedy, proceeding or compensation, except as is otherwise provided in this act, and to that end all civil actions and civil causes of action for such personal injuries and all jurisdiction of the courts of the state over such causes are hereby abolished, except as is in this law provided.

I.C. § 72-201.

Accordingly, given the Legislature's inherent control over an entity which is purely a creature of statute and which serves a public purpose, as well as its inherent police power to involve itself in matters of workers' compensation coverage, the Legislature's exercise of legislative control over statutes governing such constitutes a legitimate public purpose. Particular as to the repeal of I.C. § 72-915, the reasons were clear: the *Farber* ruling, which conflicted with years of dividend practices by the SIF and the "intent of the legislature to have the State Insurance Fund operate like an efficient insurance company subject to regulation under Title 41, Idaho Code, including the dividend provision set forth in Title 41, Chapter 28, Idaho Code," "could subject the State Insurance Fund to pay dividends on policies that are not financially profitable, thereby restricting the Fund's ability to reduce premiums and pay dividends to profitable policyholders." (Counsel Aff., Exh. C, Statement of Purpose.) Note, again, in that this is especially critical in light of the absence of the "safety net" for policyholders afforded by the Idaho Insurance Guaranty Association, which SIF is forbidden from being a member thereof. (Alcorn Aff., ¶15; I.C. §72-901(4)).

Further, another financial risk in not correcting the interpretation of the Idaho Supreme Court was direct financial impact to public coffers: "[t]he State of Idaho and public entities, which are insured by the State Insurance Fund, face losing all or part of their future dividends and deviations as a result of uncertainties as to the effect of a recent Supreme Court decision. Based on dividends and rate reduction deviations provided by the State Insurance Fund over the past two years, that number could exceed $5,000,000 annually." (*Id.*, Fiscal Note.) In doing so, the Legislature made clear that its intent was to allow the SIF – the largest workers' compensation carrier in the State of Idaho – to compete with private insurers that were not under the constraints of dividend requirements defined by the *Farber* court in analyzing I.C. § 72-915 - "This legislation will allow the State Insurance Fund to issue dividends in the same manner as other insurance companies operating within the State of Idaho."[22]

Thus, even if the repeal of I.C. § 72-915 constituted a substantial impairment on the SIF policy with its policyholder, the Legislature had a legitimate public purpose behind the repeal, as demonstrated by its Statement of Purpose, Fiscal Note, its statutory authority over the SIF, and its exercise of police power in the realm of workers' compensation insurance.

4. The adjustment of the rights and responsibilities of SIF and its policyholders, if any, is based upon reasonable conditions and is a character appropriate to the public purpose justifying the repeal of I.C. § 72-915.

Again assuming *arguendo* that the Legislature caused a substantial impairment of a contractual right, not only are Plaintiffs unable to show that the Legislature lacked a significant public purpose in repealing I.C. § 72-915, they are unable to show that any adjustment of the

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[22] Certainly, in 1998, the Idaho Legislature intended to place the SIF on equal footing with private insurers: "Finally, in the 1998 amendments to the SIF's statutes, I.C. §72-901(4) was added to make it clear the SIF is subject to, and must comply with, the provisions of the Idaho insurance code. That provision also states '[f]or purposes of regulation, the state insurance fund shall be deemed to be a mutual insurer.'" Kelso, 134 Idaho at 134.

rights and responsibilities of the contracting parties is not based upon reasonable conditions and is not of a character appropriate to the public purpose.

The repeal of I.C. § 72-915 is a narrow repeal, only impacting a discretionary dividend that is merely incidental to the core function of Plaintiffs' policies. In addition, the repeal has no impact on the express terms of the policies, and the right to a dividend has not been abolished altogether. The law has merely been changed to conform with the methodology for calculating dividends that the Manager has used for years.

Finally, any adjustment is of a character appropriate to the public purpose behind the repeal. As noted by the Legislature's Fiscal Note, the cost of reading the repeal as unconstitutional could drain upwards of $5,000,000 from the public coffers. By contrast, the Manager's current method of calculating dividends results in the SIF remaining competitive and efficient and able to offer workers' compensation coverage to Idaho employers at the lowest premium rate. In short, Plaintiffs' cannot show that any adjustment to the rights of the parties is not based upon reasonable conditions or inappropriate to the character of the public purpose behind the repeal.

CONCLUSION

Accordingly, for the reasons stated above, the repeal of Idaho Code §72-915 forecloses Plaintiffs' claims, and the Court should grant summary judgment in favor of SIF.

DATED this 26th day of October, 2010.

HALL, FARLEY, OBERRECHT
& BLANTON, P.A.

#6432

By _____
Richard E. Hall - Of the Firm
Keely E. Duke - Of the Firm
Attorneys for Defendants

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 26th day of October, 2010, I caused to be served a true copy of the foregoing document, by the method indicated below, and addressed to each of the following:

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Attorneys for Defendants

IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT OF THE STATE OF IDAHO, IN AND FOR THE COUNTY OF CANYON

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE, LLC OF SALMON,

Plaintiffs,

vs.

THE IDAHO STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its Manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN and MAX BLACK and STEVE LANDON, in their capacity as members of the Board of Directors of the State Insurance Fund,

Defendants.

Case No. CV 09-13607-C

DEFENDANTS' NOTICE OF ERRATUM RE: MEMORANDUM IN SUPPORT OF DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

Defendants The Idaho State Insurance Fund, James M. Alcorn in his official capacity as its Manager, and William Deal, Wayne Meyer, Gerald Geddes, John Goedde, Elaine Martin, Mark Snodgrass, Rodney A. Higgins, Terry Gestrin, Max Black, and Steve Landon in their

capacity as members of the Board of Directors of the State Insurance Fund (collectively, "SIF"), by and through their counsel of record Hall, Farley, Oberrecht & Blanton, P.A., hereby notify the Court and all parties of the following erratum in SIF's Memorandum in Support of Defendants' Motion for Summary Judgment, filed October 26, 2010, in lieu of filing an amended memorandum:

1. Footnote 14 on page 8: "See Affidavit of Donald W. Lojek filed on January 6, 2007, Ex. 1 (State Insurance Fund Workers Compensation and Employers Liability Insurance Policy)." This footnote should correctly read: "See Affidavit of Donald W. Lojek in Support of Plaintiffs' Motion for Partial Summary Judgment, filed September 23, 2010, at Exhibit A (State Insurance Fund Workers Compensation and Employers Liability Insurance Policy)."

DATED this 29th day of October, 2010.

HALL, FARLEY, OBERRECHT
& BLANTON, P.A.

#6432

By _____
Richard E. Hall - Of the Firm
Keely E. Duke - Of the Firm
Attorneys for Defendants

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 29th day of October, 2010, I caused to be served a true copy of the foregoing document, by the method indicated below, and addressed to each of the following:

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IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT OF THE STATE OF IDAHO, IN AND FOR THE COUNTY OF CANYON

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE LLC OF SALMON,

Plaintiffs,

vs.

THE IDAHO STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its Manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN AND MAX BLACK AND STEVE LANDON in their capacity as member's of the Board of Directors of the State Insurance Fund,

Defendants.

CASE NO. CV 09-13607-C

MEMORANDUM IN OPPOSITION TO DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

COME NOW THE PLAINTIFFS, by and through undersigned counsel, and provide the Court with a Memorandum in Opposition to Defendants' Motion for Summary Judgment:

I. INTRODUCTION

Plaintiffs have filed this case on behalf of two policyholders of the Defendant Idaho State Insurance Fund (hereafter "the Fund") and its Manager. The gravamen of this action, which is styled as a class action, is the by now incontrovertible notion that for all the years in question, which include at least 4years and arguably 6 years, the Fund breached its contracts with its policyholders. *Farber v. Idaho State Insurance Fund,* 147 Idaho 307, 208 P.3d 289 (2009).[1] In that matter, the Court ruled that the I.C. § 72-915 was a part of the contract between the Fund and its insureds, that it was clear and unambiguous, and that it required the Fund to distribute a declared dividend among all time-qualified policyholders *pro rata*, based on the amount of their premiums during the applicable period.

The proposed class in this action consists of policyholders who, for one or more of the years in the class period were billed more than $2,500 in premiums but received less than, or none of, a *pro rata* share of the dividend distributed by the Fund in each such year. Thus, as this case comes to the Court, if Idaho Code § 72-915 applies, there can be no doubt that the Fund has breached its contracts with the Plaintiffs and the members of the proposed class; that the Fund has caused millions of dollars of damage by the breach and that the damages due to each class member are mathematically determinable.

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1. The Court originally issued its opinion on March 5th, 2009. Thereafter the Defendants filed a Petition for Rehearing. The Court's substitute opinion was issued on May 5th, 2009, and it was followed shortly thereafter by an Order denying the Petition for Rehearing.

II. BACKGROUND FACTS AND PROCEDURAL POSTURE

The Fund was created by the Legislature in 1917, and has, since its inception, been governed by a set of laws now codified in Chapter 9 of Title 72. From the creation of the Fund, the sole authority it possessed to pay dividends derived from one and only one statute, namely I.C. § 72-915. Prior to its repeal in 2009, this enactment has only been amended to change the language regarding the person or entity which has the discretion to declare a dividend and the last time this occurred was in 1941. *See, Idaho Code, Bound Volume of Titles 68-73, 2006 Edition.*

After the Idaho Supreme Court initially ruled in *Farber* that the Fund must allocate dividends on a *pro rata* basis, the Fund evidenced its dissatisfaction with this decision (issued on March 5th, 2009) by filing a Petition for Rehearing. The Petition advanced claims in support of its arguments against and criticisms of the Court's decision. Despite the fact that all of these claims were rejected, they now appear in a transmuted form in the Fund's Memorandum and other pleadings in this cause. Instead of giving any relevance to these claims, the Supreme Court suggested that, if the Fund believed it was necessary to change the wording of the dividend statute in order that it might thereafter distribute dividends in a manner other than required by the unambiguous wording of I.C. § 72-915, the correct course of action would be to "approach the Legislature to change the law" *Id. at 313.* However, this suggestion cannot be read as an invitation to pass legislation which retroactively relieved the Fund of its established and generally vested obligations in derogation of the "contracts clause" of the Idaho Constitution.

The day after the Supreme Court of Idaho issued its substitute opinion in *Farber,* the Governor signed Senate Bill 1166 as amended (hereinafter SB 1166), by which the Idaho Legislature repealed I.C. §72-915. As a consequence, all contracts of insurance entered into by

the Fund after the effective date of the bill will no longer include, as one of their terms, the statutory provision regarding dividends. SB 1166 also includes the provision that the repeal is to be retroactive to January 1, 2003. This aspect of SB 1166 is at issue in this action which seeks to recover dividend shares owed to class members based on dividends distributed between December 2004 and January 2010.

On September 22, 2010, Plaintiffs have filed a Motion for Partial Summary Judgment, asking the Court to find and declare that the repeal of I.C. § 72-915 is unconstitutional insofar as it is applied retroactively in order to terminate the contractual right of the Fund's already existing policyholders to be paid dividends (a right which in most instances was fully vested) according to the method mandated by their contract of insurance with the Fund, as it was construed by the *Farber* Court. Plaintiffs' Motion is based solely upon the prohibition against the impairment of contractual rights as stated in Article 1, Section 16 of the Constitution of Idaho (Idaho Contracts Clause) as that prohibition has been interpreted and applied in Idaho decisional law. Idaho Courts, when considering legislative action which works to retroactively impair citizens' rights under contracts with entities created by the Idaho Legislature, have consistently found such statutes to be unconstitutional.

On or about October 26, 2010, the Fund filed a Motion for Summary Judgment. The Fund's Motion rests upon the premise that the analytical methodology used by Federal Courts in applying the prohibition against State action which impairs contracts set out in Article 1 Section 10 of the United States Constitution (Federal Contracts Clause) must be used by Idaho courts in evaluating a claimed violation of the Idaho Contracts Clause. This methodology requires a court to make several determinations which are not salient to the determination of the protection

provided to Idaho citizens by the Idaho Contracts Clause.

III. SUMMARY OF ARGUMENT

In framing its claim that methodology employed in Federal decisional law for testing a statute against the Federal Contracts Clause should be applied for testing that statute against the State Contracts Clause, the Fund has totally ignored the entire body of **Idaho** Appellate cases interpreting the **Idaho Contracts Clause**. The Fund premises its claim upon several Federal Court decisions, decisions from other states and upon what is easily demonstrated to be a fallacious notion, which is unsupported by any cited Idaho case, that this Court should apply Federal methodology because in one decision an Idaho Court determined that a statute was not unconstitutional "without making a distinction between the two constitutions." *Memorandum In Support Of Defendants' Motion for Summary Judgment,* p. 21 (hereinafter Def. SJ Memo). In support of this tortured logic the Fund cites *State v. Korn,* ___ Idaho ___, 224 P. 3d 480 (2009). However, the Fund's reliance upon *Korn* is not supported by a reasoned reading of the case and it is belied by the fact that when the Idaho Supreme Court was afforded an opportunity to apply Federal law interpreting the Federal Contracts Clause to resolve a challenge to an enactment based on the Idaho Contracts Clause, the Court declined the invitation and held instead that based on the Idaho Constitution the Legislature does not have the power to retroactively modify a contract.

Even if the Idaho Appellate Courts were to countenance applying Federal decisional law as the standard for interpreting the Idaho Contracts Clause, the case that the Fund relies upon has no application to the issues in this case. Moreover, even if Federal law required in the factual circumstances of the instant action that the Court, after finding that an impairment has occurred,

evaluates the public purpose behind and the reasonableness of the legislative action causing that impairment, that evaluation must be based entirely upon the legislative record (hence Plaintiffs have filed a *Motion to Strike the Affidavit of James M. Alcorn and Selected Exhibits Attached to the Affidavit of Counsel, Both of Which Were Filed in Support of Defendants' Motion for Summary Judgment*). However, if this established principle were found not to be controlling, and the Court concluded it could look to facts beyond the findings made by the Legislature, then it would be manifestly unfair to proceed to rule on the Fund's Motion for Summary Judgment given that Plaintiffs have been precluded from conducting discovery (hence Plaintiffs have filed *Plaintiffs' Motion Pursuant to Rule 56(f), to Vacate Defendants' Motion for Summary Judgment and to Continue that Motion Pending Discovery by Plaintiffs).*

The Fund rests its characterization of the applicable Federal law primarily upon *RUI One Corp. V. City of Berkeley,* 371 F. 3d 1137 (9th Cir.2004). *RUI*, however, is of little avail to the Fund, as it does not involve a retroactive change to a term of the contract at issue and, in addition, it is decided on one of the threshold determinations not at issue in this matter. Moreover, the majority opinion features very little analysis of the various inquiries and sub-inquiries that comprise a detailed Federal Contracts Clause analysis.

In response to the Fund's characterization of the Federal law as controlling, Plaintiffs will demonstrate that when the Federal methodology is correctly applied to the relevant facts of this case, SB 1166 is unconstitutional.

First, the retroactive repeal of I.C. § 72-915, even standing alone, operates as a substantial impairment of the contractual relationship between the Fund and the Plaintiff class by abrogating the established and, in most instances, fully vested contractual rights of the class members. In

this regard, it must be acknowledged that the Fund is a state managed insurance fund, which was created by statute and that, as a consequence, an impairment of a public contract is deemed substantial if it deprives a private party of an important right, thwarts performance of an essential term, defeats the expectations of the parties, or alters a financial term. In this case we need look no further than the words of the Fund's manager (in the Affidavit he filed in the *Farber* action) to find confirmation of the fact that the dividend statute defines a financial provision important to many policyholders. *See Affidavit of Philip Gordon re:Defendants Motion for Summary Judgment., Doc No.* 000127 ¶¶ 31,32.

Second, Plaintiffs will demonstrate that when the Court directs its attention to the findings expressed by the Legislature, as it must do, it will be clear that the Fund has failed to and cannot identify a legitimate and substantial public interest which is served by impairing the existing and largely fully vested contract rights of the Plaintiffs and the class members. In assessing whether a statute which impairs obligations, the United States Supreme Court has distinguished between, on the one hand, generally applicable laws that remedy broad, widespread economic and social problems, and, on the other, those enactments with an extremely narrow aim, designed to benefit only a single entity. The Supreme Court employs closer scrutiny where the statute at issue has a narrow focus, and it has recognized that a retroactive statute lacks a legitimate purpose when it has a "very narrow focus" and is "aimed at specific" parties.

Third, even if the Court could discern some underlying legitimate and substantial public purpose, looking again solely at the findings expressed by the Legislature, it will be clear that the Fund cannot demonstrate that, in the circumstances present in this case, the impairment generated by the retroactive application of SB 1166 represents a reasonable means for or is of a character

appropriate to the furtherance of that public interest. In making this inquiry, because the Fund is a public entity which is seeking to benefit from legislative action which removes an established and largely vested financial obligation from its contracts, the Court must apply strict scrutiny to the legislative findings and is not permitted to defer to those findings or to permit the Legislature to put an impairment of contract on a par with other policy alternatives.

IV. THE SUMMARY JUDGMENT STANDARD

Plaintiffs agree in principle with the Fund's formulation of the standard for the granting of summary judgment, namely summary judgment shall be rendered "if the pleadings, depositions and admissions on file, together with the affidavits, if any, show that there is no genuine issue of material fact and that the moving party is entitled to a judgment as a matter of law." *see, Def. SJ Memo* p. quoting IRCP Rule 56 (c). This rule cannot, however, be read as a justification for injecting into the record and then asking the Court to review and give weight to a good deal of irrelevant information. These concerns and the consequences of allowing irrelevant information into the record are addressed in Plaintiffs' motion to strike and motion for Rule 56(f) relief.

V. ARGUMENT

A. The Standard applied to declaring a statute unconstitutional

Plaintiffs agree that they shoulder the initial burden of convincing this Court that the challenged enactment is unconstitutional. Plaintiffs contend, however, that the unconstitutionality of making the repeal of the dividend statute retroactive is clear and obvious, *see Memorandum in Support of Plaintiffs' Motion for Partial Summary Judgment* (incorporated herein). It is enough that SB 1166 is unconstitutional under the protection afforded to Idaho

citizens by the Idaho Contracts Clause. However, if the Court deems it necessary to apply any of the methodology developed by Federal Courts for determining if State action violates the limits imposed upon the States by the Federal Contracts Clause, then the Court should be aware that, in the event that State action retroactively terminates the contract rights of a citizen who is a party to a contract with a public entity, then the burden shifts to the State or public entity to demonstrate the existence of a legitimate and significant public purpose and an impairment which is a reasonable means for and of a character appropriate to the furtherance of that public interest. *S. Cal. Gas Co. v. City of Santa Ana*, 336 F.3d 885, 889(9th Cir. Cal 2003).

B. The Idaho Supreme Court has never employed Federal law and Federal standards in analyzing a claim that an Idaho statute violates Article 1, Section 16 of the Idaho Constitution

The Fund's entire argument that SB 1166 can withstand a challenge brought under Idaho Contracts Clause rests upon the threshold proposition that the matter should be determined by application of Federal decisional law. To get to this proposition the Fund points out that "plaintiffs have pled violations of both the state and federal constitutions" *Def. SJ Memo,* p. 20 and then, in misplaced reliance upon *State v. Korn*, 148 Idaho 413, 224 P.3d 480(2009), the Fund concludes that "the examination conducted by this Court will be the same" in both instances. *Def. SJ Memo,* pp. 20-21.

The linkage suggested by the Fund is faulty. First, there is no authority for the proposition that Plaintiffs must prove that SB 1166 violates the prohibition established by both contract clauses. Second, the Fund has not, and cannot so far as Plaintiffs are able to discern, cited a single Idaho case which either employs Federal methodology in determining if State action violates the Idaho Contracts Clause or holds that Federal methodology should be applied

to determine if State action violates the Idaho Contracts Clause.

The best that the Fund can do is to point out that in *State v. Korn* a criminal defendant argued a violation of his rights under the State Contracts Clause and the Federal Contracts Clause and that in that case the Court proceeded to rule against this assertion without distinguishing between the two clauses or the jurisprudence surrounding them. However, when *Korn* is examined and when relevant Idaho cases are reviewed, it is apparent that, Idaho courts have: 1.) consistently resolved challenges to acts of the Legislature which are based on the Idaho Contracts Clause through application of Idaho law and Idaho constitutional principles; 2.) consistently applied a zero tolerance standard to Legislative attempts to retroactively impair existing contractual rights and obligations; and 3.) declined, when considering whether a statute could be applied retroactively without violating the Idaho Contracts Clause, to apply the Federal methodology even though only ten months earlier a United States District Judge for the District of Idaho had found that the very same statute could be retroactively applied without violating the Federal Contracts Clause.

On these bases, this State Court should look to the extensive body of state decisional law interpreting the state constitutional provision, the entirety of which was apparently deemed unworthy of mention by the Fund.

1. ***State v. Korn* is altogether inapposite and provides no support for this Court to equate the jurisprudence interpreting the state and federal contract clause provisions.**

To the extent that the Fund is intending to suggest that *State v. Korn* can be taken as authority for the proposition that Idaho courts should apply Federal methodology in determining

if State action violates the Idaho Contracts Clause, the Fund is totally distorting the meaning and import of the decision in *Korn.* Nowhere in its opinion does our Supreme Court engage in any substantive analysis of whether or not the ordinance Korn challenged violated either the State or Federal Contracts Clause. Nor does the Court ever state or imply that if it were to engage in such an analysis it would utilize the same case law, the same standards or the same analytical methodology to assess whether or not the law in question violated the two different constitutional provisions. Instead, our Supreme Court, faced with Korn's claim that a County ordinance violated his rights under both the State Contracts Clause and the Federal Contracts Clause found that:

> Both the magistrate and district courts assumed that contracts existed between Korn and his mother and Korn and DDR at the time the County passed the ordinance. There is, however, no substantial, competent evidence that Korn had a contract with either his mother or DDR at the time the ordinance took effect. 224 P. 3d 480, 482. (E.A.)

Following on its conclusion -reached without any citation to either federal case law or federal rules of evidence- that there was no contract to impair when the ordinance passed, the Court then concluded as follows:

> This is significant because "[t]he ...contracts clause protects only those contractual obligations already in [483] existence at the time the disputed law is enacted." *Allied Structural Steel Co. V. Spannaus,* 438 U.S. 234, 241, 98 S. Ct. 2716, 57 L.Ed. 2d 727 (1978). 224 P. 3d 480, 482-3.

In other words, having found as a matter of evidentiary -as opposed to constitutional- law that the necessary condition precedent for invocation of any "contracts clause" claim -i.e. the antecedent existence of a contract creating rights which can be impaired- had not been met, our Court never conducted any analysis relative to either the Federal Contracts Clause or the State Contract Clause and consequently never considered what analytical methodology should be

applied.

To suggest that this case lends any support to the notion that this Court should ignore all Idaho decisional precedent and resolve the State constitutional issue presented in this case based entirely on federal law finds is unjustifiable. The fact that the Idaho Court cited a federal decision in this very limited and specific context can easily be accounted for. Both Constitutions forbid impairing "the obligations of contracts." By definition, the prior existence of a contract with rights and obligations is, under any analysis, a condition precedent to the either Constitutions' prohibition upon the enactment a law or ordinance which could impair that contract. Korn thus cannot be read as holding or even suggesting that Idaho Courts should apply Federal methodology to determine whether legislative action which works to retroactively impair citizens' rights under contracts with entities created by the Idaho Legislature violates the Idaho Contracts Clause.

2. **The Idaho Supreme Court was provided with a perfect opportunity to employ federal law to resolve a contracts clause challenge under the state constitution, and it did not.**

On January 4th, 1954, United States District Judge Chase Clark issued his opinion in the case of *U.S. for Use and Benefit of Midwest Steel & Iron Works Co. v. Henley, 117 F. Supp. 928 (D. Idaho 1954)*(cited by the Fund, *Def SJ Memo* p. 29). That was an action brought under a federal statute known as the "Miller Act" to recover from a Defendant and its surety. The contract and the bond which were the subject of the suit were entered into on November 15th, 1950. *117 F. Supp. 928, 931.* In the 1951 session the Idaho Legislature passed a statute providing that insurance companies which fail to pay amounts justly due under their contracts or policies of insurance, and which are thereafter sued "in any court in this state for recovery under the terms of

such policy..." shall "pay such further *amount* as the court shall adjudge reasonable as attorneys's fees in such action." *Id. 117 F. Supp. 928, 929.*

After having been found to have improperly denied a claim and having had attorneys fees assessed against it pursuant to the 1951 law, the Defendant and its surety challenged the application of the statute to this pre-existing contractual relationship. The challenge was based solely upon Federal Contracts Clause. Judge Clark, resolved the challenge by using the methodology established by Federal decisional law, primarily *Supreme Ruling of the Fraternal Mystic Circle v. Synder,* 227 U.S. 497. After conducting this analysis, Judge Clark ruled that no violation of the Federal Contracts Clause had occurred.

A few months later, the Idaho Supreme Court considered whether in a case with a similar fact pattern, the same statute violated the Idaho Contracts Clause. In *Penrose v. Commercial Travelers Insurance Company,* 75 Idaho 524, 275 P.2d 969 (1954) the 1951 Idaho attorneys fees law was applied against an insurance company which was found to have wrongfully denied the Plaintiff's claim for disability benefits as provided for in a contract of insurance which was antedated the passage of the statue. After citing to Judge Clark's opinion, our Court found that the application of the statute to contracts formed prior to the passage of the statute violated the Idaho Contracts Clause.

The *Penrose* decision is structurally unusual. It features a lead opinion authored by Justice Thomas, which observes that:

> There are two decisive questions submitted before this court on appeal: First, whether or not respondent comes within the provisions of Part D, section 1 of the policy with reference to the convalescence clause thereof; secondly, whether under the terms of the insurance policy respondent, to whom the court allowed attorneys' fees in the sum of $500, is entitled to any attorneys' fees under Chapter

289, Session Laws of 1951.
Id. at 528.

Justice Thomas was joined in the lead opinion by three other members of the Court in concluding that respondent was disabled within the meaning of the policy in question, hence entitled to recovery under its disability provision. The contracts clause issue divided the five member Court in a different fashion: only one other Justice joined Justice Thomas in concluding that Idaho Contracts Clause was not violated by application of the newly passed attorneys' fees statute to a contract which was formed prior to the passage of that statute. Justice Thomas's lead opinion acknowledged the preceding decision by Judge Clark in *Henley* and he discussed the decisions of several sister State Courts. Ultimately Judge Thomas stated a conclusion which demonstrated a strong inclination to apply what is current Federal methodology.

Judge Thomas's extensive discussion in support of the minority view, even with the support of Judge Clark's opinion from *Henley* failed to persuade the majority of the Idaho Court that application of the attorneys' fees statute to contracts formed prior to its enactment was constitutional under the Idaho Contracts Clause.[2] Justice Givens speaking for the majority on the attorneys fees question, stated quite simply his belief that:

> "to apply the statute enacted after the insurance policy was written impairs the obligation of contract. Authorities supporting this proposition are cited in the majority opinion and it is unnecessary to add thereto, although there are others to like effect." 75 Idaho 524, 540.

Id. 75 Idaho at 540. Justices Porter and Keeton concurred with him, with the former observing

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[2] It should be noted that an attorney's fee statute is so close to the very fringe of an enactment that could impair a contract that it could be seen as and tolerated as merely a change in remedy and not a change in any substantive term of the contract and, despite being relatively innocuous the majority Idaho Court refused to allow it to be retroactively applied.

that:

> "To hold that Ch. 289, 1951 S.L. would apply to contracts of insurance written prior to its enactment, would create a new liability and impose a burden not covered by the terms of the insurance policy."

Id.

Penrose standing alone conclusively demonstrates that the Idaho Supreme Court does not apply federal standards, federal analyses or federal precedent to challenges to state laws, based on the State Contracts Cause. This conclusion makes sense given that the Federal Contracts Clause seeks to limit what the State can do to its citizens while still being sensitive to "States rights." Conversely, the Idaho Contracts Clause appears in the section of the Idaho Constitution which sets out the protected rights of the citizens and therefore deals with the limits that the citizens have imposed upon their State government. However, it is not necessary for the Court to rely solely upon Penrose and the arguments set forth in the *Memorandum in Support of Plaintiffs' Motion for Partial Summary Judgment* in order to decline the Fund's invitation for the Court to join them in disregarding the entire body of Idaho appellate decisions interpreting and applying the Idaho Contracts Clause. Additional compelling support can be drawn from the strong and highly salient language contained in *Straus v. Ketchen*, 54 Idaho 56, 83 (1933), which counsel only located after submitting that Memorandum.

Straus involved circumstances strikingly similar to those involve in this matter. Drainage Districts had been formed by legislative action and they were authorized by statute to issue bonds for development purposes. Provisions were made in the statute creating the Drainage Districts relative to how the bonds would be secured and repaid and those provisions were in place at the time the bonds (the contracts at issue in the decision) were issued by the Drainage District and

purchased by members of the public. Later the Legislature changed the law and allowed for a different manner of securing and repaying the bonds. If applied retroactively to the bonds at issue in the decision, the new system would have allowed some of the real property securing the extant bonds to be released from the liens, before all of the bonds were paid in full. The Plaintiff contended that this would unduly compromise the security of the bond holders. *Id.*, 54 Idaho at 59-63.

The Court refused to allow the change in the statute to be applied retroactively to bonds purchased before the passage of the statute at issue. Specifically the Court stated:

> The legislature cannot, under such constitutional prohibitions, authorize under the police power of the state the creation of a contracting agency and permit the contracting of obligations, and by the same power destroy its contracts and abolish its obligations. To permit the legislature to do so would destroy the very essence of the constitutional prohibitions. Clearly such was never the intention of the framers of the Constitution. Were it otherwise no person would ever be safe to enter into a contract with public or quasi-public corporations, creatures of the law.

Id. at 83 (Idaho 1933).

Clearly, Idaho Courts are expected to apply the Idaho Contracts Clause to prevent the Legislature from passing legislation which retroactively impairs citizen's rights under pre-existing contracts with entities created by the Idaho Legislature.

C. Were this Court to consider Federal law for any reason, it would readily become apparent that making the repeal of I.C. § 72-915 retroactive violates the United States Constitution as well.

If the Court should determine that it is appropriate to utilize Federal decisional law as the basis for interpreting the Idaho Contracts Clause, or that the case must be resolved under the Federal Contracts Clause, Plaintiffs contend that the retroactivity application of SB 1166 also violates the Federal Contracts Clause. Plaintiffs' engage in the following discussion of Federal

analytical methodology with great reluctance because Idaho's jurisprudence relative to the Idaho Contract Clause is dispositive of the unconstitutionality of the retroactive application of SB 1166.

Article 1, §10 clause 1 of the United States Constitution reads, in pertinent part, as follows:

> No state shall .....pass any bill of attainder, ex post facto law, or law impairing the obligation of contracts....

1. **Under Federal law, determination of whether a regulation violates Article I, Section 10, Clause 1 of the United States Constitution involves a three-step inquiry which begins with an inquiry into whether State action has caused a substantial impairment of a contractual relationship.**

Federal Courts employ a three step inquiry when called upon to decide whether or not a State legislative act "impairs the obligations of contracts" in contravention of the United States Constitution. *RUI One Corp. v. City of Berkeley,* 371 F. 3d 1137, 1147 (9th Cir. 2004). They define as the initial or threshold inquiry the question of whether or not the state law has acted as a substantial impairment of a contractual relationship. *Id.*

In *RUI One*, which is much relied on by the Fund, the Ninth Circuit, taking its cue from the United States Supreme Court's decision in *Gen. Motors Corp. V. Romein,* 503 U.S. 181, 186, defined this threshold question as, itself consisting of three components: "whether there is a contractual relationship, whether a change in law impairs that contractual relationship, and whether the impairment is substantial." 371 F. 3d 1137, 1147. [3]

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[3] The Ninth Circuit posited a controlling "sub-inquiry" to this initial question:

> The first sub-inquiry is not whether any contractual relationship whatsoever exists between the parties, but whether there was a "contractual agreement regarding the specific . . . terms allegedly at issue." (Citation omitted) *Id.*

Because the panel concluded that "It is at this initial phase of the analysis that RUI's claim. . . fails."*Id.*, it never actually conducted any extensive analysis either of the two otheraspects of the threshold question of whether or not a contractual relationship existed. Thus, *RUI One* is readily distinguishable from the case at bar.

a. A Contractual Relationship Exists

Here, any dispute as to whether or not there is a contractual agreement regarding the payment of dividends is foreclosed by two decisions of the Idaho Supreme Court.

In *Kelso & Irwin, P.A. v. State Insurance Fund,* 134 Idaho 130; 997 P. 2d 591(2000) The Supreme Court held:

> It is undisputed that Kelso has a contract for worker's compensation insurance with the SIF. Any violation of the provisions of that contract would constitute a breach of contract by the SIF. **Additionally, the contract necessarily incorporates the statutory framework which both created the SIF and governs the actions that can be taken by the SIF with regard to the SIF's funds.** When Kelso contracted with the SIF it was entitled to rely on the statutes creating and regulating the SIF....Consequently, any act taken by the SIF beyond its statutory authority would also be a breach of the SIF's contract with Kelso.

Id. 134 Idaho at 138, 997 P. 2d at 599. (emphasis added).

Five years later, in *Hayden Lake Fire Protection District v. Alcorn, 141 Idaho, 388, 111 P. 3d 73 (2005),* the Court reiterated the incorporation doctrine of *Kelso*, and specifically extended it to the statute governing the declaring and distribution of dividends:

> In *Kelso* this Court held that the SIF's governing statutes were incorporated in its contracts with its policyholders. [citation omitted]. *Kelso* also held that policyholders "had a right to rely on the statutes creating and regulating the SIF, and the limits those statutes place on how the SIF can invest its policyholders" premiums.[citation omitted] **This covenant reaches to the SIF's statutory obligations that are incorporated into its contracts. The SIF has duties to its policyholders regarding surplus and dividends by virtue of the fact that the implied covenant of good faith and fair dealing extends the statutes that are incorporated in the policyholders' contracts.**

Id. 141 Idaho at 399; 111 P. 3d at 84. (emphasis added)

Kelso and *Hayden Lake* both clearly establish the existence of a contractual agreement

between the Fund and its policyholders regarding the specific term before this Court.[4]

b. State law impairs a specific obligation of the Contract.

That the retroactivity application of the SB 1166 impairs the very right acknowledged in *Farber* cannot seriously be questioned. Indeed, the very fact that the Fund is asking this Court to grant them summary judgment based on the fact that the statute was repealed is in and of itself proof that, if SB 1166 can be applied retroactively, it would impair the very rights recognized by *Farber* and established by the Fund's contracts with its policyholders. If the Fund is correct, then Plaintiffs' contractual rights will be rendered nugatory by their inability to enforce them. This is not only an "impairment;" it is a destruction of the contractual right to receive a portion of the dividend corpus.

c. Retroactive application SB 1166 generates a substantial change of the Fund's contracts with its policyholders.

The Fund suggests, that the amounts involved in this cause are something other than "substantial." *Def. SJ Memo* at p.30 note 19. It points out that the dividend a policyholder with a $10,000.00 premium would have received in January, 2004, would only have been $391.91.[5] The suggestion that a loss of $391.51 is not substantial is both pointless and a distortion of the situation.

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[4] The Fund suggests that "there is no contractual right to a dividend under a SIF workers' compensation policy."*Def. SJ Memo* p.22, Plaintiffs are not claiming in the case at bar, just as they never claimed in *Farber*, that they have an absolute "contractual right to a dividend". What Plaintiffs have always contended is that, once the manager decides to pay a dividend, they, like every other policyholder, have a right to share in that dividend, *pro rata*, based entirely on the size of their premium. The *Farber* Court unanimously agreed.

[5] In making this point the Fund has used the lowest effective dividend rate from several identified years and as a consequence is not pointing out that in some years the amount at issue for a policyholder who was billed $10,000 would be just shy if 10% of the premium.

An argument over just exactly *how high* a percentage or *how many dollars* of lost dividends must be shown to make an impairment "substantial", is actually unnecessary for, as the District Court for the Central District of California observed:

> An impairment of a public contract is substantial if it deprives a private party of an important right , thwarts performance of an essential term,, defeats the expectations of the parties, or alters a financial term [citations omitted, e.a].

Southern California Gas Company v. City of Santa Ana, 202 F. Supp. 2d 1129, 1133 (2002), adopted in its entirety *S. Cal. Gas Co. v. City of Santa Ana*, 336 F.3d 885, 886 (9th Cir. Cal. 2003). Moreover, when assessing substantial impairment, Courts "need not resolve the 'question of valuation' in terms of dollars if an important financial provision is impaired...." (Citations omitted) *S. Cal. Gas Co. v. City of Santa Ana*, 336 F.3d 885, 890. "Even adjustments in implicit financial terms can constitute substantial impairment." *Id.*

The right at issue here is at the heart of the insurance contract. It bears directly upon the cost of that contract or the consideration for the issuance of the policy. The dividend is a return of the portion of the premium that was in excess of the true cost of the insurance agreement. *Farber* holds that the contract requires that this repayment must be made on a *pro rata* basis to all time qualified policyholders. SB 1166, if applied retroactively, creates so obvious an impairment to a financial term of the contract that the Fund's argument about the amount involved is incredibly misguided.

Even if the Court could evaluate the amount at stake when it is clear that a financial term of the contract has been altered, there is a good deal more at stake here than $391.91. To suggest that each policyholder's individual claim for one year is in the hundreds or even the thousands of dollars misses the point. This is a class action and the damages are an aggregate of the individual

damages, which in this case are expected to be in excess of one million dollars. This action involves thousands of policyholders and years worth of policies. That is why the Fund is defending it vigorously. The "impairment" completely destroys the right of several thousand policyholders to a *pro rata* share of the dividend corpuses that were distributed over several years. In terms of dollars the class members are being deprived of a sum of money which no one can argue is, in aggregate, *de minimus* or insubstantial.

SB 1166 would unquestionably operate to "alter a financial term" of the contract of insurance between the Plaintiffs and the members of the class on the one hand, and the Fund on the other and the impairment is substantial.

2. **Where, as here, State action has caused a substantial impairment of a contractual relationship, the Court must next determine if the impairment furthers some significant and legitimate public purpose.**

Where State action generates a substantial impairment of a contractual relationship the Court must look to determine if the impairment was intended to further some significant and legitimate public purpose. *RUI One Corp. v. City of Berkeley, supra.*, at 1147 (9th Cir. 2004). This inquiry turns upon the text of the ordinance, not the alleged motives behind it. *Id.* at 1146, note 7.

a. <u>When the State itself, or public entities are the contracting parties, strict scrutiny of any legislative measure is required and deference is not to be accorded to the declared intent of the Legislature and the State entity has the burden of proof.</u>

The Federal courts apply different standards to situations where the enactment impairs only contractual relationships between competing private actors and situations in which the State itself, a state agency or a public body such as the Fund is a party. Where the State acts to impair its own existing contracts, the far stricter scrutiny set forth in *U.S. Trust Co. V. New Jersey, 431*

U.S. 1 (1977) supplies the controlling standard. *See Energy Reserves Group, Inc. V. Kansas Power & Light Co., 459 U.S. 400 at 412 n.14* ("the stricter standard of *United States Trust Co."* applies where state alters its own contracts); *and So. Cal Gas Co. v. City of Santa Ana, 336 F. 3d 885 at 894 (9th Cir. 2003) ("Energy Reserves* approves *U.S. Trust's* holding and reasoning when state entities interfere with their own obligations.").

The law in the Ninth Circuit is clear and unambiguous: the public entity always carries the burden of proof when the legislation in question impairs a State's own contracts. *S. Cal. Gas Co. v. City of Santa Ana, supra.* 336 F.3d 890, *Univ. of Hawaii Prof Assembly v. Cayetano*, 183 F. 3d 1096, 1107 (9th Cir.21999. Laws that work an "impairment of a state's own contracts . . . face more stringent examination under the contract clause than [do] laws regulating contractual relationships between private parties . . . ." *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 244 *n.* 15, 98 S. Ct. 2716 (1978). There is a good reason for this. Parties enter into contracts to "order their personal and business affairs according to their particular needs and interests. Once arranged, those rights and obligations are binding under the law and the parties are entitled to rely on them." *Id.* at 45. When the state is a party, there is an additional risk that it will employ its sovereign powers to alter the terms of the contract. States should resist the temptation as previously arranged by contract. In this instance, the Legislature has apparently employed its sovereign power to eliminate contractual terms which the Supreme Court of Idaho has stated are binding on the Idaho State Insurance Fund. That action requires strict scrutiny.

b. <u>The Fund is a state managed legislatively created insurance fund. As such its character is much more public than private</u>.

In the pivotal case of *Kelso & Irwin, P.A. v. State Insurance Fund, supra.*, our Supreme Court was compelled first to ascertain the nature of the Fund. After making an in-depth

examination of the statutory framework applicable to the Fund, the Court rejected Kelso's core contention that, in creating the Fund, the Idaho Legislature intended to create a mutual insurance company. Instead, after comparing the statutory attributes of mutual insurance carriers to those of the Fund, the Court concluded that:

The statutory comparison referenced by the Court focused to a great extent on those provisions of Title 72, Chapter 9 which *tend to impart to the Fund a governmental or public character*, such as the fact that it "is administered and managed by people appointed by the Governor" in contradistinction to a private mutual insurance company, which "is managed by people elected by the policyholders." *Id.* 134 Idaho 135.

Again, in *Hayden Lake Fire Protection District v. Alcorn supra.* our Court stated categorically that "[t]he SIF is not a private corporation." *141 Idaho 388, at 401, 111 P.3d 73 at 86.* The Hayden Lake decision acknowledged the existence of a further aspect of the law governing the Fund which helps impart to it a public character, namely that the official actions of the Fund, like those of State agencies, are entitled to a presumption of regularity:

> The district court held that the presumption of regularity applied to the actions taken by the SIF and the State in the real estate transactions challenged by HLFPD, citing ..., which stated that "there is in Idaho, as in most states, a presumption of regularity in the performance of official duties by public officers." This conclusion was proper. (citations omitted).

Id. 141 Idaho at 403.

In sum, while the Fund has some attributes of a private corporation, and is required to conduct itself as an insurance company, it is:

> "an agency of the state created for the purpose of carrying on and effectuating a proprietary function as distinguished from a governmental function. It serves a "public purpose" but not a "governmental purpose."

State ex rel. Williams v. Musgrave, 84 Idaho 77, 85, 370 P.2d 778, 782 (Idaho 1962).

c. The Fund cannot identify a legitimate and significant public purpose which is furthered by the retroactive application of SB 1166

In order for an enactment to be deemed as having a significant and legitimate public purpose, it must be aimed at remedying a broad and public purpose. *RUI, supra*, at 1147. This is a requirement meant to guarantee that "the State is exercising its police power, rather than providing a benefit to special interests. *Id.* at 1147. SB. 1166 has neither a broad nor a public purpose, but is very narrow and specific and only designed to benefit a single entity by retroactively legitimizing its disregard of a law governing and circumscribing its conduct. Even, under a deferential standard of review, the Supreme Court has recognized that a statute may lack a legitimate purpose when it has a "very narrow focus" and is "aimed at specific" parties. *Energy Reserves, supra, 459 U.S. at 412, n. 13.* This case does not merit a deferential standard of review because, as demonstrated above the challenged State action benefits a legislatively created entity and strict scrutiny is mandated. *U.S. Trust,* 431 U.S. at 25-26

The importance of an underlying broad concern is demonstrated in *Allied Structural Steel, Co, v. Spannus,* 438 U.S. 234 (1978). At issue was a law that impaired existing pension plan contracts. The Minnesota Legislature had become aware that a large employer was planning to terminate its pension plan, thereby depriving more than 1,000 employees of certain benefits. *Id.* at 247-248 & n. 20. To protect those employees, the Legislature quickly enacted a generally applicable law that became effective several weeks before the termination could occur. *Id.* When another employer challenged the pension law, the Supreme Court struck it down because it "was not even purportedly enacted to deal with a broad, generalized economic or social problem." *Id. at 250.*

The facts here are even more extreme than in *Allied Structural Steel,* in that SB 1166 is not only meant to undo a decision of the highest Court of this State, but to reward the Fund for having ignored the clear and unambiguous language of a law which has governed its actions since its creation in 1917. The very text of both the original SB 1166 and SB 1166 as amended display that the legislative response was motivated almost entirely by the holding and, more importantly, the implications of *Farber. See, Affidavit of Philip Gordon, In Support of Plaintiffs' Motion for Partial Summary Judgment,* Documents 000100 and 000119.

Looking at the Statement of Purpose and Fiscal Note to SB1166, as amended, we see from the first sentence that the Legislature was not pleased with the adverse decision of the Idaho Supreme Court regarding the correct interpretation of I.C. § 72-915 because it "could" subject the Fund to pay dividends on policies that *are* not financially profitable. Thus, there is some speculation here ("could") with respect to *existing* policies that *may not* be "financially profitable." The consequence of that speculative statement is that the Fund *might* have its ability restricted to reduce premiums and to pay dividends to profitable policyholders. These are not findings, they are statements of possibilities and they are all concerned with future contingency. The policies involved in this class action are year-to-year contracts which are completed.

The Statement of Purpose goes on to state that the legislation "will allow' the Fund "to issue dividends in the same manner as other insurance companies operating within the State of Idaho." Taking that statement at face value and assuming that there is a public purpose expressed, the focus is clearly prospective.

The prospectivity of what the Legislature has done is confirmed by the Fiscal Note. That Note is clearly prospective and speaks to the possibility or contingency that the insured public

entities may lose all or part of their future dividends and deviations as a result of "uncertainties" as to the effect of a recent Supreme Court decision. It is stated in the Note that number "could" exceed $5,000,000 annually. A further prospective contingency is included with reference to provide businesses which "may" experience the loss future dividends and deviations.

What is not stated in the Statement of Purpose and/or the Fiscal Note is any emergency, any specific indication that the Fund will become insolvent, any prediction that the Fund will not be able to meet future obligations, or any indication that the Fund will not be able to meet its statutory function as provided in Chapter 9 of Title 72. There is nothing in the Statement of Purpose or Fiscal Note that indicates that the Fund cannot act efficiently on a prospective basis. There is nothing in the Statement of Purpose or Fiscal Note that indicates that the payment of any monies owed to the Members of the Class will keep the Fund from discharging its primary purpose of underwriting worker's compensation policies.

The Fund states that "the legislature had a legitimate public purpose behind their repeal." *Def. SJ Memo* p. 36. Even if that is true for prospective operation of the repeal, it is not enough. There must be both a "significant" and a "legitimate" public purpose for retroactive effect and no such effect is not supported by the Statement of Purpose or Fiscal Note. But that is all the Court may properly rely upon. Statements by Mr. Alcorn, whether under oath or not, or affidavits from undoubtedly well-meaning counsel for the State Insurance Fund are irrelevant to the Court's inquiry as to this test.

Behind all of this Legislative speculation is the fact that, in the course of conducting pre-trial discovery and motion practice in *Farber,* Counsel for the Plaintiffs had learned, through not only the Alcorn Affidavit but a host of other means, that the Fund was not only failing to pay any

dividends to the named Plaintiffs and the members of the class in *Farber*, but was also violating the dividend statute by employing a sliding scale percentage scale in distributing the dividends, where the larger the policyholder's premium was, the larger the percentage of the premium that was returned to them as dividend. Thus, when the *Farber* decision issued, it had to be apparent to the Fund (and its Manager, Directors and Counsel) that another class of policyholders, i.e. those who were paid some, but less than a *pro rata* share of dividends (hereafter referred to as the "second class"), might soon be seeking redress. Senator Goedde's bill was accordingly an attempt both to undo the *Farber* ruling and thereby deny justice to the class of policyholders who had been totally denied their rightful dividends, and also to foreclose any avenue of redress for the second class of policyholders, consisting of the Plaintiffs herein, and the class they seek to represent.[6] Thus it is apparent that the Legislation is clearly narrowly aimed at specific persons and businesses and is impermissible. *See Allied Structural Steel, supra.,* and *Energy Reserves, supra.*

Because SB 1166 is, in essence, nothing more than an amnesty provision for the illegal conduct of the Fund; because it only targets past wrongdoing; and because Plaintiffs do not suggest that the Legislature could not repeal the dividend statute prospectively, the Court should conclude that, under the applicable strict level of scrutiny, SB 1166 was clearly not enacted to deal with a "broad generalized economic or social problem" as required by *Allied Structural Steel supra*. This measure would never be found constitutional in the Federal Courts given its total

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6. Because they have been barred, by a Protective Order, from conducting discovery, Plaintiffs are unable to specify with any precision, the number of employers in the class. The Court will recall, however, that, at the hearing on Defendants' Motion for Protective Order, counsel for the Fund estimated the size of the class at between forty and fifty thousand. Given that the size of the class in *Farber* was approximately 43,600, counsel's estimate appears reasonable.

lack of a significant and legitimate public purpose.

3. Even if it could be shown in this case that there was a legitimate and significant public purpose to justify State action which has caused a substantial impairment of a contractual relationship, the Court must next determine if the impairment is a reasonable means for or is of a character appropriate to the furtherance of that public purpose.

Where State action generates a substantial impairment of a contractual relationship which furthers some substantial and legitimate public purpose, the Court must next look to determine if the impairment is a reasonable means for or is of a character appropriate to the furtherance of that public purpose. *RUI One Corp. v. City of Berkeley, supra.*, at 1147 (9th Cir. 2004). As before, the burden is upon the State or its legislatively created entity to demonstrate that a retroactive impairment of a contract is a reasonable means for accomplishing the public purpose. *Univ. of Hawaii Prof Assembly v. Cayetano, 183 F. 3d at 1106.* Moreover, legislative declarations and findings are not entitled to deference and the Court is expected to scrutinize the means employed to determine if they are reasonable and appropriate to the public purpose., *RUI* at 1137 and the legislature is never " free to consider substantial contractual impairments on a par with other policy alternatives." *State of Nevada Employees Ass'n, Inc.* 903 F. 3d 1223 1228 (9th Cir. 1990). The State or the legislatively created entity has the burden of proving that the impairment reasonable and appropriate to the public purpose. *So. Cal Gas 336 F. 3d 885 at 894; Univ. of Hawaii Prof Assembly v. Cayetano, 183 F. 3d at 1107.*

The task presented to the Court is to to examine the availability of alternative measures which the legislature could have taken which would have addressed its legitimate concerns without producing a concomitant impairment of the Fund's contractual obligations to the Plaintiffs and the members of the class. This inquiry must be conducted within the analytical

framework of the duty to balance the claimed public purpose with the extent of the impairment.

In making this inquiry, the Court must initially determine "if the problem sought to be resolved by an impairment of the contract existed at the time the contractual obligation was incurred", *Cayetano, supra, 183 F. 3d at 1107.* Changed circumstances and important government goals do not make an impairment reasonable if the changes circumstances are "of degree and not kind." *U.S, Trust, supra, 431 U.S. at 32.*

Here, the "problem" was the existence of a legislative enactment, which had never been materially altered and which as the Idaho Supreme Court held in *Kelso*, supra, constituted a term of all contracts entered into by the Fund. Thus, to the extent that the Legislature was free to consider a statute which it originally enacted when the Fund was created in 1917, and which it left alone for 92 years as constituting a "problem", there can be no doubt that the "problem" not only existed at the time the Plaintiffs and each and every member of the class purchased insurance from the Fund, but also was a term of each and every contract of insurance purchased from the Fund up until the effective date of the repeal. Judicial scrutiny which is stricter still is therefore required because of the dividend statute's antiquity, and its inclusion in every policy of insurance written up to the date of its repeal. In this regard the "problem" has existed for years and under these circumstances an impairment which seeks to address a problem that existed at the time the contractual obligation was incurred as been held to be manifestly unreasonable." *Univ. of Hawaii Prof'l Assembly, 183 F.3d at 1107.*

Moreover, the retroactivity application of SB 1166 is a disproportionate response to a single decision of the Idaho Supreme Court. Careful examination of both the original and amended version of SB 1166 shows that its only intended retroactive effect was to respond to the

Farber decision, by taking away rights that had existed pursuant to the Fund's contracts since 1917. As noted in the dissenting opinion in *RUI*:

> The United States Supreme Court has often expressed its suspicion of retroactive laws because they are "generally unjust" *Eastern Enterprises v. Apfel,* 524 U.S. 498, 533(O'Connor, J., plurality)(citation omitted), and "deprive citizens of legitimate expectations and upset settled transactions." (Citation omitted)

Id at 1167. Clearly retroactive application is a harsh remedy which should be sparingly used and which is difficult to justify.

It is not difficult to anticipate that the Fund will attempt to rely on the language of the repealer statute which declared the existence of an emergency. While neither the statute itself nor the legislative history defines the nature of this emergency, the only type of emergency imaginable would be one of a financial nature. To the extent that the Fund contends that broad application of *Farber* to existing contracts would impact the Fund financially, there is, in view of the Fund's $197,000,000 surplus coupled with Mr. Alcorn's testimony that *Farber* could cost the Fund 24 million (this was before it resolved about 8 million dollars worth of claims in *Farber)* no legitimate basis for that the situation was so grave as to necessitate drastic action of voiding existing and largely vested contract provisions retroactively. See the Affidavit of Philip Gordon In Support of Plaintiffs' Motion for Partial Summary Judgement, Doc. Nos. 000117-000118.[7] Nothing about these key indices of the Fund's solvency suggests any sort of emergency financial situation whatsoever. The very fact that the Fund was able to pay such a hefty sum as a dividend and still witness the simultaneous growth of its net assets and surplus should end any suggestion

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[7] Net Admitted Assets of the Fund grew by approximately $2.5 million dollars during 2009 (000117 line 26, columns 2/4); the Unallocated Surplus of the Fund ["Unassigned funds (surplus)(00011, line 33)] grew by more than seven million dollars from that on hand (000118, line 11.2) at the end of the prior year, and the Fund declared dividends to policyholders in excess of fourteen million dollars to be distributed in January, 2010

that the Fund was confronting an emergency in 2009 or as result of the claims being made in *Farber* or being made in this case.

In this matter, the only conceivable public purpose behind the passage of SB 1166 is to help the Fund be more competitive in the future. However, there is nothing about this purpose or the legislative findings which lend any justification to a retroactive repeal of the I .C. §72-915. Under these circumstances the Fund cannot met its burden to demonstrate retroactive application of SB 1166 is a reasonable means for or of an character appropriate to the furtherance of any identified legitimate and substantial public purpose.

VI. CONCLUSION

The provision of Section 1 of S.L. 2009, chapter 294 (which is the number assigned to the enacted law repealing Idaho Code §72-915 *retroactively)* clearly violates the Idaho Contract Clause.

Should, however, the Court examine the Federal precedent for any reason, which it is decidedly not **required** to do, it will become readily apparent that the attempt to make the repeal of I.C. §72-915 retroactive falls far short of surviving the strict scrutiny reserved for situations where a state or public entity is one of the contracting partners; the very strict scrutiny applied when the "problem" is one which was in existence when the contractual obligations were incurred; the extremely strict scrutiny reserved for enactments as narrow and specific in character as the one herein challenged; and the special judicial disfavor reserved for statutes which apply retroactively when they could be applied be applied prospectively.

While not required to do so in order to deny the Fund's Motion for Summary Judgment, the Court could, should it wish to render an advisory opinion, find and rule that, if the attempt to

retroactively impair Idaho citizen's rights under contracts an entities created by the Idaho Legislature herein challenged were to be scrutinized under the Federal contracts clause, using Federal law, it would also be found in violation of the United States Constitution.

For all of the reasons stated herein and in the Memorandum in Support of Plaintiffs' Motion for Partial Summary Judgment, this Court is respectfully requested to deny the Fund's Motion For Summary Judgment, and enter an order declaring that the repeal of Idaho Code §72-915 is unconstitutional insofar as it is declared to be retroactive to any date prior to the effective date of the repeal for the simple reason that, in contravention of Article 1, § 16 it impairs the Fund's obligation to honor the vested rights of the Plaintiffs and the members of the class.

Dated this 22nd day of November, 2010.

Philip Gordon

Donald W. Lojek

Attorneys for Plaintiff and the Class

CERTIFICATE OF SERVICE

I hereby certify that on the 22nd day of November, 2010, I caused the foregoing document to be delivered by the method indicated below and addressed to the following:

Richard E. Hall
Keely Duke
Hall Farley Oberrecht & Blanton
702 W. Idaho St. Ste. 700
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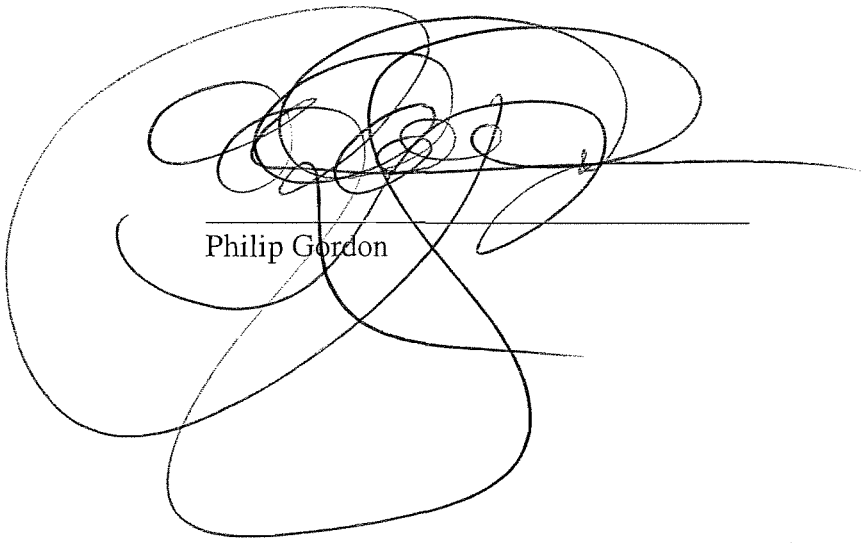
____ HAND DELIVERY
_____ U.S. MAIL
_____ OVERNIGHT MAIL
X FACSIMILE **208-395-8585**



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IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT OF THE

STATE OF IDAHO, IN AND FOR THE COUNTY OF CANYON

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE, LLC OF SALMON, Plaintiffs, vs. THE IDAHO STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its Manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN and MAX BLACK and STEVE LANDON, in their capacity as members of the Board of Directors of the State Insurance Fund, Defendants.	Case No. CV 09-13607-C **OPPOSITION TO PLAINTIFFS' MOTION FOR PARTIAL SUMMARY JUDGMENT**

COME NOW the defendants, The Idaho State Insurance Fund, James M. Alcorn in his official capacity as its Manager, and William Deal, Wayne Meyer, Gerald Geddes, John Goedde, Elaine Martin, Mark Snodgrass, Rodney A. Higgins, Terry Gestrin, Max Black, and Steve

Landon in their capacity as members of the Board of Directors of the State Insurance Fund (collectively, "SIF"), by and through their counsel of record Hall, Farley, Oberrecht & Blanton, P.A., and hereby submit their opposition to plaintiffs' Motion for Partial Summary Judgment ("plaintiffs' Motion"). For the reasons stated herein, plaintiffs' Motion should be denied.

SUMMARY OF ARGUMENT

Plaintiffs have moved for partial summary judgment, seeking a ruling from the Court that the retroactive portion of the Legislature's repeal of Idaho Code § 72-915 is unconstitutional per the Contract Clause of the Idaho Constitution.[1] However, as discussed herein, plaintiffs' Motion should be denied.

Plaintiffs have the burden of proving that the repeal is unconstitutional, and the test of whether the repeal violates the Contract Clause is a demanding one plaintiffs cannot meet in this case. Per RUI One Corp. v. City of Berkeley, 371 F.3d 1137, 1147 (9th Cir. 2004), in order to prevail on their claim that the repeal violates the Contract Clause, plaintiffs must show that:

- the state law has, in fact, operated as a substantial impairment of a contractual relationship;
- the State does not have a significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem; and
- the adjustment of the rights and responsibilities of contracting parties is not based upon reasonable conditions and is not of a character appropriate to the public purpose justifying the legislation's adoption.

[1] Although the plaintiffs' First Amended Class Action Complaint and Demand for Jury Trial references both the U.S. and Idaho Constitution, plaintiffs' Motion apparently only addresses the Idaho Constitution. *See* First Amended Complaint and Demand for Jury Trial, at ¶ 11. Plaintiffs also apparently seek to further piecemeal the questions of the repeal's constitutionality and efficacy by not addressing other arguments at this time: "If the emergency driven retroactive appeal of I.C. 72-915 is not effective the Court will be later called upon to determine if the repeal is wholly ineffective, if the repeal is effective but that the effective date is July 1, 2009, or if the repeal is effective when the Governor signed the Bill on May 6, 2009. These questions are not, however relevant, to the issues raised in this motion." Plaintiffs' Memo at n.4. To avoid a steady stream of piecemealed motions by plaintiffs, defendants have requested the ruling of the Court on all such issues of the repeal's constitutionality and efficacy in their own Motion for Summary Judgment, filed October 26, 2010.

As a matter of law, plaintiffs are unable to meet their burden under this test.

First, the Idaho Legislature has not operated a substantial impairment of a contractual relationship because there is no contractual right to dividends in the SIF workers' compensation policies. In addition, even assuming a right of contract existed, the repeal cannot be considered to have substantially impaired it. The purpose behind the Legislature's creation of SIF was to ensure the well-being of the public's wage-earners through insurance for employers who may have to pay workers' compensation, and this core function of the policies held by plaintiffs remains unchanged by application of the repeal. What is more, reading the repeal as unconstitutional would enhance, rather than impair, the rights of some policyholders.

Second, the SIF and the workers' compensation coverage it provides are creatures of statute and, when the Legislature created them, it did not prevent itself from using its police powers to shepherd the SIF, a quasi-public entity, and run it efficiently.

Third, the repeal merely conforms to the law to the way the Manager has paid dividends for years. Therefore, the only expectations the policyholders may have had for dividends to be paid otherwise would have been attributable to the *Farber* litigation and would have been uncertain and quickly quashed by the Legislature's repeal.

Fourth, the Legislature, recognizing the vitality of the SIF is necessary to the vitality of the public welfare, repealed I.C. § 72-915 so the Manager would have the authority to make the decisions necessary to the economic health and competitiveness of the entity in today's market.

Fifth, the repeal is based upon reasonable conditions and is of a character appropriate to the public purpose justifying the action.

Finally, plaintiffs' cited authority provides little to the determination of this action. Plaintiffs' cited caselaw either fails to reflect the modern, refined interpretation of the Contract

Clause and its three-step analysis, or otherwise illustrates 'easy' Contract Clause cases (that is, very substantial impairments of contracts with no justified public purpose).

Thus, for these reasons, plaintiffs' Motion should be denied.

UNDISPUTED MATERIAL FACTS

Plaintiffs provide a lengthy discussion of prior legislative history, the *Farber* decision, and the underlying dispute between the parties regarding the payment of dividends, but plaintiffs fail to identify the actual salient material facts to the determination of this motion for partial summary judgment.

The undisputed material facts this Court must consider in light of the question posed (to wit, the constitutionality of the repeal of Idaho Code § 72-915) are comparatively few in number. These facts are not – and cannot – be disputed by plaintiffs. While SIF certainly provides its own background discussion of the State Insurance Fund, and the prior *Farber* litigation, below are the undisputed material facts relevant to plaintiffs' Motion:

1) Plaintiffs' claim is predicated on Idaho Code § 72-915. Plaintiffs' suit makes claim for distribution of dividends pursuant to a pro rata distribution. However, the workers' compensation policy itself does not provide for the payment of a dividend to the policyholders.[2] Instead, the distribution methodology is set forth in the now-repealed Idaho Code § 72-915, thus making the sole basis for plaintiffs' claim that statute. Plaintiffs' First Amended Class Action Complaint and Demand for Jury Trial ("Amended Complaint") states as follows:

10.

As of June 30, 2009, Idaho Code § 72-915 provided as follows:

[2] Affidavit of Donald W. Lojek in Support of Plaintiffs' Motion for Partial Summary Judgment, filed September 23, 2010 ("Lojek Aff."), at Exhibit A (State Insurance Fund Workers Compensation and Employers Liability Insurance Policy).

> At the end of every year, and at such other times as the manager in his discretion may determine, a readjustment of the rate shall be made for each of the several classes of employments or industries. If at any time there is an aggregate balance remaining to the credit of any class of employment or industry which the manager deems may be safely and properly divided, he may in his discretion, credit to each individual member of such class who shall have been a subscriber to the state insurance fund for a period of six (6) months or more, prior to the time of such readjustment, such proportion of such balance as he is properly entitled to, having regard to his prior paid premiums since the last readjustment of rates.
>
> This term of contract between the parties requires that any dividend which the Fund elects to distribute must be distributed among all "Qualified Policyholders" (those who had entered into a contract for a policy during the period covered by any dividend being distributed and who held that policy in effect for at least six months). The term of the contract requires that total amount of the dividend be allocated into shares based upon the ratio between the amount of annual premiums billed to each Qualified Policyholder during the Dividend Period and the total annual premiums billed to all Qualified Policyholders during the same period. Neither this term of the contract nor any other term of the contract or any applicable law provides the Manager any authority whatsoever to distribute the dividend based upon any other allocation formula.

Id. at p. 6. This statutory basis for plaintiffs' claim is further confirmed in plaintiffs' Amended Memorandum in Support of Plaintiffs' Motion for Partial Summary Judgment ("Plaintiffs' Memo"): "A breach by the Fund of its duty to distribute the dividend corpus according to the statutory method set forth in Idaho Code § 72-915 thus constituted a breach of the contracts of insurance which the Fund entered into with the Plaintiffs and the members of the Class." *Id.* at 11. Thus, it is an undisputed material fact that plaintiffs' claim is based on Idaho Code § 72-915.

2) Idaho Code §72-915 was repealed on May 6, 2009. While the *Farber* litigation was still pending before the Idaho Supreme Court, the Idaho Legislature voted to repeal I.C. § 72-915. (Affidavit of Counsel in Support of Defendants' Motion for Summary Judgment, filed October 26, 2010 ("Counsel Aff."), at Exh. C.) The repeal specifically provided that: "An emergency existing therefor, which emergency is hereby declared to exist, Section 1 of this act

shall be in full force and effect on and after passage and approval, and Section 2 of this act shall be in full force and effect retroactively to January 1, 2003." (*Id.* at § 3.) The repeal was approved in the Legislature, and advanced to the Governor, who signed it on May 6, 2009. *Id.*

The Idaho Supreme Court then denied Respondent's Petition for Rehearing on May 12, 2009, and issued its Remittitur to the District Court on May 27, 2009. (Counsel Aff., Exh. F.)

3) Idaho Code §72-915 was repealed to a retroactive date of January 1, 2003. When Idaho Code §72-915 was repealed, it was retroactively repealed to January 1, 2003:

> An emergency existing therefor, which emergency is hereby declared to exist, Section 1 of this act shall be in full force and effect on or after passage and approval, and Section 2 of this act shall be in **full force and effect retroactively to January 1, 2003.**

Counsel Aff., at Exh. C (emphasis added). Plaintiffs do not dispute that the repeal was expressly retroactive to January 1, 2003.[3] *See* Plaintiffs' Memo at 12 (stating that: "The very wording of the Bill repealing Idaho Code § 72-915 permits no doubt that the Idaho Legislature intended the repeal to have retroactive effect and be applied retroactively so that certain of the Fund's contractual obligations would be impaired."). Thus, it is an undisputed material fact that Idaho Code § 72-915 was repealed retroactively to January 1, 2003.

4) Plaintiffs' claims all relate to dividend distributions after January 1, 2003. Plaintiffs' Amended Complaint expressly states that "this action pertains to any dividends distributed after December 24, 2004." (Amended Complaint, ¶ 12).[4] Thus, it is an undisputed material fact that plaintiffs' claims all related to dividend distributions after January 1, 2003.

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[3] Idaho law reflects the Legislature's authority to pass retroactive legislation, but requires that retroactive laws be expressly declared retroactive. *See* Idaho Code §73-101. Here, there is no dispute that the repeal is expressly declared to be retroactive in conformity with this requirement.

[4] SIF disputes plaintiffs' use of a 5-year statute of limitations. Rather, as plaintiffs' action is based in statute, a 3-year statute of limitation should apply. However, for purposes of opposing plaintiffs' Motion, SIF references plaintiffs' claimed 5-year period to demonstrate that, even under plaintiffs' broadest theory, there is no dispute that the retroactive repeal of Idaho Code § 72-915 forecloses plaintiffs' action.

5) Plaintiffs' action was not filed until December 24, 2010. Plaintiffs' initial complaint in this action was filed on December 24, 2009, as reflected on ISTARS.

6) Plaintiffs' claim is foreclosed if the repeal is upheld. The Legislature only provided a limited carve-out to the retroactive effect of the repeal of Idaho Code § 72-915, that being for extant litigation (and, in particular, the *Farber* action):

> (6) it is the intent of the Legislature that the provisions of this act shall not apply to any action filed in a state or federal court of law in the state of Idaho on or before December 31, 2008, and the provisions of this act shall not apply to the aforementioned case of *Farber v. Idaho State Insurance Fund* as currently pending with respect to those policy holders paying annual premiums of not more than two thousand five hundred dollars ($2,500).

(Counsel Aff., Exh. C.) As outlined above, as plaintiffs' action was filed on December 24, 2009, and relates to dividend distributions from December 24, 2004 going forward, if the repeal is upheld, plaintiffs' action is fully foreclosed, a point plaintiffs do not appear to dispute. *See* Plaintiffs' Memo at 22 ("[A]bsent the retroactivity provision of the legislation, the Fund would have been obligated to pay to the Plaintiffs and the members of the Class such sums as would result in their receiving their *pro rata* share of the total dividends paid.")(emphasis added).

7) The purpose of the SIF is to provide Worker's Compensation coverage to Idaho employees. In 1917, the Idaho legislature enacted a comprehensive statutory scheme, now codified as I. C. §§ 72-901 *et seq.*, creating the SIF "for the purpose of insuring employers against liability for compensation under this worker's compensation law ... and of securing to the persons entitled thereto the compensation provided by said laws." I.C. § 72-901(1). Since its enactment, the SIF has fulfilled its public purpose by providing worker's compensation coverage to thousands of Idaho employers who have relied on such service being available.[5]

BACKGROUND

Although the undisputed materials facts as identified above are the necessary facts in deciding plaintiff's Motion for Partial Summary Judgment, it is helpful to review the background of the State Insurance Fund, the *Farber* litigation, and the related Idaho Supreme Court decision giving rise to the legislative repeal of Idaho Code § 72-915. In an effort to reduce duplication, however, SIF instead references and incorporates as if fully set forth herein its "Background" section outlined in its own Memorandum In Support of Defendants' Motion for Summary Judgment, filed October 26, 2010, at pp. 4-13.

STANDARD OF REVIEW

A. The Summary Judgment Standard.

Motions for summary judgment should be granted only when no genuine issues of material fact exist after the pleadings, deposition, admission and affidavits have been construed most favorably to the non-moving party and the moving party is entitled to a judgment as a matter of law. I.R.C.P. 56(c); Johnson v. Studley-Preston, 119 Idaho 1055, 1057, 812 P.2d 1216, 1218 (1991). Additionally, the court must construe the record liberally in favor of the non-moving party and draw all reasonable factual inferences in favor of such party. Bear Lake West Homeowner's Assoc. v. Bear Lake County, 118 Idaho 343, 346, 796 P.2d 1016, 1019 (1990). Furthermore, all doubts are to be resolved against the moving party and the motion must be denied if the evidence is such that conflicting inferences may be drawn therefrom, and if reasonable people might reach different conclusions. Parker v. Kokot, 117 Idaho 963, 966, 793 P.2d 195, 198 (1990).

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[5] *See* Affidavit of Jim Alcorn in Support of Defendants' Motion for Summary Judgment, filed October 26, 2010, at ¶ 13 ("Alcorn Aff.").

B. **The Standard Applicable to Declaring a Statute Unconstitutional.**

Idaho law is clear that legislative acts are presumed to be constitutional: "[a] legislative act is presumed to be constitutional and all reasonable doubt as to its constitutionality must be resolved in favor of its validity." Oneida County Fair Bd. v. Smylie, 86 Idaho 341, 346, 386 P.2d 374, 376 (1963). The burden of proving that a legislative act rests squarely on the challenger:

> There is a presumption in favor of the constitutionality of the challenged statute or regulation, and the burden of establishing that the statute or regulation is unconstitutional rests upon the challengers. An appellate court is obligated to seek an interpretation of a statute that upholds it [sic] constitutionality. The judicial power to declare legislative action unconstitutional should be exercised **only in clear cases.**

Stuart v. State, 149 Idaho 35, ___, 232 P.3d 813, 818 (2010) (quoting Am. Falls Reservoir Dist. No. 2 v. Idaho Dep't of Water Res., 143 Idaho 862, 154 P.3d 443 (2007))(emphasis added).

ARGUMENT

A. **Plaintiffs' arguments and the applicable tests under the Contract Clause.**

Recognizing that the repeal of I.C. § 72-915 is fatal to their claims, plaintiffs attempt to have the repeal declared unconstitutional. Plaintiffs' Amended Complaint seeks, in relevant part, a declaration:

> That the repeal of I.C. § 72-915 by the 2009 legislature be deemed to be unconstitutional, void and of no effect as to all policies issued prior to July 1, 2009.

Id. at p. 15. The basis for such is stated to be that:

> such attempted repeal is, pursuant to Article I, Section 16 of the Idaho Constitution and Article 1, Section 10 of the United States Constitution, unconstitutional, null, void and of no effect as to contracts of insurance in existence prior to the effective date of the repeal.

Id. at p. 8.

1. Federal law is applicable in interpreting Idaho's Constitution both generally and in this case.

Notably, while plaintiffs' Amended Complaint alleges that the repeal of Idaho Code § 72-915 violates both the state and federal constitutions, plaintiffs' Motion apparently only addresses the Idaho Constitution. Plaintiffs do not make any contention that the Idaho Constitution's Contract Clause differs from the U.S. Constitution, or that it is otherwise interpreted differently.

The Idaho Supreme Court has held that "we seriously consider federal law in determining the parameters of our own constitutional provisions, and we may adopt federal precedent under the state constitution but only to the extent that we believe the federal law is not inconsistent with the protections afforded by our state constitution." State v. Guzman, 122 Idaho 981, 988, 842 P.2d 660, 667 (1992). The Idaho Supreme Court has clearly not been persuaded that federal law is inconsistent with the protections under the contract clause in the Idaho Constitution; to the contrary, the Idaho Supreme Court recently addressed a federal and state constitutional argument with a single, dispositive analysis. *See* State v. Korn, 148 Idaho 413, 224 P.3d 480, 482 (2009).

In Korn, the defendant argued that a city violated his rights under "the contract clauses found in the Idaho and U.S. constitutions." The Korn Court, without making a distinction between the two constitutions, engaged in a single analysis, relying on federal law (Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 241 (1978)) to hold that the city's ordinance did not violate his rights under either constitution. *Id.* at 483; *cf.* State v. Newman, 108 Idaho 5, 16 n.6, 696 P.2d 856, 867 n.6 (1985) (holding that while defendants sued under federal constitution and "did not also argue that the due process clause of art. 1, § 13 of Idaho's Constitution invalidates the Act in question, had they done so, we do not think that the result would have been different, for we are convinced that the rules we set down for facial challenges to the constitutionality of a statute, although derived from federal sources, are also sound and proper

under Idaho's Constitution.") Thus, whether analyzed under the Idaho Constitution or the U.S. Constitution, the analysis is the same, and the Idaho Supreme Court has not indicated it has (or will) differentiate its analysis of Idaho's Contract Clause versus that of the federal constitution.

2. The Idaho and United State's Constitutions contract clauses are not to be read literally and, therefore, a three-step analysis must be evaluated to determine whether there has been a violation of the contract clause.

The United States Constitution, Article 1, Section 10 and the Idaho Constitution, Article 1, Section 16, both provide that there shall be no "law impairing the obligations of contracts" (the "Contract Clause"). "The constitutional impairment of contracts clause protects only those contractual obligations already in existence at the time the disputed law is enacted." Lindstrom v. Dist. Bd. of Health Panhandle, 109 Idaho 956, 961, 712 P.2d 657, 662 (1985).

Plaintiffs' Motion presents a bare contention that the Idaho Constitution's Contracts Clause is a "model of categorical brevity." (Plaintiffs' Memo at 10.) Contrary to the suggestion by plaintiffs that minimal analysis of the Contract Clause is needed based upon its "categorical brevity," whether there is a violation of the Contract Clause actually requires a three-step analysis: (1) "whether the state law has, in fact, operated as a substantial impairment of a contractual relationship[;]" (2) "whether the State . . . [has] a significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem[;]" and (3) "whether the adjustment of the rights and responsibilities of contracting parties is based upon reasonable conditions and is of a character appropriate to the public purpose justifying the legislation's adoption." RUI One Corp. v. City of Berkeley, 371 F.3d 1137, 1147 (9th Cir. 2004) (internal quotations omitted).

Indeed, the U.S. Supreme Court has emphasized that the Contract Clause prohibition is not absolute:

> [The Contract Clause] prohibition is not an absolute one and is not to be read with literal exactness like a mathematical formula.
>
> ...
>
> The economic interests of the state may justify the exercise of its continuing and dominant protective power notwithstanding interference with contracts.

Home Building & Loan Association v. Blaisdell, 290 U.S. 398, 428 & 437, 54 S.Ct. 231, 236 & 239 (1934). Such position was reaffirmed in 1987 by the United States Supreme Court.

> **[I]t is well settled that the prohibition against impairing the obligation of contracts is not to be read literally.**
>
> ...
>
> [I]ts primary focus was upon legislation that was designed to repudiate or adjust pre-existing debtor-creditor relationships that obligors were unable to satisfy. Even in such cases, the Court has refused to give the Clause a literal reading. Thus, in the landmark case of *Home Building & Loan Assn. v. Blaisdell*, the Court upheld Minnesota's statutory moratorium against home foreclosures, in part, because the legislation was addressed to the "legitimate end" of protecting "a basic interest of society," and not just for the advantage of some favored group.

Keystone Bituminous Coal Ass'n v. DeBenedictis, 480 U.S. 470, 503, 107 S.Ct. 1232, 1251 (1987) (emphasis added).

A strong analysis of the modern test for whether legislation violates the Contract Clause is found in Los Quatros v. State Farm Life Ins. Co., 800 P.2d 184 (N.M. 1990), wherein the New Mexico Supreme Court applied the modern Contract Clause analysis to a claim made under the New Mexico state constitution's own Contract Clause. In Los Quatros, a mortgagor sued for declaratory judgment that a law allowing for early payment applied to its mortgage, despite the contract's language to the contrary. The mortgagee relied on Von Hoffman v. City of Quincy, 71 U.S. (4 Wall.) 535, 18 L.Ed. 403 (1866), for the proposition that states cannot constitutionally reduce a party's existing rights under a contract; however, the *Quatros* court pointed out that "much water has flowed over the dam since *Von Hoffman*, and so we prefer to apply more modern Contract Clause analysis in deciding whether or not to invalidate this statute in this case." Quatros, 800 P.2d at 192. The mortgagor relied upon Home Building & Loan

Association v. Blaisdell, *supra*, in which the Court held that "[The Contract Clause] prohibition is not an absolute one and is not to be read with literal exactness like a mathematical formula . . . . The economic interests of the state may justify the exercise of its continuing and dominant protective power notwithstanding interference with contracts." 290 U.S. at 428, 437, 54 S.Ct. at 236, 239. The Quatros court went on to explain that different Contract Clause cases had different factors present; for example, in Blaisdell, there was an emergency and the legislative relief was tailored to that emergency. 800 P.2d at 192. The Court also pointed out that in National R.R. Passenger Corp., 470 U.S. 451, 472 (1985), "the impairing statute was a federal one, and so judicial scrutiny of the legislation was minimal, which doubtless reflects a federal court's concern with principles of federalism lacking here." 800 P.2d at 192. The Quatros court found these cases to be nevertheless applicable:

> Perhaps the case providing the best overview of the appropriate methodology is *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, [459 U.S. 400 (1983)]. There the Court reviewed a Kansas statute regulating the price of natural gas sold intrastate between a producer and a public utility, and held that it was not invalid under the Contract Clause. The Court noted, first, that "[t]he threshold inquiry is 'whether the state law has, in fact, operated as a substantial impairment of a contractual relationship.'" It went on to say that "[t]he severity of the impairment is said to increase the level of scrutiny to which the legislation will be subjected," or "the height of the hurdle the state legislation must clear." In determining the extent of the impairment, it is relevant that the industry which the complaining party has entered has or has not been regulated in the past.
>
> If the answer to the threshold inquiry is that the state regulation does indeed constitute a substantial impairment, the state "must have a significant and legitimate public purpose behind the regulation," so that there is some guarantee that the state "is exercising its police power, rather than providing a benefit to special interests." Finally, once a legitimate public purpose has been identified, the reviewing court must determine "whether the adjustment of 'the rights and responsibilities of contracting parties [is based] upon reasonable conditions and [is] of a character appropriate to the public purpose justifying [the legislation's] adoption.'"

Quatros, 800 P.2d at 192 (citations omitted). The Quatros court allowed the legislation to stand, because it did not effect the underlying debt and because the banking industry is highly regulated, thus the impairment was slight. Even though the impairment was slight, the court still found it necessary to evaluate the public purpose, though it need not be too pressing; the court concluded that promoting the alienability of land was a public purpose, and that the legislation was appropriately tailored to that end. *Id.*

Thus, the RUI and Quatros decisions illuminate how the modern Contract Clause is to be applied, both with respect to analyzing the U.S. Constitution's Contract Clause and a parallel state constitutional provision. This modern analysis should also be employed in this matter.

B. The repeal of Idaho Code § 72-915 was constitutional under both the Idaho and U.S. Constitutions.

1. The Idaho Legislature has not operated a substantial impairment of a contractual relationship.

In analyzing a claim that the Contract Clause has been violated, "[t]he threshold inquiry is 'whether the state has, in fact, operated a substantial impairment of a contractual relationship.'" RUI One Corp. v. City of Berkeley, 371 F.3d at 1147; *accord,* Quatros, 800 P.2d at 192 ("[t]he threshold inquiry is 'whether the state law has, in fact, operated as a **substantial** impairment of a contractual relationship.'") (emphasis added) (quoting Energy Reserves Group, Inc. v. Kansas Power & Light Co., 459 U.S. 400 (1983)). "The threshold inquiry . . . itself has three components: 'whether there is a contractual relationship, whether a change in law impairs that contractual relationship, and whether the impairment is substantial." *Id.*

As discussed herein, plaintiffs cannot meet any of these mandatory elements.

a. ***There is no contractual right to dividends in the SIF workers' compensation policies and, therefore, plaintiffs are unable to establish the Contract Clause was violated.***

"The first sub-inquiry is not whether any contractual relationship whatsoever exists between the parties, but whether there was a 'contractual agreement regarding the specific . . . terms allegedly at issue.'" RUI One Corp. v. City of Berkeley, 371 F.3d at 1147 (emphasis added). In the present case, there is no contractual right to a dividend under a SIF workers' compensation policy. Critical to this evaluation is the fact that here, plaintiffs' dividend claim is not an express term of the insurance policy, but instead emanates from a statute written by the Legislature in exercising its authority to create a workers' compensation scheme and the SIF.

In this case, Idaho employers who purchase their worker's compensation insurance from the SIF receive a contract of insurance which sets forth the parameters of their coverage. (*See* Lojek Aff., at Exh. A.) The contract of insurance does not provide for the payment of a dividend to the policyholders – in fact nowhere does it even address dividends. In an attempt to get around the inescapable fact that dividends are not mentioned in any way, shape or form in each SIF policyholder's contract for insurance with the SIF, plaintiffs instead point to Kelso's statement that "the contract necessarily incorporates the statutory framework with both created the SIF and governs the actions that can be taken by the SIF with regard to the SIF's funds." Kelso, 134 Idaho at 138. This argument fails for several key reasons.

First, Idaho has expressly rejected the "reasonable expectations doctrine" as a means for interpreting insurance policies. *See* Purdy v. Farmers Ins. Co. of Idaho, 138 Idaho 443, 450, 65 P.3d 184, 191 (2003) (citing Ryals v. State Farm Mut. Auto. Ins. Co., 134 Idaho 302, 1 P.3d 803 (2000)); Casey v. Highlands Ins. Co., 100 Idaho 505, 600 P.2d 1387 (1979). The "reasonable expectations doctrine" is an insurance policy interpretation tool that allows for consideration of

the "reasonable expectations" of an insured as to what coverage an insurance policy affords. *See generally* Corgatelli v. Globe Life & Acc. Ins. Co., 96 Idaho 616, 619-20, 533 P.2d 737 (1975). However, as explained by the Ryals Court in rejecting the reasonable expectations doctrine:

> Ryals invites this Court to overrule precedent and adopt the doctrine of reasonable expectations. This result would preclude any further contract analysis as Ryals certainly expected to be covered while driving in New York. We decline the invitation. We have previously rejected the reasonable expectations doctrine in favor of traditional rules of contract construction. *Casey v. Highlands Ins. Co.*, 100 Idaho 505, 508-09, 600 P.2d 1387, 1390-91 (1979). The traditional rules of contract construction avoid the danger of a court creating a new contract between the parties by relying on the notion of reasonable expectations. *Casey,* 100 Idaho at 509, 600 P.2d at 1391. We find no reason to revisit that holding.

Ryals, 134 Idaho at 304.

In addition, even if the policyholders' expectations are considered, which they should not be given the state of Idaho law, the governing statutes for the SIF do not guarantee payments of dividends to policyholders, nor do they set forth that the policyholders have a property interest in the surplus or assets of the SIF. *See generally* Idaho Code § 72-901 *et seq.* In fact, the Idaho Supreme Court previously concluded the SIF's statutory framework does not create any property rights in the SIF's policyholders and no right to a dividend. Kelso, 134 Idaho at 135 ("Consequently, Kelso does not have [a] vested property interest in the assets of the SIF simply because the SIF operates much like a private mutual insurance company.").

Moreover, plaintiffs cannot paint a right to a strict pro rata dividend distribution as some variety of expected or vested contractual right that has been disrupted by retroactive application because SIF dividends have not previously been paid pro rata. Second, any change in the law created by *Farber* was promptly remedied by the Idaho legislature even before any remittitur in *Farber* issued. *See* Southwestern Bell Tel. Co. v. Public Utility Commission of Texas, 615 S.W.2d 947, 956-57 (Texas Civ. App. 1981) ("In determining whether a retroactive statute

impairs or destroys vested rights, the most important inquiries are (1) whether the public interest is advanced or retarded, (2) whether the retroactive provision gives effect to or defeats the bona fide intentions or reasonable expectations of affected persons, and (3) whether the statute surprises persons who have long relied on a contrary state of the law.").

Courts will look to whether a reasonable expectation in a particular 'right' has developed based upon past expectation; where no such expectation existed based upon contrary past practices, courts have been loath to find a reasonable expectation that is then disrupted by a change in the law. This critical legal principle is well described in the Boykin v. Boeing Co. 128 F.3d 1279 (9th Cir. 1997) and In Re Marriage of Giroux, 704 P.2d 160 (Wash.App. 1984), discussed below.

In Boykin v. Boeing Co., *supra*, the 9th Circuit addressed the question of disturbing vested rights in the context of an overtime dispute. In Boykin, the Washington State Court of Appeals had held that payment of overtime on an hourly basis defeated a claim that an employee was exempt, in a decision named Tift. 128 F.3d at 1282. In response to Tift, the Washington Legislature passed retroactive, emergency legislation to state that "[t]he payment of compensation or provision of compensatory time off in addition to a salary shall not be a factor in determining whether a person is exempted[.]" *Id.* Employees involved in litigation regarding exempt status argued, in turn, that the legislature's retroactive legislation disturbed their vested rights as emanating from Tift. *Id.* The 9th Circuit rejected this argument finding that the retroactive application of the Senate Bill did not defeat any reasonable expectation of the plaintiffs in the lawsuit:

> The employees next argue that the retroactive application of Senate Bill 6029 impairs their vested rights under the Washington Constitution. A vested right is "an immediate, fixed right of present or future enjoyment." *Gillis v. King County*, 42 Wash.2d 373, 377, 255 P.2d 546 (1953) (quotation omitted). In order for a

> vested right to be entitled to protection from legislation, it "must be something more than a mere expectation based upon an anticipated continuance of the existing law." *Washington v. Hennings*, 129 Wash.2d 512, 528, 919 P.2d 580 (1996) (quotation and citation omitted). The proper inquiry in determining the constitutionality of retroactive legislation is "whether a party has changed position in reliance upon the previous law or whether the retroactive law defeats the reasonable expectations of the parties." *Id.* at 528-29, 919 P.2d 580.
>
> The employees have not changed position in reliance upon *Tift*: As Boeing notes, at issue in this case are primarily the 1992-1994 compensation practices at Boeing; *Tift* was not announced until 1995. Further, retroactive application of Senate Bill 6029 does not defeat any reasonable expectations of the employees. The employees governed by the SPEEA collective bargaining agreement cannot claim any expectations from the terms of their contract, as it provides for overtime compensation at a rate less than time and one-half. Moreover, none of the employees had expectations, under the MWA, to overtime pay at a rate of time and one-half prior to *Tift*.

Id. at 1283.

In a Washington appellate case entitled In Re Marriage of Giroux, *supra*, the court examined whether or not a "vested right" had been disturbed following a change in military pension law. Military retirement pensions were traditionally considered community property. However, the U.S. Supreme Court ruled, in McCarty v. McCarty, 453 U.S. 210 (1981), that federal law prohibited states from dividing military pensions as community property. The Girouxes' divorce was decided under McCarty, and Rose Giroux was denied any part of her husband's pension. In response, however, Congress passed the Services Former Spouses' Protection Act, 10 U.S.C. § 1408, restoring courts' right to divide pensions as community property. Rose Giroux sued for relief from her divorce judgment. James Giroux argued that upsetting the divorce settlement by retroactive application of the Congress' change in the law would disturb his vested rights, an argument rejected by the Washington Court of Appeals because Mr. Giroux had no reasonable expectation that his military pension would not be treated as community property:

James Giroux argues that even if Congress intended the Act to be retroactive, retroactive application deprives him, without due process of law, of his vested right to the pension payments. He claims that his right to the pension vested when the amended decree became final. However, to determine the constitutionality of retroactive legislation, the proper inquiry is not whether vested rights have been interfered with, but whether "settled expectations honestly arrived at with respect to substantial interests" will be defeated. 2 C. Sands, *Statutes and Statutory Construction* § 41.05, at 261 (4th ed. 1973).

An argument similar to James Giroux's was made to this court in *In re Santore*, 28 Wash. App. 319, 623 P.2d 702 (1981). After the unintentional repeal of a statute permitting adoption by written consent of natural parents, the Legislature passed former RCW 26.32.916 with provisions for retroactivity. The Santores then sought to regain custody after having consented to the adoption of their child. They argued that the statute retroactively interfere[d] with their "vested rights," in violation of the due process and contract clauses of the federal and state constitutions, by making effective Mrs. Santore's consent to adoption, which was ineffective under the law existing when the consent was executed . . . . *In re Santore*, *supra* at 324, 623 P.2d 702. The court held:

> The proper test of the constitutionality of retroactive legislation is whether a party has changed position in reliance upon the previous law or whether the retroactive law defeats the reasonable expectations of the parties, not whether the law abrogates a "vested right," which is merely a conclusory label. Curative laws, such as RCW 26.32.916, which implement the original intentions of affected parties are constitutional because there is no injustice in retroactively depriving a person of a right that was created contrary to his expectations at the time he entered into the transaction from which the right arose.

(Citations omitted.) *In re Santore*, *supra* at 324, 623 P.2d 702.

Applying the test adopted in *Santore* to the case at bar, it is difficult to see how retroactive application of the Act would defeat the reasonable expectations of the parties. Throughout their marriage, and until the *McCarty* decision, the Girouxs could reasonably have expected that James Giroux's military pension would be treated as community property by the courts of this state. Only after the *McCarty* decision could the husband have reasonably expected to receive as his separate property what was formerly almost all of the couple's community property. Retroactive application of the Act cannot be said to be unfair or unreasonable. Recognizing the important contribution of the military spouse to our national defense, "that frequent change-of-station moves and the special pressures placed on the military spouse as a homemaker make it extremely difficult to pursue a career affording economic security, job skills and pension protection", Congress intended that the "status of the military spouse be acknowledged, supported and protected." 1982 U.S. Code Cong. and Ad. News, at 1601.

Id. at 162-63.

In the present case, the SIF policyholders could not have had a reasonable expectation that dividends would be paid on a pro rata basis because the dividend methodology – not one based on a pro rata basis – employed by the SIF has been employed for many years. (Alcorn Aff., ¶ 25.) Prior to the Farber decision, the SIF policyholders did not receive a strict pro rata share of the declared dividends. (Alcorn Aff., ¶ 25.) The Farber decision announced an interpretation of I.C. § 72-915 that the Legislature itself did not intend for the statute, as borne out by S.B. 1166a's Statement of Purpose.[6] Indeed, even before the Idaho Supreme Court's Order Denying Petition for Rehearing (May 12, 2009) and subsequent Remittitur (May 27, 2009), the repeal of Idaho Code § 72-915 was put into effect. (Counsel Aff., Exhs. C & F.) Thus, even after the Farber decision, no expectation in pro rata distribution of declared dividends could reasonably have been contemplated by SIF policyholders, given that I.C. § 72-915 was repealed even before the Idaho Supreme Court had finished with the Farber appeal. Thus, here, an SIF policyholder could have only reasonably expected to receive dividends in pro rata fashion after the Farber decision – and even then, the law was immediately changed by the Idaho legislature before the remittitur was ever issued.

Accordingly, there is no contractual right to dividends, and a legislative change to the statute governing the methodology for distribution of dividends does not implicate a term of the SIF insurance policy.

[6] It is also significant to point out that since the significant statutory amendments of 1998, the SIF has been squarely under the regulatory authority of the Department of Insurance, and is deemed, for the purposes of regulation, a mutual insurer. *See* I.C. §72-901. Since 1998, however, the SIF has never been subject to any regulatory action by the Department of Insurance as a result of its dividend practices, further demonstrating that the Farber decision offered a view of Idaho Code §72-915 that was not even shared by the State of Idaho's own insurance regulatory authority.

b. The repeal of I.C. § 72-915 was not a change in law that impaired the contractual relationship between SIF and its policyholders.

Even were the Court to determine that SIF's statutory provisions are necessarily part of each policyholders' contract for insurance with the SIF – which it should not given the above analysis – the policy expressly puts the policyholder on notice that the policy will conform with the law. The policy expressly provides:

> Terms of this insurance that conflict with the workers compensation law are changed by this statement to conform to this law.

(Lojek Aff., Exh. A, at p. 2.) Thus, an SIF policyholder is on notice from the commencement of coverage that the terms of the policy are governed by statutes, and are subject to amendment at any time by a change in the law. As such, even were the court to determine a dividend methodology may be a term of the contract by virtue of statute, that term expressly emanates from statute, and is subject to change at any time by the Legislature, which is expressly outlined in the policy. *Accord,* National R.R. Passenger Corp. v. Atchison Topeka and Santa Fe Ry. Co., 470 U.S. 451, 466, 105 S.Ct. 1441, 1451 (1985)("Policies, unlike contracts, are inherently subject to revision and repeal, and to construe laws as contracts when the obligation is not clearly and unequivocally expressed would be to limit drastically the essential powers of a legislative body."). A repeal of I.C. § 72-915 (or, more specifically, the lack of a statute mandating a particular dividend methodology), then, would be automatically incorporated into the policy, and no "impairment" would exist. Moreover, as discussed above, there is no expectation being impaired, as SIF policyholders had no expectation of a pro rata dividend under I.C. § 72-915 given it was retroactively repealed before the *Farber* case was remitted to the district court.

Thus, no impairment to any contractual right is implicated by the change in the law – rather, only at best a statutory policy term wholly subject to Legislative change.

c. The SIF policies were not "substantially impaired."

Even assuming, *arguendo*, that the right to a particular dividend methodology is a statutory provision that becomes a term of a workers' compensation contract, and that the repeal effectuated some kind of impairment, a repeal of the statute governing such methodology would not constitute a "substantial" impairment to the SIF policy, a necessary showing under a Contract Clause analysis.

"The Contracts Clause provides protection against 'substantial' impairments of the obligation of contract only. A finding of minimal alteration of contractual obligations may end the court's inquiry." 16B Am. Jur. 2d Constitutional Law § 776 (2010). Similarly,

> [I]n determining the extent of the impairment, a reviewing court may also consider "whether the industry the complaining party has entered has been regulated in the past." *Id.* For, "where a complaining party enters a contractual relationship in a heavily regulated industry, expectations of further regulation of that industry may lessen the severity of a subsequent impairment of that party's contractual rights and obligations." *Segura [v. Frank],* . . . 630 So.2d [714,] 730.

State v. All Property and Cas. Ins. Carriers Authorized and Licensed To Do Business In State, 937 So.2d 313 (La. 2006); *see also* U.S. for Use and Benefit of Midwest Steel & Iron Words Co. v. Henly, 117 F. Supp. 928, 930-31 (D. Idaho 1954) (stating that "[a]s has been stated in numerous decisions, all contracts are entered into with the understanding that the reserve power of the state to pass laws for the general welfare may be invoked at any time and therefore if the legislature in the proper exercise of that power is convinced that the public good demands that an insurance company unsuccessfully resisting payment should pay attorneys' fees, there is no constitutional objection to their doing so."); *accord* Allstate Ins. Co. v. Kim, 829 A.2d 611, 625 (Md. 2003) (holding that retroactive abolition of child-parent immunity in tort action involving motor vehicle such that insurer was required to pay on mother's behalf did not impair insurance contract, since both insurance industry and field of tort law are heavily regulated, change was "in

the wind" for some period of time, and there was no evidence of significant economic impact on Allstate or any other insurer); Hawkeye Commodity Promotions, Inc. v. Miller, 432 F.Supp.2d 822, 846-49 (Iowa 2006) (holding that statute making it illegal for retailers to offer certain gaming machines did not violate constitution because although the impairment was substantial, i.e., a total wipeout, the state had the right to terminate the contract at any time and the impairment was thus foreseeable).

In regard to workers' compensation policies issued by the SIF, the overarching purpose of such policies is not to potentially allow a fractional return on paid premiums, depending on whether the SIF Manager, in his statutorily-authorized discretion, declares a dividend. Instead, the core, fundamental function and purpose of worker's compensation coverage (which is required by Idaho law, *see generally* I.C. §§72-201 *et seq.*) is to provide coverage for covered worker injuries (and, under Part 2, additional $100,000 in coverage for employer liability, or in a greater amount as may be desired by the policyholder) to its policyholder regardless of the premium size. Thus, assuming there is a covered loss, the SIF policy provides a $300 policyholder (and any policyholder under or above that amount) with the same amount of upper coverage as a $500,000 policyholder. The repeal of I.C. § 72-915 does nothing to alter, in any way, the purpose of the workers' compensation policy; it merely grants the SIF Manager the discretion to pay declared discretionary dividends in a fashion that complies with the statutory directive that SIF be an "efficient insurance company, remain[. . .] actuarially sound and maintain[. . .] the public purposes for which the state insurance fund was created." I.C. § 72-901(3). Altering the way the SIF Manager pays out dividends to particular policyholders, then, does not constitute a "substantial" impairment to the parties' contract of insurance.[7]

[7] Indeed, even the amount declared as dividends, as a percentage of premiums, is not "substantial." For the 6 years in which dividends were declared between December 2003 and December 2008, the average dividend was only

Moreover, plaintiffs cannot demonstrate that the repeal effectuated a "substantial impairment" on the insurance polices between SIF and the policyholders based upon the limitations of their own Amended Complaint. Plaintiffs do not, and cannot, contend that their claims in this action are applicable to all policyholders paying in excess of $2,500 in premiums for the years at issue. In years where SIF elected to not distribute dividends to those policyholders below a certain paid premium level ($2,500, as was the subject of the *Farber* action), the dividends declared were, instead, redirected to policyholders of more than $2,500 in premiums – thus, certain of those larger policyholders received dividends that were larger than what their pro rata share would have been under Idaho Code § 72-915. In fact, plaintiffs' own complaint even seeks to exclude those same certain policyholders from this action:

> For some or all of the Dividend Periods falling within the Class Period, the Plaintiffs and the members of the Class purchased a worker's compensation insurance policy from the Fund, were billed annual premiums which were in excess of $2,500.00, retained each such policy for at least 6 months, and for each such Dividend Period, did not receive an amount which was equal to or greater than a *pro rata* share of the dividend distributed by the Fund.
>
> . . . .
>
> The Class shall include, for each of the Dividend Periods during the Class Period as to which a dividend was or may be distributed, all Idaho employers who: . . . (d) did not or may not, with respect to the Dividend Period in which the policy was acquired, receive a dividend which was at least equal to a *pro rata* share of the total amount of dividend being distributed[.]

Amended Complaint at ¶¶ 13 & 15.

Plaintiffs' efforts to nullify the repeal of I.C. § 72-915, then, is not predicated on the claim that all policyholders' rights were "impaired" by the repeal, but only that certain policyholders were. In fact, a nullification of the repeal - whether its retroactive application, its

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5.8582% of paid premiums, ranging from 3.9191% to 9.0304%. Counsel Aff., at Exh. E, pp. 7-8. Thus, a pro-rata share under Idaho Code § 72-915 for the dividend declared in December 2003 for a policyholder paying $10,000.00 in annual premiums would have been $391.91.

prospective application, or both – would actually adversely impact dividend payments to certain policyholders, by either potentially creating a right in SIF for recoupment of dividend overpayments, or by restricting their ability to secure a larger dividend as the SIF Manager may, in his discretion, determine is appropriate for those policyholders based upon premium level and other factors, including individual policyholders' losses.

As such, given that the repeal of I.C. § 72-915 does not impact the purpose of the SIF's workers' compensation policies in the slightest, and given that plaintiffs cannot even contend that all policyholders are impacted by the change in the law (which some policyholders will, in fact, benefit from), plaintiffs cannot demonstrate that the repeal "substantially impaired" their contracts of insurance with SIF.

2. The State has a significant and legitimate public purpose behind the repeal of I.C. § 72-915.

Even if the threshold showing – a substantial impairment of contractual relationship – is met, the Court must then inquire "whether 'the State, in justification, [has] a significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem,' to guarantee that 'the State is exercising its police power, rather than providing a benefit to special interests.'" RUI, 371 F.3d at 1147. Thus, plaintiffs must demonstrate that there lacked a legitimate public purpose behind the repeal of I.C. § 72-915.

Of course, the legitimate public purpose behind the repeal of I.C. § 72-915 is borne out by the Legislature's Statement of Purpose and Fiscal Note to S.B. 1166, as amended. (Counsel Aff., Exh. C.) There, the Legislature stated:

> Repeal of Idaho Code Section 72-915 will serve to offset an adverse decision of the Idaho Supreme Court regarding the interpretation of Idaho Code Section 72-915 which could subject the State Insurance Fund to pay dividends on policies that are not financially profitable, thereby restricting the Fund's ability to reduce

> premiums and pay dividends to profitable policyholders. The proposed repeal of Idaho Code 72-915 will clarify the law regarding the payment of dividends by the State Insurance Fund by making it clear that in passing House Bill 774aa in 1998, it was the intent of the legislature to have the State Insurance Fund operate like an efficient insurance company subject to regulation under Title 41, Idaho Code, including the dividend provision set forth in Title 41, Chapter 28, Idaho Code. Repeal of the law effective April 3, 1998 is necessary because on that date laws were enacted which subjected the State Insurance Fund to regulation under the Insurance Code, Title 41 of the Idaho Code. This legislation will allow the State Insurance Fund to issue dividends in the same manner as other insurance companies operating within the State of Idaho.

Id.[8] In turn, the repeal's Fiscal Note emphasized the financial uncertainly faced by SIF in light of the Court's ruling:

> The State of Idaho and public entities, which are insured by the State Insurance Fund, face losing all or part of their future dividends and deviations as a result of uncertainties as to the effect of a recent Supreme Court decision. Based on dividends and rate reduction deviations provided by the State Insurance Fund over the past two years, that number could exceed $5,000,000 annually. Private businesses may also, due to the same uncertainties, experience the loss of future dividends and deviations since, according to the Court's decision, the Fund has no option when distributing dividends, other than to use a pro rata formula.

Id.

The public purpose of the SIF is well-established. The SIF is a "creature of statute, . . . limited to the power and authority granted to it by the legislature." Kelso, 134 Idaho at 135. In particular, the SIF was created "for the purpose of insuring employers against liability for compensation under this worker's compensation law . . . and of securing to the persons entitled thereto the compensation provided by said laws." I.C. § 72-901(1). In structuring the SIF, the Legislature determined it should be "created as an independent body corporate politic" and derive its financial well-being from "premiums and penalties received," "property and securities

[8] Of course, even in the absence of such a legislative statement as to a particular decision by the Idaho Supreme Court: "[s]tatutes are construed under the assumption that the legislature was aware of all other statutes and legal preceden[t] at the time the statute was passed." State, ex rel. Wasden v. Maybee, 148 Idaho 520, ____, 224 P.3d 1109, 1118 (Idaho 2010)(quoting Druffel v. State, Dep't of Transp., 136 Idaho 853, 41 P.3d 739 (2002)); *accord* Smith v. Washington County, ___ Idaho ___, ___ P.3d ____, 2010 WL 3895341 (Idaho, October 6, 2010) ("We

acquired," and "of interest earned" thereon. I.C. § 72-901(1). The Board of the SIF[9] is instructed to "direct the policies and operations of the state insurance fund to assure that [it] is run as an efficient insurance company, remains actuarially sound and **maintains the public purposes for which [it] was created.**" I.C. § 72-901(3) (emphasis added). The money generated is deposited with the state treasurer, who acts as custodian for the SIF; however, "[t]he money in the fund does not belong to the state . . . [the money is held by the treasurer] . . . for the contributing employers and the beneficiaries of the compensation law, and for the payment of the costs of the operation of the fund." State ex rel. Williams v. Musgrave, 84 Idaho at 84.

Additionally, I.C. § 72-913 directs that premiums be set "at the lowest possible rate consistent with the maintenance of a solvent state insurance fund and the creation of a reasonable surplus and reserve." Public corporations are required to first attempt to insure through the SIF, unless declined as a matter of risk or if they opt to self-insure. I.C. § 72-928(a); City of Boise v. Industrial Comm'n, 129 Idaho 906, 935 P.2d 169 (1997). SIF's own stated underwriting policy requires that "It is the policy of the Idaho State Insurance Fund (ISIF) to offer insurance coverage to **all Idaho employers** who are required, by Idaho Code, to obtain workers compensation insurance on their Idaho employees and who are willing to comply with reasonable business terms and conditions," subject to limited circumstances where an employer may be cancelled, non-renewed, or refused to quote. (Alcorn Aff., Exh. A.)(emphasis added).

Further, the SIF is also statutorily required to administer workers' compensation claims for the Idaho National Guard, but is forbidden from collecting premiums or otherwise charging for such administration – in effect, serving as the Idaho National Guard's third-party

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presume that when it amended § 12-117(1), the Legislature was aware of the prevailing judicial interpretation of that statute and specifically chose to change that interpretation.").

[9] Note, again, that the SIF Board is comprised of individuals appointed by the Governor, two of whom are required to be sitting legislators. I.C. § 72-901(2).

administrator for free. I.C. § 72-928(b). Thus, it is clear that the SIF "serves a 'public purpose.'" State ex rel. Williams v. Musgrave, 84 Idaho at 85; *accord* Board of County Com'rs of Twin Falls County v. Idaho Health Facilities Authority, 96 Idaho 498, 502, 531 P.2d 588, 592 (1974) ("Thus, no entity created by the state can engage in activities that do not have primarily a public, rather than a private purpose, nor can it finance or aid any such activity.").

Moreover, the very requirement of workers' compensation is, itself, an express exercise of the police power of the State:

> DECLARATION OF POLICE POWER. The common law system governing the remedy of workmen against employers for injuries received and occupational diseases contracted in industrial and public work is inconsistent with modern industrial conditions. The welfare of the state depends upon its industries and even more upon the welfare of its wageworkers. The state of Idaho, therefore, exercising herein its police and sovereign power, declares that all phases of the premises are withdrawn from private controversy, and sure and certain relief for injured workmen and their families and dependents is hereby provided regardless of questions of fault and to the exclusion of every other remedy, proceeding or compensation, except as is otherwise provided in this act, and to that end all civil actions and civil causes of action for such personal injuries and all jurisdiction of the courts of the state over such causes are hereby abolished, except as is in this law provided.

I.C. § 72-201.

Accordingly, given the Legislature's inherent control over an entity which is purely a creature of statute and which serves a public purpose, as well as its inherent police power to involve itself in matters of workers' compensation coverage, the Legislature's exercise of legislative control over statutes governing such constitutes a legitimate public purpose. Particular as to the repeal of I.C. § 72-915, the reasons were clear: the *Farber* ruling, which conflicted with years of dividend practices by the SIF and the "intent of the legislature to have the State Insurance Fund operate like an efficient insurance company subject to regulation under Title 41, Idaho Code, including the dividend provision set forth in Title 41, Chapter 28, Idaho

Code," "could subject the State Insurance Fund to pay dividends on policies that are not financially profitable, thereby restricting the Fund's ability to reduce premiums and pay dividends to profitable policyholders." (Counsel Aff., Exh. C, Statement of Purpose.) Note, again, in that this is especially critical in light of the absence of the "safety net" for policyholders afforded by the Idaho Insurance Guaranty Association, which SIF is forbidden from being a member thereof. (Alcorn Aff., ¶15; I.C. § 72-901(4)).

Further, another financial risk in not correcting the interpretation of the Idaho Supreme Court was direct financial impact to public coffers: "[t]he State of Idaho and public entities, which are insured by the State Insurance Fund, face losing all or part of their future dividends and deviations as a result of uncertainties as to the effect of a recent Supreme Court decision. Based on dividends and rate reduction deviations provided by the State Insurance Fund over the past two years, that number could exceed $5,000,000 annually." (*Id.*, Fiscal Note.) In doing so, the Legislature made clear that its intent was to allow the SIF – the largest workers' compensation carrier in the State of Idaho – to compete with private insurers that were not under the constraints of dividend requirements defined by the *Farber* court in analyzing I.C. § 72-915 - "This legislation will allow the State Insurance Fund to issue dividends in the same manner as other insurance companies operating within the State of Idaho."[10]

Thus, even if the repeal of I.C. § 72-915 constituted a substantial impairment on the SIF policy with its policyholder, the Legislature had a legitimate public purpose behind the repeal, as demonstrated by its Statement of Purpose, Fiscal Note, its statutory authority over the SIF, and its exercise of police power in the realm of workers' compensation insurance.

[10] Certainly, in 1998, the Idaho Legislature intended to place the SIF on equal footing with private insurers: "Finally, in the 1998 amendments to the SIF's statutes, I.C. §72-901(4) was added to make it clear the SIF is subject to, and must comply with, the provisions of the Idaho insurance code. That provision also states '[f]or purposes of regulation, the state insurance fund shall be deemed to be a mutual insurer.'" Kelso, 134 Idaho at 134.

3. The adjustment of the rights and responsibilities of SIF and its policyholders, if any, is based upon reasonable conditions and is of a character appropriate to the public purpose justifying the repeal of I.C. § 72-915.

Again assuming *arguendo* that the Legislature caused a substantial impairment of a contractual right, not only are plaintiffs unable to show that the Legislature lacked a significant public purpose in repealing I.C. § 72-915, they are unable to show that any adjustment of the rights and responsibilities of the contracting parties is not based upon reasonable conditions and is not of a character appropriate to the public purpose.

The repeal of I.C. § 72-915 is a narrow repeal, only impacting a discretionary dividend that is merely incidental to the core function of plaintiffs' policies. In addition, the repeal has no impact on the express terms of the policies, and the right to a dividend has not been abolished altogether. The law has merely been changed to conform with the methodology for calculating dividends that the Manager has used for years.

Finally, any adjustment is of a character appropriate to the public purpose behind the repeal. As noted by the Legislature's Fiscal Note, the cost of reading the repeal as unconstitutional could drain upwards of $5,000,000 from the public coffers. By contrast, the Manager's current method of calculating dividends results in the SIF remaining competitive and efficient and able to offer workers' compensation coverage to Idaho employers at the lowest premium rate. In short, plaintiffs cannot show that any adjustment to the rights of the parties is not based upon reasonable conditions or inappropriate to the character of the public purpose behind the repeal.

C. **Plaintiffs' cited authority is unavailing.**

In support of plaintiffs' Motion, plaintiffs cite a handful of Idaho cases in support of their contention that the repeal of Idaho Code § 72-915 was unconstitutional under the Idaho

Constitution. Plaintiffs ultimately fail to make discussion of how these cases interact with the correct test under the Contract Clause, or that Idaho courts employ a Contract Clause analysis different from that employed by the federal courts regarding the U.S. Constitution's Contract Clause. *See, e.g.,* State v. Korn, 148 Idaho at 413 (claim made under Contract Clause of both U.S. and state constitutions; no indication that separate tests apply). Further, the issues in the cited authority have little bearing on the issue currently before the Court.

In In re Fidelity State Bank of Orofino, 35 Idaho 797, 209 P. 449 (1922), the Legislature passed a law providing that unless a district's deposit is made as a special deposit, the district has only the same priority as other depositors, changing banks' prior status as beneficiaries with vested rights. *Id.* at 451-52. Thus, the change in the legal landscape in Fidelity completely altered the material relationship of the parties, from being bailor and bailee to being creditor and debtor. *Id.* In other words, the ultimate material condition of the contract, the relationship of the parties, would have been wholly altered. By contrast, the repeal in this case has no affect whatsoever on the contractual relationship of the parties. The parties were, prior to the repeal, insured and insurer. After the repeal, they remain so. *Fidelity* is thus inapt.[11]

Penrose v. Commercial Travelers Ins. Co., 75 Idaho 524, 275 P.2d 969 (1954) is a murky decision, wherein the lead decision contains discussion of why a new statute creating attorneys' fees rights in insureds was constitutional, with three subsequent concurrences then asserting that the statute impaired existing contracts. However, the Penrose decision has been reeled in by later decisions, clarifying that retroactive legislation, even as applied to existing contracts, is not

[11] Plaintiffs, in discussing Fidelity, point to language in Von Hoffman v. City of Quincy, 71 U.S. 535, 1866 WL 9440 (1866), which is cited in Fidelity. However, as the Los Quatros court explained, the 1866 Von Hoffman decision is not "the last word on the subject": "[M]uch water has flowed over the dam since *Von Hoffman*, and so we prefer to apply more modern Contract Clause analysis in deciding whether or not to invalidate this statute in this case." 800 P.2d at 191. The Court went on to cite and discuss more recent refinements by the U.S. Supreme Court on Contract Clause analysis. *Id.* at 191-192 & n.10.

per se unconstitutional. In Eriksen v. Blue Cross of Idaho Health Services, Inc., the Idaho Court of Appeals clarified that "[b]ecause the statute shifted the balance of power between contracting parties, by identifying a favored party in the event of litigation, the Supreme Court barred its application to pre-existing contracts." 116 Idaho 693, 696, 778 P.2d 815, 818 (Ct. App. 1989). Thus, the Eriksen Court narrowed Penrose to scenarios where a statutory change would "affected bargaining relationships by designating favored parties," characterizing the Penrose decision as resting upon a "policy rationale." *Id.* This explanation by the Idaho Court of Appeals was later confirmed by the Idaho Supreme Court in Bott v. Idaho State Bldg. Authority, 122 Idaho 471, 835 P.2d 1282 (1992). As discussed above, however, the repeal of Idaho Code § 72-915 did not impact the "bargaining relationships" between the parties, but rather maintained the status quo of dividend practices in accord with the Idaho Legislature's intent. Further, the policy needs of the repeal of Idaho Code § 72-915, outlined above, were not at issue in Penrose and, applied here, demonstrate that the repeal complies with the Contract Clause. Tellingly, this later discussion of Penrose by the Idaho appellate courts is not cited by plaintiffs.

Agricultural Products Corp. v. Utah Power & Light Co., 98 Idaho 23, 557 P.2d 617 (1976) is another decision cited by plaintiffs, but for which actually supports SIF's position. In that case, the Court held that:

> Contracts of any sort are protected by the Idaho Constitution, which provides in Article I, s 16 that no 'law impairing the obligation of contracts shall ever be passed.' Any contract is thus assured some measure of protection from governmental interference. In determining the status of public utility contracts, and the ability of the Public Utilities Commission to alter the terms of such contracts, it is important to remember the special protected status given any contract by the constitution.
>
> **On the other hand, the state has a well established right to regulate public utilities.** This court held in Sandpoint Water and Light Co., Ltd., v. City of Sandpoint, 31 Idaho 498, 173 P. 972 (1918):

> 'It is held uniformly and universally that the power to supervise and regulate rates or charges for services rendered by public utilities is an inherent function of government, and occupies a large place within the domain of the police powers of the state.' 31 Idaho 498, 501, 173 P. 972, 973.
>
> **Pursuant to that power, it has been settled that the state may fix rates for a public utility service which will supersede rates previously fixed by private contract.** Interference with private contracts by the state regulation of rates is a valid exercise of the police power, and such regulation is not a violation of the constitutional prohibition against impairment of contractual obligations. A Public Utility Commission may thus annul or supersede contract rates between utilities and their customers. **Private contracts with utilities are regarded as entered into subject to reserved authority of the state to modify the contract in the public interest.**

Id. at 29, 557 P.2d at 622-623 (citations omitted)(emphases added). Again, the Legislature's judgment that the repeal was necessary to the vitality of ISIF is conclusive in this matter, and given the significant and important public realm that the workers' compensation scheme and State Insurance Fund operate within (as discussed above), plaintiffs' absolutist view of the Contract Clause is simply not borne out.

Similar to the question posed in Agricultural Products, the Idaho Court of Appeals mulled the question of whether ordinances could impose fees upon existing franchises in the later decision of City of Hayden v. Washington Water Power Co., 108 Idaho 467, 700 P.2d 89 (Ct. App. 1985). There, while rejecting the particular fees at issue, the Court took pains to indicate that the State had the authority to act pursuant to its police power, even if it impacted existing contracts: "We do not suggest, of course, that a municipality never may impose new burdens upon an existing franchise grantee. A city has the inherent right to enact valid police power regulations, even if contracts are thereby affected." *Id.* at 469. Thus, the police power exception to the constitutional proscription against impairing contracts could be considered to those acts "promoting the health, comfort, safety and general welfare of society." *Id.* In the present case, as discussed above, the Statement of Purpose in the repeal of Idaho Code § 72-915 emphasized

that the repeal was need to accurately reflect the "intent of the legislature to have the State Insurance Fund operate like an efficient insurance company" in fulfilling its public purpose under Idaho's workers' compensation scheme (itself a creature of an exercise of the state's police power).

The decision in Steward v. Nelson, 54 Idaho 437, 32 P.2d 843 (1934) can be categorized as an "easy" Contract Clause case. In that case, the Idaho legislature passed two statutes which attempted to limit the amount of time in which a mortgage could be foreclosed, irrespective of the life of the debt that the mortgage was securing. The effect, then, was to deprive the plaintiff mortgage-holders of the right to foreclose on the mortgages after a certain period of time. The Court readily found that the law effectively obliterated the intent of the mortgages. 32 P.2d at 845 & 847. Thus, the crux of the case really turns on the question of whether a 'substantial' impairment of the contracts occurred – which, as explained by the Steward court, can be safely answered in the affirmative. In the present case, however, as discussed above, there has been no 'substantial' impairment by virtue of the repeal of Idaho Code § 72-915.

Tanner v. Shearmire, 115 Idaho 1060, 772 P.2d 267 (Ct. App. 1989) and Curtis v. Firth, 123 Idaho 598, 850 P.2d 749 (1993), both related to the rights of beneficiaries seeking to sue a grantor/successor on a trust deed. The Tanner and Curtis decisions, like Steward, present comparatively 'easy' Contract Clause questions. In both cases, the Court considered the remedies available to note-holders at the time they entered into a note: that remedy would, as the law stood, naturally include the right to sue on the note. The effect of the amendment, however, was to effectively strip the right to act on the note, requiring note-holders to seek foreclosure as a primary recovery mechanism instead. Such a change would obviously be a 'substantial' impairment of the note, as the note-holders would largely be left with a right without a remedy

(or, at least, a heavily-impaired remedy). Further, Tanner and Curtis lack any discussion of the remaining two parts of the consideration governing an alleged Contract Clause, as did Steward. Thus, these string of cases – Steward, Tanner, and Curtis - represent 'easy' Contract Clause cases where the Legislature attempted to impair existing notes and mortgages between private parties by stripping down the remedies to act on such. This scenario is wholly inapposite to the present case, where the impairment (if any at all) is not substantial, and otherwise is a narrowly-tailored change for a "significant and legitimate public purpose."

Curr v. Curr, 124 Idaho 686, 864 P.2d 132 (1993), actually involves administrative action, rather than legislative action. In that case, the Idaho Supreme Court reviewed the authority of the Idaho Industrial Commission to cap attorneys fees at 25% via a "letter of understanding." The Court's primary basis for rejection was the IIC's failure to abide by the APA. *Id.* at 691. However, the Court did not take the absolutist view that because the 'letter of understanding' impaired fee agreements, it was *per se* unconstitutional; rather, the Court focused on the IIC's lack of procedure in promulgating the 'letter of understanding': "In order to **justifiably modify attorney fee agreements in the interest of public welfare**, the Commission must afford due process to the contracting parties, i.e., notice and an opportunity to be heard at a meaningful time." *Id.* (emphasis added). Thus, the Court's gripe was ultimately not with the right to modify the agreements, but the procedure in which it was done. Thus, Curr's focus on an improper administrative action offers no guidance in this matter.[12]

[12] In the present case, of course, the repeal proceeded through the Legislature and was passed as a public law. Indeed, during the course of drafting the legislation, the bill was taken up at hearing in the Senate Commerce and Human Resources Committee on April 7 and April 14, 2009. *See* Affidavit of Counsel in Opposition to Plaintiffs' Motion for Partial Summary Judgment, Exhibits A and B. Notably, at the April 7, 2009 hearing on the bill, plaintiffs' counsel in this action – Mr. Gordon and Mr. Lojek – specifically provided testimony in opposition to the bill. *Id.* at Exh. A, at pp. 3-4.

Accordingly, the case law offered by plaintiffs in support of their motion for summary judgment either fails to reflect the modern, refined interpretation of the Contract Clause and its three-step analysis, or otherwise illustrates 'easy' Contract Clause cases (that is, very substantial impairments of contracts with no justified public purpose). However, as discussed in sections above, application of the three-part test to the case at bar more than amply demonstrates that the Legislative repeal of Idaho Code § 72-915 was constitutional, both under the Idaho and U.S. Constitutions.

CONCLUSION

For the reasons stated above, plaintiffs' Motion for Partial Summary Judgment should be denied.

DATED this 22nd day of November, 2010.

HALL, FARLEY, OBERRECHT
& BLANTON, P.A.

By _____
Richard E. Hall - Of the Firm
Keely E. Duke - Of the Firm
Attorneys for Defendants

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 22nd day of November, 2010, I caused to be served a true copy of the foregoing document, by the method indicated below, and addressed to each of the following:

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Attorneys for Defendants

IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT OF THE STATE OF IDAHO, IN AND FOR THE COUNTY OF CANYON

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE, LLC OF SALMON,

Plaintiffs,

vs.

THE IDAHO STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its Manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN and MAX BLACK and STEVE LANDON, in their capacity as members of the Board of Directors of the State Insurance Fund,

Defendants.

Case No. CV 09-13607-C

DEFENDANTS' NOTICE OF ERRATA RE: PENDING MOTIONS

Defendants The Idaho State Insurance Fund, James M. Alcorn in his official capacity as its Manager, and William Deal, Wayne Meyer, Gerald Geddes, John Goedde, Elaine Martin, Mark Snodgrass, Rodney A. Higgins, Terry Gestrin, Max Black, and Steve Landon in their

capacity as members of the Board of Directors of the State Insurance Fund (collectively, "SIF"), by and through their counsel of record Hall, Farley, Oberrecht & Blanton, P.A., hereby notify the Court and all parties of the following errata in SIF's briefing on motions to be heard on December 15, 2010, in lieu of filing amended memoranda:

1. Undisputed Material Fact #5 states[1] that "Plaintiffs' action was not filed until December 24, 2010." This statement should correctly read: "Plaintiffs' action was not filed until December 24, 2009."

2. Reply in Support of Defendants' Motion for Summary Judgment, Dec. 6, 2010, at p. 14 – citation to *Energy Reserves Group, Inc. v. Kansas Power and Light Co.*, 459 Idaho 400, 411, 103 S.Ct. 697, 704 (1983) should correctly read *Energy Reserves Group, Inc. v. Kansas Power and Light Co.*, 459 U.S. 400, 411, 103 S.Ct. 697, 704 (1983).

DATED this 8th day of December, 2010.

HALL, FARLEY, OBERRECHT
& BLANTON, P.A.

By #6432
Richard E. Hall - Of the Firm
Keely E. Duke - Of the Firm
Attorneys for Defendants

[1] As reflected in: 1) Opposition to Plaintiffs' Motion for Partial Summary Judgment, Nov. 22, 2010, at p. 7; 2) Reply in Support of Defendants' Motion for Summary Judgment, Dec. 6, 2010, at p. 4; 3) Opposition to Plaintiffs' Motion to Strike, Dec. 3, 2010, at p. 12; and 4) Opposition to Plaintiffs' Motion, Pursuant to 56(f), Dec. 3, 2010, at p. 9.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 8th day of December, 2010, I caused to be served a true copy of the foregoing document, by the method indicated below, and addressed to each of the following:

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IN THE DISTRICT COURT OF THE THIRD JUDICIAL DISTRICT OF THE STATE OF IDAHO, IN AND FOR THE COUNTY OF CANYON

CDA DAIRY QUEEN, INC., and DISCOVERY CARE CENTRE LLC OF SALMON,
Plaintiffs,

vs.

THE IDAHO STATE INSURANCE FUND, JAMES M. ALCORN, in his official capacity as its Manager, and WILLIAM DEAL, WAYNE MEYER, GERALD GEDDES, JOHN GOEDDE, ELAINE MARTIN, MARK SNODGRASS, RODNEY A. HIGGINS, TERRY GESTRIN AND MAX BLACK AND STEVE LANDON in their capacity as member's of the Board of Directors of the State Insurance Fund,
Defendants.

CASE NO. CV 09-13607-C

MOTION TO STRIKE THE AFFIDAVIT OF JAMES M. ALCORN AND SELECTED EXHIBITS ATTACHED TO THE AFFIDAVIT OF COUNSEL BOTH OF WHICH WERE FILED IN SUPPORT OF DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

COME NOW THE PLAINTIFFS, by and through undersigned counsel, and hereby move this Court for its Order, granting the *Motion to Strike the Affidavit of James M. Alcorn and Selected Exhibits Attached to the Affidavit of Counsel Both of Which Were Filed in Support of Defendants' Motion for Summary Judgment*. This Motion is made on the grounds and for the reasons that as more fully set forth in the *Memorandum In Support Motion to Strike the Affidavit of James M. Alcorn and Selected Exhibits Attached to the Affidavit of Counsel Both of Which Were Filed in Support of Defendants' Motion for Summary Judgment* filed herewith:

1. Exhibits A, B, D, E as attached to the Affidavit of Counsel are not admissible either or both because they are irrelevant to the resolution of the issues identified in the proceedings before the Court or they are testimonial in nature and the declarant is not properly sworn. Being inadmissible, they have, pursuant to I.R.C.P. Rule 56(e) no role in this summary judgment proceeding.

2. The Affidavit of James M. Alcorn contains no information as individual or aggregated paragraphs which is relevant to the resolution of the issues identified in the proceedings before the Court and is therefor inadmissible and not pursuant to I.R.C.P. Rule 56(e) a properly filed affidavit in this summary judgment proceeding.

ORAL ARGUMENT IS REQUESTED.

DATED this 17th day of November, 2010

Bruce S. Bistline

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 17th day of November, 2010, a true and correct copy of the foregoing instrument was served on the following by the method indicated below, and addressed as follows:

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