10-17-2011

CDA Dairy Queen, Inc. v. State Ins. Fund Appellant's Reply Brief Dckt. 38492

IN THE SUPREME COURT OF THE STATE OF IDAHO

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

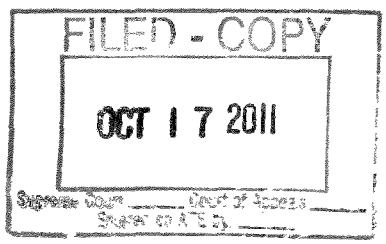
Plaintiffs-Appellants,

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-Respondents.

DOCKET NUMBER: 38492



APPELLANTS' REPLY BRIEF

Appeal from the District Court of the Third Judicial District of Canyon County

Honorable Renae Hoff
District Judge, Presiding

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I. INTRODUCTION

Relying upon a string of Idaho cases beginning with a 1922 decision, Dairy Queen has demonstrated that the retroactivity provision (*SB1166aa(3)*) in the enactment repealing I.C. § 72-915 (*SB 1166aa*) is an unconstitutional impairment of the obligations of contracts formed more than 180 days prior to its effective date. These cases articulate an approach (hereinafter the "Idaho approach") for resolving actions asserting that a statute impairs a contract and impermissibly deprives one of the contracting parties of the protections afforded by Art. I §16 of the Idaho Constitution (hereinafter the "Idaho Contracts Clause"). SIF has neither demonstrated that Dairy Queen is misreading these cases, nor has SIF cited a single relevant Idaho case which reaches a contrary conclusion.

SIF has argued for the utilization of a different approach, one which has never before been used in Idaho in a similar case. SIF misidentifies this as the "modern approach" but this approach is neither modern nor, given the uniqueness of Idaho, the language of the Idaho Constitution, and the long-standing precedent for determining contracts clause challenges, is it better. SIF's proposed approach (hereinafter the "Federal approach") provides less protection to contracts than is provided by the long-standing Idaho approach. It has been employed by federal courts since at least 1938 to address claims based upon Art. 1 § 10 of the United States Constitution (hereinafter the "Federal Contracts Clause"). SIF urges reliance upon this "Federal approach" despite the fact that this Court is free to rule and clearly has ruled that the Idaho Contracts Clause affords greater protection to Idaho contracts than might be afforded to them by the Federal Contracts Clause.

SIF makes a lukewarm attempt to argue that, utilizing the well established Idaho approach, SB 1166aa(3) does not offend the Idaho Contracts Clause. This attempt is premised upon the erroneous assertion that SB1166aa(3) neither materially impairs a term of Dairy Queen's contract with SIF nor works to impair any vested rights.

While nothing in the long-standing Idaho jurisprudence provides any reason for deferring to the less protective Federal approach to contracts clause challenges, Dairy Queen will demonstrate that even if this approach is employed the result is the same – SB 1166aa(3) is unconstitutional.

Because it is pointless to do so, Dairy Queen has not and will not separately address the District Court's determination that SB1166aa(3) does not offend the Federal Contracts Clause. Whether the Idaho approach or the Federal approach is used, the result is the same: the Idaho Constitution has been violated. There is no need to examine the Federal Contracts Clause.

II. ARGUMENT

A. SB 1166(3) MATERIALLY IMPAIRS THE CONTRACTS AT ISSUE AND IS PRECLUDED BY THIS COURTS LONG-STANDING INTERPRETATION OF ARTICLE 1 §16 OF THE IDAHO CONSTITUTION.

With narrow exceptions which are irrelevant to this action, this Court has consistently employed the principle that, with respect to contracts similar to those involved in this matter, legislation that attempts to make material alterations in the character, terms or legal effect of existing contracts is clearly void. *Fidelity State Bank v. North Fork Highway Dist.,*35 Idaho 797, 810, 209 P. 449, 452 (1922). A material alteration is one which alters an existing contract term "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." *Supra,* 35 Idaho at

813, 209 P. 453. The "terms" of the contract which may not be impaired include the law existing when the contract is formed and a change in that law which "denies or obstructs any rights accruing under the contracts" impairs the obligation of contract and violates the Idaho Contracts Clause. *Curtis v. Firth,* 123 Idaho 598, 610, 850 P.2d 740, 761 (1993).

In the Appellants' Brief, Dairy Queen demonstrated that the Idaho approach compels the conclusion that SB 1166aa(3) is, unconstitutional. This conclusion is supported by three key facts: 1) there were contracts between Dairy Queen and SIF formed prior to the enactment of SB 1166aa; 2) the contracts provided that time-qualified policyholders acquired a right to receive a *pro rata* share of any amount distributed as a rate readjustment; and, 3) this acquired right was a material and vested contract right, and, once the Manager determined that there were funds to be distributed as rate readjustments, a right with a determinable value. Based upon these facts, SB 1166aa(3) cannot be seen as constitutionally permissible.

1. Contracts between SIF and Dairy Queen existed prior to the effective date of the enactment.

While the parties do not agree upon much, they appear to agree that it is not necessary to engage in any evaluation of whether a legislative action impermissibly impairs a contract unless a contract in fact exists. This foundational requirement is axiomatic. And, in fact, this Court has specifically reached this conclusion. *See State v. Korn*, 148 Idaho 413, 415-416, 224 P.3d 480, 482-483 (2009). SIF and Dairy Queen also appear to agree that a contract exists between them.

2. For each year of the class period the contract between SIF and Dairy Queen which included the requirement that any rate readjustment be distributed upon a *pro rata* basis among time-qualified policyholders.

In an effort to generate a dispute over whether the contract between SIF and its

policyholders includes a right to receive a *pro rata* share of an amount which the Manager decides to distribute as rate readjustments, SIF invites this Court into a blind alley. [1]

SIF contends in this regard that Plaintiffs' right to receive a *pro rata* share of any funds distributed as rate readjustments is not addressed anywhere within the four corners of the printed policy issued to Dairy Queen by SIF. (R:4 to 79 (herein the *"policy"*)) . SIF then argues that the right to a *pro rata* share of any rate readjustments is not a "term of the insurance policy." SIF concludes "no provision of the SIF *policies* is impacted by the repeal of I.C. § 72-915." Respondents' Brief p. 9 (herein "R.B.")(emphasis added). SIF then shifts to using *policy* and *contract* as if they are interchangeable terms.

There is more to the *contract* between SIF and Dairy Queen than is set out in the *policy*.[2] The *policy* is but a part of the *contract*. The *contract* also includes, by incorporation, the relevant statutes of this state along with all of the express or implied agreements between the parties relative to subject matter and consideration. *State v. Korn, supra,* 148 Idaho at 415, 234 P. at 482. *Policy* and *contract* are not synonymous.

Any assertion that the provisions of I.C. § 72-915 are not actually part of the contract between SIF and its insureds is completely foreclosed by long-standing precedent.[3] Specific to

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[1] SIF arguments that are addressed here appear in Respondent's Brief at pages 9-10 and 20.

[2] This refusal is perplexing given that Mr. Hall (counsel of record in this action) advised the members of the Senate Commerce and Human Resources Committee that " the Supreme Court did rule in *Kelso & Irwin v. State Insurance Fund* that Worker's Compensation statutes became part of the contract of insurance between the State Insurance Fund and the policyholder." R:188.

[3] This Court has repeatedly held that relevant statutes in force at the time that a contract is formed are incorporated into the contract. *see, e.g. Kelso & Irwin, P.A. v. State Insurance Fund,*

the statute at issue in this matter, this Court has held that SIF "has duties to its policyholders regarding ... dividends by virtue of the ... statutes that are incorporated in the policyholders' contracts." *Hayden Lake Fire Protection Dist. v. Alcorn,* 141 Idaho 388, 399, 111 P.3d 73, 84 (2005). Moreover, this Court, despite being presented with this identical argument by SIF, enforced I.C. § 72-915 as a *contractual* right without discussing incorporation yet one more time. *See Farber, et al. v. Idaho State Insurance Fund, et al.,* 147 Idaho 307, 208 P.3d 289 (2009).

SIF suggests that even if I.C. § 72-915 is incorporated into its contracts, the contracts provide for reformation in the event of changes in the "workers compensation law." (R.B., p.22, n. 8.) This language cannot cure a constitutional defect. It is irrelevant because I.C. §72-915 is not part of the "workers compensation law." *See I. C. § 72-101 (1), and Statutory Notes to I.C. 72-101.*[4] Moreover, for this type of language in a contract or a statute to be treated as authorizing a retroactive change of the contract, the intent to allow for such changes must be explicitly stated. *see, e.g. Caritas Servs. Inc. v. The Dep't of Social & Health, supra.* (1994).

These conclusions are obvious: 1) there was a contract between Plaintiffs and SIF for

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134 Idaho 130, 138, 997 P.2d 591, 599 (2000) and *Steward v. Nelson*, 54 Idaho 437, 441, 32 P.2d 843, 845 (1934). *See.also. Home Bldg. & Loan Ass'n v. Blaisdell et. al.*, 290 U.S. 398, 429-430 (1934) and *Caritas Servs. Inc. v. The Dep't of Social & Health,* 123 Wn.2d 391, 406-407, 869 P.2d 28, 31 (1994)(A contractual right to specific reimbursement is not different from a statutory right to specific reimbursement where the statute is incorporated by reference into the contract. "There is therefore no difference between mere "statutory rights" to reimbursement and contract rights to reimbursement.").

[4] In 1971 the Legislature engaged in a "comprehensive recodification of the workmen's compensation law and occupational disease law of the state of Idaho." As part of that process it repealed Chapters 1, 2,3,4,5,6,7,8,10,11 and 12 of Title72. Clearly, while the creation of the State Insurance Fund was part of the process of adopting a Worker's Compensation system, the statutes establishing and regulating the Fund are not themselves part of the Workers's Compensation law.

each year during the class period; 2) a term of that contract was a requirement for a *pro rata* distribution of any amounts that the Manager elected to distribute as rate readjustments; 3) the failure to observe that contractual right was a breach of contract which leads to this action.

3. SB 1166aa(3) vitiates a term of thousands of contracts and the change impermissibly impairs a vested right under those contracts.

As to all policies held more than 180 days prior to the effective date of SB 1166aa, the policyholder had an unchallengeable and protected contract right to receive a *pro rata* share of any amount that might later be distributed as a rate readjustment. *Farber.* In Idaho, such a right is a protected property right. *Curr v. Curr, 124 Idaho 686, 691: 864 P.2d 132, 138 (1993).* When, in every year relevant to this action, the Manager elected to distribute an amount as rate readjustments, each policyholder automatically acquired by virtue of the mandatory language of I.C. § 72-915, a right to receive a *pro rata* share of the amount distributed. *Farber.* Where mandatory statutory language which affords an automatic right to receive property is associated with a commercial transaction, the right is equivalent to a vested property right. *Griggs v. Nash* 116 Idaho 228, 235, 775 P.2d 120, 127 (1989).

SB 1166aa(3) impairs a right of Dairy Queen's contract with SIF by depriving Dairy Queen of vested property rights and by taking away its breach of contract claims. SIF attempts to avoid this conclusion by claiming that the contractual language provided by I.C. § 72-915 provides no "guarantee" of the payment of rate readjustments. (R.B., p.10.) As to those years in which the manager made the discretionary decision to distribute funds as a rate readjustment, this argument is foreclosed by this Court's decision in *Farber*.

Ignoring *Farber,* SIF erroneously relies upon language from *Kelso, supra,* relative to the

absence of vested rights. The holding in *Kelso* has no bearing here. In *Kelso* the plaintiff claimed that because SIF had adequate reserves and surpluses some amount was vested in the policyholders and *had* to be distributed as a rate readjustment. This Court concluded that the decision of *whether to distribute* rate readjustments was a discretionary and until that decison was made, the policyholders had no vested property interest in the funds held by SIF.

Here, in each year within the Class Period, the Manager had already made the discretionary determination to distribute rate readjustments. Once this happened, the clear language of I.C. § 72-915 mandated *how to distribute* those rate readjustments. *Farber*, 147 Idaho at 312, 208 P.3d at 294. Thus, the decision to distribute gives rise to a guaranteed and vested right to receive a *pro rata* share of any amount distributed as rate readjustments.

Clearly, once the decision was made to distribute a rate readjustment the contractual right to receive a *pro rata* share of any rate readjustment became a vested and protected property right.

4. Based upon long-standing Idaho Law, to the extent it is given retroactive application SB 1166aa(3) violates the protections afforded to Idaho citizens and businesses by Art. I § 16 of the Idaho Constitution.

SIF employs four tactics in its effort to obfuscate the clear holdings of a long line of Idaho cases which demonstrate that, with respect to the types of contracts which are involved in this case, the Idaho Contracts Clause has historically been applied in an strict manner as to invalidate enactments which seek to materially impair a term of a contract.

First, SIF argues that these cases have been overruled by the by this Court in *State v. Korn, supra.* This reading of *Korn* is absurd. *Korn* was resolved on the threshold determination that the evidence did not demonstrate that a contract had been formed prior to the passage of the

challenged enactment. While a federal case was cited in support of principle that only contracts existing prior to an enactment are protected the Court could have cited *In Re Fidelity State Bank, supra,* 35 Idaho 811, 209 P.452. As no protected contract existed there was no discussion regarding the analytical approach applicable to challenges premised upon the Idaho Contracts Clause. *Korn* certainly does not explicitly or implicitly overrule or abandon the Idaho approach.

Second, SIF attempts to divert the discussion by pointing to cases which are wholly irrelevant in this matter. There are two types of contracts (public utilities contracts and agreements relative to fees in worker's compensation matters) which are regulated to such an extent that the price term is, by statute, subject to retroactive adjustments. (public utilities -- I.C. § 61-641, workers compensation I.C. § 72-803). No such degree of regulation is present with respect to the contracts at issue in this case. While I.C. § 72-915 bears upon the price term of the contracts formed by SIF, nothing in the language of I.C. § 72-915, nor any other statute, discloses to Idaho citizens that this price term is subject to retroactive regulation or change.

The core differences between the circumstances underlying the formation of the contracts at issue in this case and those underlying public utilities contracts are illuminated in the cases cited by SIF. *Agric. Prod. Corp. v. Utah Power & Light Co.*, 98 Idaho 23, 557 P.2d 617 (1976) and *City of Hayden v. Washington Water Power Co.,* 108 Idaho 467, 700 P.2d 89 (Ct. App. 1985). First, both these cases involved governmental action which *prospectively* adjusted the price term of an existing contract. Neither case suggests that similar analysis would be acceptable if governmental action caused a retroactive modification of a contract.[5] Second, in

[5] Indeed Dairy Queen has been unable to find any Idaho decision in which even a public utilities contract was retroactively modified to change the rates as to services already provided.

both cases the Court determined that, due to the nature and extent of utilities regulation (authority to operate a monopoly enterprise conditioned upon regulation and rate control), the terms agreed upon by the parties to a utilities contract may lawfully be changed by governmental action. As such, these cases pertaining to public utilities contracts cannot be read as overruling the long line of Idaho cases which have consistently held to protect the types of contracts involved in this matter.

Similarly, *Curr v. Curr,* 124 Idaho 686, 864 P.2d 132 (1993) has no bearing upon the analysis that should be employed in evaluating the claims at issue in this matter. At issue in *Curr* were attorney fee agreements which were formed with the full knowledge of and implied acquiescence to the statutory power of the Industrial Commission to regulate fees. The cases consolidated in *Curr* were fully resolved on a variety of due process grounds. The Commission was found to have overstepped its authority to regulate attorney fees by doing so without any properly promulgated regulations. The Federal Contracts Clause is referenced only as a constitutional acknowledgment that an executed contract gives rise to a protected property right. The Court engaged in absolutely no discussion relative to the correct analysis for determining if any enactment or regulation was prohibited by either the Federal or the Idaho Contracts Clause. As with the public utilities related cases, the contracts in *Curr* are distinguished from the contracts at issue because of the fact that Dairy Queen did not enter into any contract with any notice that the government had retained the power to retroactively change the price term of any contract.

Third, SIF misplaces reliance upon a few of the cases which address the question of whether statutes engrafting attorney fee recovery provisions onto contracts which existed prior to

the passage of the statute can be applied to suits based upon those contracts. The seminal case in this area and the only one that involves any discussion of the analytical process to be utilized in determining if an enactment impairs a contract is *Penrose v. Commercial Traveler's Insurance Co.*, 75 Idaho 524, 275 P.2d 969 (1954). In that case this Court considered an Idaho Contracts Clause challenge to a statute which only a few months earlier had been held by a federal judge not to offend the Federal Contacts Clause. *United States for the Benefit of Midwest Steel & Iron Works v. Henly*, 117 F. Supp. 928 (1954). With full awareness, supplied by the dissenting Justices, that federal courts might give limited deference to exercises of police power this Court held that a one-sided mandatory attorney fee statutes could not constitutionally be superimposed upon contracts in existence prior to the passage of the statute.

The balance of the cases identified by SIF involved fee statutes which were either party-neutral and/or discretionary. Fee statutes which are party-neutral and discretionary, have consistently been treated as procedural/remedial in nature and applicable without regard to when the contract at issue was formed. *See, e.g. Jensen v. Shank*, 99 Idaho 565, 585 P.2d 1276 (1978). These holdings turn upon the proposition that matters which are procedural in nature do not impair vested rights. *See, e.g., State v. Daicell Chem. Indus., Ltd.* 141 Idaho 102, 105, 106 P.3d 428, 431 (2005). Where a fee statute is party-neutral but mandatory, this Court has found these provisions are substantive in nature. Instead of treating them as impairments of the existing contract, the Court has held they may only be applied in actions filed after the statutes in question became effective. *Griggs v. Nash,* 116 Idaho 228, 775 P.2d 120 (1989).

SIF suggests that these decisions dealing with attorney fees statutes manifest the Court's intention to abandon the long-established Idaho approach to Contracts Clause cases and,

notwithstanding its prior rejection of the federal approach, to begin giving limited deference to exercise of the police power as to a wide range of contract terms.. Other than *Penrose,* none of these cases involve any Contracts Clause analysis. When these cases are read for what they do address, it is apparent that where fee statutes do not designate a favored party or materially change the core elements of the contract and they are not seen as impairing the relevant contract. *See, e.g. Bott v. Idaho State Bldg. Authority,* 122 Idaho 471, 481, 835 P.2d 1282, 1292 (1992).

SB 1166aa(3) can satisfy none of the criteria that would qualify it for "procedural matter" treatment. The measure is not party-neutral. If allowed, SB 1166aa(3) will absolve SIF of responsibility for breaching its contracts with its policyholders. Instead of distributing available funds on a *pro rata* basis among all policyholders, SIF gave the money to those who SIF considered to be favored policyholders –many of which appear to have been State agencies. On the other hand, Dairy Queen is both denied money which is due and deprived of its right to enforce its contracts with SIF. SB 1166aa(3) is anything but party-neutral.

Fourth, lacking any relevant Idaho authority which contradicts the clear Idaho rule rendering any "legislation that attempts to make material alterations in the character, terms or legal effect of existing contracts...clearly void" *Fidelity, supra*, 35 Idaho at 810, 209 P. 452, (emphasis added), SIF turns to other jurisdictions. SIF relies upon an out-of-context snippet lifted from *Keystone Bituminous Coal Ass'n v. DeBenedictis,* 480 U.S. 470 (1987). Considered in context, the language clearly has no relevance. The Court's statements pertained only to the Federal Contracts Clause. The Court made no effort to evaluate Idaho jurisprudence or to consider whether the Idaho Contracts Clause had been applied to afford greater protection to Idaho citizens.

SIF also looks to Washington decisions on the basis that the Washington Contracts Clause is nearly identical to the Idaho Contracts Clause. While this is true, the analytical path followed by the Washington Courts has long differed from the one taken by this Court. Since at least 1916, the Washington Supreme Court has, in dealing with Contracts Clause challenges, considered whether the enactment at issue involved a reasonable exercise of the police power of the State. *See, State ex rel. Olympia v. Olympia Light & Power Co.*, 91 Wash. 519, 158 P. 85 (1916). Since its decision in *Fidelity* (1922) this Court has continued to find legislation void if it makes material alterations in the character, terms or legal effect of existing contracts and no exception has been made for purported police power justifications.

In sum, SIF fails in all of its efforts to refute Dairy Queen's assertion that under the Idaho approach, as articulated by this Court in decisions spanning nearly 90 years, SB 1166aa(3) is plainly unconstitutional because it acts retroactively.

B. FEDERAL DECISIONAL LAW IS COMPLETELY IRRELEVANT TO THE RESOLUTION OF THIS MATTER.

Federal decisional law is completely irrelevant to the resolution of this matter.[6] Federal decisional law is not entitled to *any* consideration, let alone serious consideration, where the principles espoused in those federal decisions are inconsistent with the protections afforded by

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[6] The SIF erroneously asserts that Dairy Queen's claim would be "eviscerated" by the application of the Federal Approach. This assertion is really little more than self-serving grandstanding. Dairy Queen's position is a matter of economy. If Dairy Queen is right there is no need for the parties and the Court to deal with briefing regarding the resolution of this matter based upon the Federal approach. Dairy Queen, will, given that these arguments have now been raised by the SIF, proceed in this memorandum to demonstrate that it prevails even if it is appropriate to utilize the Federal approach.

the Idaho Constitution. *State v. Guzman,* 122 Idaho 981, 988, 842 P.2d 660, 667 (1992). While it may be appropriate in certain cases to employ the interpretation and methodology utilized by federal courts in evaluating constitutional challenges, Idaho does not blindly apply federal decisional law. *State v. Newman,* 108 Idaho 5, 11 n.6, 696 P.2d 856, 862 n.6 (1985).

SIF goes off the track and asserts, without supporting citation, that federal decisional law is relevant unless the Idaho Supreme Court has "been persuaded that federal law is inconsistent with the Idaho Constitution." By framing the standard in this manner, SIF seeks in a subtle manner to avoid the threshold inquiry identified in *State v. Newman* and followed in *State v. Guzman.* If, as SIF suggests, the Idaho Constitution can not be read as affording Idaho citizens greater protection until there is a prior decision announcing that the Idaho Supreme Court has been persuaded that greater protection is afforded by the Idaho Constitution, then the seminal decision will always be absent. The question which must be asked is: Does the Idaho Constitution, as interpreted by the Idaho Appellate Courts, afford greater protections than are afforded by the Federal Constitution as it is being interpreted and applied in federal courts?

In an effort to buttress its assertion that this Court should deviate from established jurisprudence, SIF makes two claims that will not withstand scrutiny. First, the SIF wrongly asserts that this Court has already determined that reliance upon federal decisional law is appropriate in resolving a challenge to legislation based upon the Idaho Contracts Clause. SIF supports the proposition with unfounded reliance upon *State v. Korn,* 148 Idaho 413, 224 P.3d 480 (2009) and *Lindstrom v. Dist. Bd. of Health Panhandle,* 109 Idaho 956, 961, 712 P.2d6576, 662 (Ct. App. 1985). Both cases reflect that no contract was formed prior to the adoption of the challenged enactment. Neither case can be read as a rejection of or modification of Idaho's

jurisprudence relative to contracts which are impaired by governmental action.

Second, SIF asserts that, in relying upon *Guzman*, Dairy Queen has failed to account for the effect of subsequent decisions. In this regard, SIF directs attention to *State v. Donato,* 135 Idaho 469, 20 P.3d 5 (2001). It is not clear how SIF concludes that *State v. Donato, Id.* supports its position in this matter. What is clear is that the case buttresses Dairy Queen's position.[7]

The Court in *Donato* points out that, because of long-standing jurisprudence, unique characteristics of this State or specific language of Idaho's Constitution, some provision in the Idaho Constitution have been interpreted to afford protection concomitant with that afforded by the Federal Constitution, while others have been held to provide Idaho citizens with greater protection. For example, Idaho's Constitution affords greater protection against some searches and seizures than was afforded by the Federal Constitution because over a period of sixty-five years the Idaho Courts have due to the uniqueness of our state and the language of our Constitution, developed an exclusionary rule which was independent of and more protective than the rule as it has developed in federal courts.

The circumstances the *Donato* Court cited as militating in favor of applying a unique Idaho rule provide the rationale for adhering to the established Idaho approach for resolving contract clause claims. It is clear that since the 1930's, Idaho has employed an approach for addressing Contract Clause challenges which is materially different from the approach employed

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[7] The decision in *Donato* undermines SIF's argument that *Korn* can be read as support for the proposition this Court has concluded that for all purposes and in all circumstances the Idaho Contract Clause does not afford greater protection to the contracts of Idaho business and citizens than is afforded by the U.S. Constitution. At most *Korn* stands only for the proposition that with respect to *contracts formed after passage of an enactment*, the Federal and the State clause affords the same level of protection to contracts – none.

in federal courts. Indeed, fifty-seven years ago, with full knowledge of the inclination of federal courts to allow the exercise of police power to, in the right conditions, trump the restriction against the impairment of contracts afforded by the Federal Contracts Clause, this Court maintained Idaho's independent position that the Idaho Contracts Clause was a prohibition against enactments which, without regard to police power concerns, materially impaired the rights and obligations of existing contracts. *Compare*, *Penrose supra, with United States for the Benefit of Midwest Steel & Iron Works v. Henly, supra.*

In sum, this Court can and should resolve this matter based upon the approach it established as early as 1922 in *Fidelity* and utilized as recently as 1996 in *Curtis v. Firth.* The established Idaho precedent affords Idaho citizens greater protection than is afforded under the Federal approach. Idaho has opted for this higher level of protection and SIF has failed to explain why this Court should ignore *Guzman* and proceed to reduce the protection which it has for over nearly 90 years found to be afforded by the Idaho Contracts Clause.

C. THE "MODERN CONTRACT CLAUSE ANALYSIS" EVIDENCES SIF'S WISHFUL THINKING.

SIF argues that a three-step analysis utilized by federal courts in interpreting the *Federal* Constitution is the better, more modern and the required way for this *Idaho* Court to interpret the *Idaho* Constitution. (R.B., p.17.) SIF thus engages in wishful thinking about a better forum. Since, as demonstrated above, it cannot defeat Plaintiffs' argument based appropriately on Idaho precedent it urges the unnecessary employment of the Federal approach. This approach is contrary to the Idaho Constitution's plain meaning. And finding its roots in *Home Bldg. & Loan*

Ass'n v. *Blaisdell*, 290 U.S. 398 (1934), it is hardly a "modern" approach. Assuming for the sake of discussion that the Federal approach could properly be utilized, the correct application of that approach also leads to the conclusion that SB 1166aa(3) is unconstitutional.

Before jumping into the federal pool, however, it is important to be mindful of the Idaho prism through which such an analysis must be seen. As discussed above, if Idaho's established jurisprudence affords greater protections to its citizens, that jurisprudence should be honored. As to constitutional challenges, it is settled in this State that the presumption of legislative validity is rebutted " . . . by demonstrating that the law violates a constitutionally protected right such as the right to do business." *Sun Ray Drive-In Dairy, Inc. v. Trenhaile*, 94 Idaho 308, 310, 486 P.2d 1021, 1023 (1973). The Idaho Supreme Court has identified itself as having ". . . a duty to protect the people's rights as enumerated in the Idaho and United States Constitutions from legislative encroachment." *Thompson v. Hagan*, 96 Idaho 19, 24, 523 P.2d 1371 (1974).

This Court has recognized legislative limits. "It must be kept in mind that the Constitution of the State of Idaho is not a delegation of power to the legislature but is a limitation on the power it may exercise, and that the legislature has plenary power in all matters *except those prohibited by the Constitution. Idaho Tel. Co. v. Baird*, 91 Idaho 425, 428, 423 P.2d 337, 340 (1967). (Citations omitted, emphasis added.) Further, "'A statute cannot declare a policy contrary to the Constitution.' Any such declaration of policy is restricted by the limitations of the constitution." *Id.*, 428-429. (citations omitted)

1. Overview

There are three steps urged by SIF under the federal framework. The first step concerns "whether the state law has, in fact, operated as a substantial impairment of a contractual

relationship." *RUI One Corp. v. City of Berkley*, 371 F.3d 1137, 1147 (9th Cir. 2004).

Within this first inquiry are three sub-components, the first of which being "whether there is a contractual relationship." *Id.* The U.S. Supreme Court has indicated that this determination looks beyond whether, in general terms there is a contractual relationship and focuses instead upon whether there is "a contractual agreement regarding the specific . . . terms allegedly at issue." *General Motors Corp. v. Romein*, 503 U.S. 181, 187, 112 S.Ct. 1105, 1110 (1992). The second sub-component examines whether a change in the law impairs that contractual term. The third sub-component evaluates whether the impairment is substantial.

If this three-part threshold inquiry results in a finding that a law has substantially impaired a contract right, the court must determine in the next step if "the State, in justification, has a significant and legitimate public purpose behind the [legislation] such as the remedying of a broad and general social or economic problem." *RUI, supra*, at 1147. (Citations omitted.)

The third and final step requires the court to address "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. *Id.* (Citations omitted.)

2. Was there a contract term or a contractual relationship?

The first component of this initial inquiry is easily answered. As explained in greater detail above; there is a contract, it includes a right to receive a *pro rata* share of any rate readjustments and that right is vested and determinable. SIF attempts to avoid the fact that protected property interest are at issue through misplaced reliance on *Nat'l R.R. Passenger Corp. v. Atchison Topeka & Santa Fe Ry. Co.,* 470 U.S. 451 (1985). (R.B., p.21-22.) In the portion of

the decision from which SIF has extracted a quotation, the U.S. Supreme Court concluded that absent the express intent to do so, statutes could not create contracts binding upon the Government. It was in this context, and this context only, that the Court held that statutes reflect the policies of government which are inherently subject to change and that, in and of themselves, statutes so not create contracts.[8] *Nat'l R.R.* provides no authority for the proposition that statutes which are by law incorporated into properly formed contracts can be retroactively removed with the effect of defeating rights that have become fixed and vested.

SIF's reliance upon policy language which incorporates changes in the "workers compensation law" is misplaced. As discussed above, the "workers compensation law" does not include the provisions of I.C. § 72-901 *et .seq.* (See note 4 above). Hence, even if this language could cause a change in the "workers compensation law" to be retroactively applied to the contract, the repeal of I.C.§ 72-915 does not qualify as such a change. Moreover, no mention is made in the policy that such changes could have *retroactive* application. Courts have acknowledged that such clauses should be explicitly stated and that they are antithetical to the intent of the contract clause because a provision "in a contract that gives one party the power 'to deny or change the effect of the promise, is an absurdity.'" *Caritas Servs. Inc. supra.*,123 Wn.2d at 411 869 P.2d at 35(Citing *United States Trust Co.* 431 U.S. at 25, n. 23.).

SIF has completely failed in its attempt to support an argument that its contractual relationship with Dairy Queen does not involve a contract term providing that any rate readjustment must be allocated among all policyholders on a *pro rata* basis.

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[8] The U.S. Supreme Court separately considered whether the contracts (Basic Agreements) between Amtrak and the Railroads were impaired by Congress's prospective change of the reimbursement rates and concluded that they were not.

3. Was the contractual relationship impaired?

Rather than directly address this second component in the first step of the federal analysis SIF argues that "there is no vested or expected right to a dividend. (R.B., p.22.) Dairy Queen has already amply demonstrated that vested contractual rights have been impaired (pages 7 & 8 above) and will not repeat those arguments here. However, in support of its assertion that Dairy Queen cannot show that the circumstances warrant the threshold finding that SB 1166aa(3) causes a substantial impairment of a contractual relationship, SIF does raise a number of additional arguments.

First SIF asserts, without citing any supportive authority, that Dairy Queen cannot claim it has vested rights to a *pro rata* share of any funds distributed as rate readjustments because Dairy Queen provided no evidence of past practices that would give rise to such a right. (R.B., pp.22-23.) Dairy Queen's claim is not based upon a course of conduct. Rather, Dairy Queen's claim is based upon the express terms of its contracts with SIF (the allocation calculus set forth in I.C. § 72-915) and upon the fact that, as demonstrated in the record, in all years relevant to this action, the Manager chose to distribute money as rate readjustments. The existence of the claimed right given these circumstances is evident from the decision in *Farber*.

As a second argument, SIF claims that Dairy Queen cannot recover what it is entitled to pursuant to I.C. §72-915 because it cannot show that it had a "reasonable expectation" that it would be paid. (R.B., p.23.) SIF cites no relevant authority. Aside from ignoring the fact that this Court determined in *Farber* that SIF policyholders have a right to be paid a *pro rata* share of any amount distributed as rate readjustments, this argument takes on the appearance of an unsupported claim of waiver. Waiver is an affirmative defense requiring a showing that there

was an intentional relinquishment of a known right which cannot be implied absent evidence of a clear and unequivocal act manifesting the intent to waive. *Seaport Citizens Bank v. Dippel,* 112 Idaho 736, 739, 735 P.2d 1047, 1050 (1987). The record is does not lend any support to a claim that Dairy Queen has waived its rights to receive a *pro rata* share of any rate readjustments.

As a third argument, SIF seeking to make its repeated illegal conduct a controlling factor in the determination of whether Dairy Queen has vested and protected rights misplaces reliance upon upon a decision from the Texas Court of Appeals. But there is no rational linkage between this assertion and the cited case. In *Southwestern Bell Tel. Co. v. Public Utility Commission of Texas*, 615 S.W.2d 947, 956-57 (Texas Civ. App. 1981) the Court considered the constitutionality of a statute allowing for rates established by the Texas utilities commission to be, under very limited circumstances, retroactively applied. The Texas constitutional provision involved, one prohibiting retroactive application of statutes is not relevant to the resolution of this case because the core issue presented in this Texas case was whether under the circumstances (which include taking into account what the parties could in all the circumstance have reasonably expected) it was appropriate to conclude that a statute was being retroactively applied. There is nothing in the decision supporting the assertion that the vesting of a contract right can be defeated because one party to the contract has repeatedly breached the contract.

As a fourth argument, SIF attempts to use one of the evaluative standards utilized by the Texas Court in *Southwestern Bell* as a springboard from which to launch a claim that SB 1166aa is not a change in the law but rather a return to the law that existed before *Farber.* In this regard SIF suggests that the intent manifested by a state of the law is demonstrated by its repetitive violation of that law and the declarations of the 2009 Legislature relative to the intent of the 1998

Legislature. This argument is both brazen and specious.

Between 1917 and the enactment of SB1166aa, the law clearly and unambiguously expressed a legislative intention that any rate readjustments which were distributed would be distributed on a *pro rata* basis. *Farber* There has never been any contrary decision upon which anyone could rely. The Manager's failure to follow the clear and unambiguous statutory requirements of I.C.§ 72-915 has nothing at all to do with what the law of this State was for the interval between 1917 and 2009. The Manager does not determine the law of this State.

Similarly, the pronouncements of the 2009 Legislature relative to the intentions of the 1998 Legislature are not relevant to any determination of those intentions. SIF supplies no authority or facts to support a determination that the 2009 Legislature is competent to determine the intent underlying the enactments of the 1998 Legislature. Indeed, the such a determination would be contrary to law and in any event not supportable given the record in this matter.

The duty to interpret statutes and the underlying intent of the legislature rests exclusively with the judiciary. *Banker's Trust New York Corp. v. United States*, 225 F.3d 1368, 1376 (Fed.Cir. 2000) (relying upon *Marbury v. Madison,* 5 U.S. 137 (1803)) "[I]t is fundamental that the judiciary has the ultimate responsibility to construe legislative language to determine the law." *Mason v. Donnelly Club,* 135 Idaho 581, 583, 21 P.3d 913, 915 (2001).

The principles of statutory construction lend additional support to the determination that the 2009 Legislature is not competent to determine the intent of the 1998 Legislature. Where the language of a statute is clear and unambiguous, the plain, usual, and ordinary meaning of the words used by the Legislature is determinative of the intent of the Legislature that adopted that statute. *See, e.g., Wheeler v. Idaho Dept. of Health & Welfare,* 147 Idaho 257, 263, 207 P.3d 988,

994 (2009). Moreover, when the Legislature adopts a bill it is presumed to understand the reasonable interpretation of that bill. *State v. Taylor*, 59 Idaho 724, 87 P.2d 454 (1939) and to have known the law in effect at the time that it acts. *Druffel v. State, Dep't of Transp.*, 136 Idaho 853, 856, 41 P.3d 739, 742 (2002). There is no lawful basis upon which this Court can or should defer to an attempt by the 2009 Legislature to declare that a Legislature acting 21 years earlier did not understand what it was doing and did not intend to do exactly what it did.

Indeed, courts which have looked at this issue the have held that post-enactment statements of legislators are not part of the record of the Legislature that are considered the contemporaneous "history" that is appropriate for courts to consult. *See, e.g. Gillham v. Gump,* 140 Idaho 264, 268, 92 P.3d 514, 518, (2004) citing *Epstein v. Resor*, 296 F. Supp. 214, 216 (ND Ca 1969), *aff'd*, 421 F.2d 930 (9th Cir 1970), *McGee v. Stone*, 522 A.2d 211, 216 (RI 1987). Where there has been a substantial passage of time, the views of one legislative body about the intentions of its predecessor bodies form a hazardous basis for inferring intent. *South Dakota v. Yankton Sioux Tribe,* 522 U.S. 329, 355 (1998)

There is no rational basis to conclude that the 2009 Legislature is capable of correctly interpreting the intent of either the 1917 or the 1998 Legislature. It is apparent that in 1998, when the legislature substantially revised the laws pertaining to the State Insurance Fund, there was a discussion regarding the importance of allowing the SIF to distribute "dividends." R:105. Notwithstanding this discussion and the Legislature's knowledge of the clear meaning of IC. § 72-915, nothing in the legislative record nor in the 1998 enactment (House Bill 774, R:87-100) supports a determination that the legislature had any intention to change the methodology for allocation of rate readjustments as provided for by the clear and unambiguous language of I.C.

§ 72-915. In considering this question, this Court has already concluded that: "[i]n general the Manager's authority with respect to setting surplus and reserve levels and declaring dividends was not affected by the [1998]amendments." *Hayden Lake, supra.,* 141 Idaho at 392, 111 P. 2d at 77.

As its final argument the SIF suggests that the fact that SB 1166aa was passed before the remittur issued by this Court in *Farber* is relevant evidence that Dairy Queen had no vested right to a *pro rata* share of every dividend at issue in this matter. In support of this claim SIF cites two inapposite Washington decisions. Both *Boykin v. Boeing Co.,* 128 F.3d 1279 (9th Cir. 1997) and *In re Marriage of Giroux*, 704 P.2d 160 (Wash. App. 1984) involve situations where regulatory agencies, businesses and citizens had been proceeding based upon a judicially recognized application of the law until an overriding decision held that the previously recognized application was incorrect and the law had to be read and applied in a different manner. In both instances these court decisions lead to legislative action which would have the effect of causing the law to revert to what it had been before those decisions. Both cases were resolved on due process grounds and not on an impairment of contracts analysis. In both cases the Courts concluded that given the long-standing rule of law in place before the brief period in which the law was different and the short period of time in which the law was different, a party seeking the advantage of the change of law had acquired no vested right to the benefit of that change. Thus, even if "settled expectations" or "reasonable expectations" might, in Idaho, have some application where a judicially imposed change in the law is quickly followed by legislative action reverting to the previously applicable law, neither of these cases is authority in a case in which a clear and unambiguous Idaho law has remained unchanged for ninety-two years.

4. Was there a substantial impairment?

The pivotal determination in the three part threshold determination in the Federal approach involves a determination of whether the impairment to a contract right is substantial. SIF does not cite authority for assessing whether an impairment is substantial. In cases in which a federal court has utilized the Federal approach, an impairment of a contract has been found to be 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. See, e.g., S. Cal. Gas Co. v. City of Santa Ana*, 336 F.3d 885, 890 (9th Cir. 2003).[9]

Dairy Queen has demonstrated above that SB1166aa(3) relieves the SIF from a duty to comply with a financial term of the contact and completely deprives Dairy Queen of a remedy for the loss of a contract right. Those arguments will not be repeated here. On the other hand, SIF has not demonstrated any reason why the *Fidelity* test should not be the test applied to determine "substantiality" of the impairment caused by SB.1166aa(3). Instead, SIF relying upon a hefty portion of self-serving and myopic conclusions, conjures arguments for the proposition that depriving some of its insureds of millions of dollars of premium refunds (and at least one of its insureds of over $18,000) is an insubstantial impairment of the contract rights of those insureds.

First, SIF attempts to divert the focus from the terms of the contract to what it calls the overriding purpose of the workers compensation insurance policy – the provision of coverage. Dairy Queen agreed to pay premiums in order to secure the benefits of a contract with SIF. One

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[9] This looks a lot Idaho's materiality test ("a material impairment of a contract term is one which imposes new conditions or dispenses with conditions, or which adds new duties or releases or lessens any part of the contract obligation or substantially defeats its ends") *Fidelity, supra,* 35 Idaho at 813, 209 P. 453 , which would under *Guzman* be controlling if more restrictive.

of the benefits of that contract was Dairy Queen's inclusion into a risk pooling/averaging arrangement. Dairy Queen also gained the right to received a portion of its premiums back as a rate readjustment in the event that the admission charges collected by SIF exceeded the amount it needed in order to fulfill and secure its obligations to the pool. This right is a part of the consideration given and received and thus, a material element of this contract. That there are several benefits of the contract does not justify erasing or negating any of its material terms.

SIF's claim that it provides the same coverage to a policyholder who pays a premium of $300 as to a policy holder who pays $500,000, while correct on a superficial level, is part of the SIF's distorted view of the workers compensation system created by the Legislature. There may be marketing and political benefits inherent in SIF approach to rate readjusting – which reduces rate readjustments by losses – it was until the repeal of I.C. 72-915, illegal. *Farber.*

Up until May of 2009, the provisions of the law which created and controlled SIF demonstrate that the Legislature had a different vision of how the SIF should operate than the one SIF chose to see. The Legislature set up a no-fault system but SIF's dividend approach established a system which punishes without consideration of fault. The system created by the Legislature contemplated that employers would pay a premium based upon total payroll and rates determined by SIF (later the N.C.C.I.). The rates would be determined by the expected and demonstrated costs of securing all losses, administering all claims, operating the Fund and developing adequate reserves and unallocated surplus. The amount that each employer would pay did not and indeed could not depend upon the amount that is paid out due to injuries suffered

by that policyholder's employees.[10]

If the established rate was too high, SIF could end up with a few million dollars left over after fulfilling all of its obligations. Recognizing that this could happen the 1917 Legislature, acting upon the premise that if there was an excess then the rate used to calculate all premiums was too high, adopted a statute requiring that excess collections be refunded as rate readjustments on a *pro rata* basis to all policyholders. Recognizing that there might not be enough money the 1917 Legislature, instead of requiring that the employers be assessed based upon their losses, mandated that *all* policyholders be assessed.[11]

While the Legislature was free to determine that excess premiums should be shared among those policyholders who incurred fewer losses, it is clear that this is not the system that it created in 1917. Nor is it the system that existed after 1971 when the Legislature substantially revised the Worker's Compensation law. Nor is it the system that existed after1998 when, with dividends actually in its mind, it revised the statutes regulating SIF without making any changes to I.C. § 72-915. SIF may perceive unfairness in a system that allows a policyholder who suffers losses to share in the distribution of premium overpayments but SIF has not demonstrated any basis upon which this Court can conclude that the legislatures on 1917, 1971 and 1998 shared the SIF's concerns. SIF's hand wringing does nothing to alter this defect in its arguments.

SIF also asserts, without any citation of authority, that Dairy Queen cannot show that

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[10] SIF never had authority to assess individual policyholders extra premiums on account of that employer's losses though it could assess classes of employers (classified by risk) where it determined that the amount collected was insufficient to cover the risk assumed. Even this limited assessment right was taken away when I.C. § 72-916 was repealed in 1951.

[11] Indeed, the rate readjustment system employed by SIF is really a form of assessment as policyholders lose their share of the rate readjustment because they had losses.

there is a substantial impairment because this action is not applicable to all policyholders. Dairy Queen's action could not include those policyholders whose premiums were $2,500 or less because as a result of *Farber* they have already recovered damages. Dairy Queen's action also does not include those policyholders who have, in any given year, received more than a *pro rata* share of the amount being distributed because they are, as to that year, not damaged. Dairy Queen seeks recovery for a substantial minority of policyholders who have been denied a benefit of their contracts directly tied to the cost of those contracts. SIF fails to cite any authority supporting an assertion that an impairment of the price term of a contract is not substantial unless the impairment affects all similarly situated contracts.

SIF attempts to minimize the impairment involved in this action by overstating the impairment considered unconstitutional in decisions upon which Dairy has relied. SIF claims that the statute at issue in *Steward v. Nelson, supra.*, "effectively obliterated the intent of the mortgage." The statute at issue had the effect of shortening the period during which an action on the mortgage could be initiated and the statute provided the mortgagee no remedy of equal or similar value. 32 P. 2d at 845. Dairy Queen has suffered a greater loss. Its right to pursue a claim for the rate readjustments, while still legally viable, has been declared to have never existed and no alternative right or remedy has been supplied. SIF fails to explain how the impairment at issue here is not in fact more egregious than the impairment at issue in *Steward.*

SIF erroneously declares that the statute found to impermissibly impair a pre-existing contract in *Curtis v. Firth,* 123 Idaho 598, 850 P.2d 749 (1993), "would effectively eviscerate the right to act on a note secured by a deed of trust." The statute at issue in *Curtis* required that the deed of trust be foreclosed upon *before* a suit is initiated upon the note. The law in effect at the

time the note and deed of trust were executed allowed for an action on the note independent of when or if an action on the deed was initiated. The Court held that while the creditor still had a remedy, the change in that remedy impermissibly denied or obstructed one of the rights he had under a contract that pre-existed the statute. SIF fails to explain how restructuring the rights of one of the parties to a contract is more problematic than completely and retroactively taking away vested property rights as SB 1166aa(3) seeks to do.

SIF attacks Dairy Queen's assertion that the aggregate amount at issue could be as much as $24 million dollars [12] and that the amount at issue for one of the Plaintiffs exceeds $18,000. It should be noted that Dairy Queen's inability to provide exact figures is a byproduct of the District Court's refusal to allow Dairy Queen time to conduct discovery. Regardless, even with the information available it is clear that millions of dollars are involved and losses for individual policyholders that will exceed $10,000. This cannot be seen as insubstantial.

The contractual impairment affected by SB 1166aa(3) is clear. Set against the Idaho Contracts Clause, this impairment is prohibited. The impairment is not only apparent, it is substantial by any measure either quantitative or qualitative. This conclusion takes us over the threshold into the balance of the unnecessary application of the Federal approach.

5. The lack of a significant and legitimate public purpose is apparent.

SIF goes on to argue the second step of its borrowed jurisprudence by stating that even if

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[12] The sponsor testified both that SIF faced a potential loss as $24 million and that SB 1166 was not intended to change the holding in Farber. R:187-188. Hence, the only logical way to take this testimony is that Senatory Goedde and Mr. Hall were speaking about future judgments and not the amount at issue in *Farber* (those costs were going to be incurred with or without the passage SB 1166aa). R:188, & 190 (respectively). They did not elaborate or tie that number specifically to this action which, at that point in time, had not yet been filed.

there is a substantial impairment of the contractual relationship there should nevertheless be an inquiry "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.'" (R.B., p.30.) Again, the inapplicability of this tack is remarkably evident: there is neither a "significant" nor a "legitimate" *public* purpose afoot here which would support an exercise of the police power necessary to overcome the constitutional protection afforded contracts in Art. I § 16.

This is not to deny to the Idaho Legislature a legitimate exercise of the police power. But that exercised power must address a " . . . consideration of public health, safety, morals or general welfare . . ." in order to pass constitutional muster. *Dry Creek Partners v. Ada County Comm'rs*, 148 Idaho 11, 19, 217 P.3d 1282, 1290 (2009). The Legislature of this State must observe and respect those fundamental rights and liberties protected by the Idaho Constitution. The right to contract freely and to depend on the law to protect that right is one of those fundamental rights. Indeed, Art. I, § 16 does protect this fundamental, substantive right.

In addition to these general limitations, it should be recalled that State Agencies are apparently some of SIF's policyholders. The Fiscal Note accompanying the repeal of I.C. § 72-915 frets in a speculative manner that these State Agencies might be adversely affected by Farber because of some non-identified "uncertainties." (R. 245) [13] When the State engages in this type

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[13] State agencies (who are in privity of contract with SIF) fall into two categories. Any State agencies who were paid too little in the way of rate redistribution because of SIF's failure to follow I.C. 72-915 will benefit from this action. State agencies which were favored by SIF and overaid to the detriment of the non-State policyholders will get to keep the windfall arising from SIF's willful and illegal departure from the legislatively-mandated distribution methodology.

of self-protective legislature which affects its contractual obligations, the federal case law on which SIF depends recognizes that the "standard of review is more stringent ..." *S. Cal. Gas Co. v. City of Santa Ana, supra* 336 F.3d at 894 citing *Energy Reserves Group, Inc. v. Kan. Power & Light Co.*, 459 U.S. 400, 412-13 & n.4.

We have here a whole constellation of factors which militate against the District Court's finding of constitutionality. There is a fundamental right. It is a substantive right. It is a clear and unambiguous right declared by this Court in *Farber*. The right has been impaired on a retroactive basis. Yet, the right is explicitly protected by an unambiguous constitutional provision.

With this constellation we have a requirement that legislative action negating a right cannot be sustained if the legislation favors a special interest. The police power, if it is to be sustained, must affect a "broad and general social or economic problem" as has been admitted by SIF. (R.B., p.30.) The retroactive repeal of I.C. § 72-915 is not in conformity to this requirement.

Beauty is said to be in the eye of the beholder. From SIF's point of view the retroactive repeal of I.C. § 72-915, instigated by one of its Directors, Senator Goedde, is a lovely piece of legislation. However, even SIF must recognize the special interest aspect of this legislation. Rather than having a broad and general social or economic problem as its focus, what is addressed is SIF's pique at being told by the Idaho Supreme Court in *Farber* that it has been illegally allocating rate readjustments. SIF and only SIF benefits from this legislation. Neither the public nor any other insurance company are benefitted.

This situation falls squarely under the analysis of this Court in *Straus v. Ketchum*, 54

Idaho 56, 83 (Idaho 1933) where a legislative enactment changed the prior law (treated as a part of the contract) relative to how property could be released from a lien. The police power was discussed but was marginalized by the very basic concept we see here.

> "The Legislature cannot, under such constitutional provisions, (Art. I § 16) 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."

Indeed, rather than a "broad and general social or economic problem" being addressed by this legislation, we do not even have all of the SIF's policyholders being targeted by the retroactive aspect of this legislation. As has been discussed above, the only policyholders penalized by SB1166aa(3) are those policyholders in this vastly reduced subset, CDC Dairy Queen among them.

The 2009 Legislature's Statement of Purpose and Fiscal Note to S.B. 1166aa (R.245) does not assist SIF's arguments. The legislative Statement says that there is a need to "clarify" the law regarding the payment of future dividends. This Court had just then unanimously stated in *Farber* that the "law" regarding the distribution of rate readjustments (dividends) is "clear and unambiguous." Something that is clear and unambiguous, needs no "clarification."

A legislature cannot posit that there has been an "adverse decision" by the Supreme Court unless, of course, the legislature has identified with a special interest which had been impacted by the decision. A judicial holding that a legislative enactment is "clear and unambiguous" cannot possibly be "adverse" to the legislature's will as expressed in I.C. § 72-915. The ruling in *Farber* may have been "adverse" to the position taken by an obtuse SIF. But that hardly rises to the level of adversity to any legislative intent or to the *public* interest. The "problem" being addressed by the retroactive repeal is not something broad and general in the sense of a social or

economic problem. It is a problem only for SIF. The legislative solution to SIF's unique problem does not address any "consideration of public health, safety, morals or general welfare . . .." *Dry Creek, supra.* It is specific to SIF.

SIF does not monopolize the worker's compensation insurance business in this state. The Manager's Affidavit of record states that there are many insurance companies offering worker's compensation insurance in Idaho. (R. 212.) Thus, where is the "public purpose" behind the retroactive repeal of I.C. § 72-915? There is nothing in the record which demonstrates how SIF's competitors pay dividends to their policyholders. There are only conclusory statements obliquely referencing "competition" in the Statement of Purpose which do not demonstrate that other sureties pay out discriminatory dividends.

SIF points out that "the very requirement of worker's compensation is, in itself, an express exercise of the police power of the State" and cites to I.C. § 72-201. (R.B., p. 30.) Indeed, that statutory scheme abrogated the common law system governing the remedy of workers against their employers for work-related injuries. This remedy was an idea whose time had come.

But this statutory framework did not exclude other sureties from writing worker's compensation insurance. *See*, I.C. § 72-301. Accordingly, the SIF, while it may have been the first surety for these purposes, SIF does not control the system. If SIF disappeared tomorrow, there are other sureties approved by the director of the Department of Insurance which would continue to write this line of business. Indeed, this is the "competition" against which SIF wants to compete. If SB 1166aa(3) helps SIF to compete against its rivals, that is further evidence of special interest legislation. While a fundamental change in the law governing all workers'

injuries in Idaho was a valid exercise of the police power in 1917, special interest legislation attempting to bail out one of Idaho's worker's compensation sureties from its illegal activity is not.

Clearly, not every act of the Legislature for the benefit of SIF is automatically clothed with a public purpose. A legislative declaration of public purpose, while entitled to consideration by the Idaho Supreme Court, "is not binding and conclusive upon the question of public purpose." *Board of County Comm'rs v. Idaho Health Facilities Authority*, 96 Idaho 408, 502 (Idaho 1975). It follows, then, that this Court can conclude that the retroactivity of SB 1166aa(3) serves no public purpose and is an overreach and misapplication of the police power.

Contrary to the suggestion of SIF, (R.B., p.31), its assertion that public employers must insure through SIF is cleverly worded. SIF lost that battle when the Supreme Court ruled that I.C. § 72-301 allows public employers to reject the SIF and may, instead, self-insure for the purposes of worker's compensation. *City of Boise v. Industrial Comm'n*, 129 Idaho 906, 909 (1997). And SIF, while acting as administrator of workers' claims while employed by the Idaho National Guard, is fully reimbursed for monies paid out on account of the Guard's liability to injured members. The fact that SIF is not reimbursed for its administrative costs is not relevant to this action which neither involves any of SIF's administrative costs nor the Idaho National Guard. *See*, I.C. § 72-929.

As far as any "financial uncertainty" for this insurance company, previous briefing has shown that the surplus of SIF is nearly ten times greater than any amount that could possibly be at risk by this lawsuit. Moreover, despite the decision in *Farber*, SIF continues to grow its

surplus and pay substantial dividends.[14]

Finally, when one looks at the publically promulgated justification for this questionable legislation, one notes that the Legislature engages in rank speculation. (R.245.) There is no absolute statement by the Legislature that the general public will be harmed by this Court's ruling in *Farber*. At best, there are "uncertainties" which "could" impact "future" dividends and deviations– not as to all insurance companies but only as to SIF. The Statement of Purpose speculates that there is a possibility that "could" force SIF to pay rate readjustments (future tense) on policies that are (present tense) not financially profitable. This is only speculation about what the future holds for this insurance company and no others. Recall, please, that the instant litigation does not threaten SIF's ability to distribute money in the form of rate readjustments however it wishes *after* the effective date of the subject litigation. Nor will this suit force SIF to bankruptcy court. It is only the elimination of material and vested rights on a retroactive basis that is being questioned by Plaintiffs here. Thus, nothing the Legislature has said demonstrates or supports a legitimate *public* purpose. Everything stated by the Legislature favors a special interest – Senator Goedde's insurance company.

It is not only what is said in the Statement of Purpose and Fiscal Note that is important. What is *not* said seems dispositive when one considers the requirements for an appropriate exercise of the police power. Cases, both within this jurisdiction and others, are uniform in

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[14] In 2008 SIF showed a unallocated surplus of more than $190,000,000 and authorized in excess of 13,000,000 in rate readjustments. (R.202.) In 2009 SIF showed a unallocated surplus of more than $197,000,000 and authorized in excess of 14,000,000 in rate readjustments. (R.202.) In. In 2010 SIF resolved *Farber* and still showed a unallocated surplus of more than $201,000,000 and authorized in excess of 10,000,000 in rate readjustments. *Appellants Submission of Public Records of Which the Court May Take Judicial Notice.*

stating that the police power has limitations. Were it not so the government could act by unchecked fiat and the constitutional protections afforded the people would have no meaning. It is the public peace, welfare, health, and safety that must be the focus of any exercise of the police power. *Dry Creek Partners, supra.* Aid to a singular insurance company is special interest legislation. There must be a rational connection between the protection of the health, safety, morals, and welfare of the people and the legislation at issue. This is particularly true when that legislation is facially prohibited by an explicit constitutional protection as here. If there is a case to be made for a rational connection, it does not appear from anything the Legislature has provided in 2009 or from SIF's arguments contained in its Response Brief.

That there is nothing in the Statement of Purpose or in the Fiscal Note which states directly that the retroactive effect of this legislation is even important, much less necessary. The best that can be said is that looking to the future SIF wants to be freed up in the future from the constraints of I.C. § 72-915. But what has *not* been said is anything about the ability of SIF to remain solvent. Nothing is said regarding the future availability of worker's compensation insurance for those employers who wish to contract with SIF. Nothing is said regarding businesses leaving the state. Nothing is said regarding the ability of the state to attract new business. Nothing is said regarding the ability of SIF to pay claims. Nothing is said regarding the collection of premiums or the ability of employers to pay those premiums. Nothing is said regarding the future ability of SIF to declare that there is sufficient unallocated surplus so as to pay to its favored policyholders as much or as little as it wishes. Nothing is said regarding the ability of SIF to conduct its operations on a day to day basis. Nothing is said regarding the ability of injured workers to receive benefits under existing SIF policies and applicable legislation. Any

bridge, therefore, between the retroactive effect of this legislation and the necessary foundation for the appropriate exercise of the police power is absent. There is nothing provided by the Legislature which indicates that the purpose behind the historical establishment of SIF will be in any way destroyed, inhibited, crippled, damaged, rendered inoperative, or altered in such a way so as to frustrate the no-fault worker's compensation scheme adopted by Idaho nearly 100 years ago.

SIF states that there is a "new interpretation" of I.C. § 72-915 found in *Farber* which excuses the Legislature's retroactive tinkering with contractual terms and relationships. (R.B., p.32.) The eyes of SIF may have been opened by the unanimous decision in *Farber* but given the ruling by this Court that statute was "clear and unambiguous" it is hard to fathom how SIF could have interpreted I.C. § 72-915 any other way than did this Court. All of the arguments of SIF were found to be unpersuasive in *Farber*. "Unless the result is palpably absurd [the Supreme Court] must assume that the Legislature means what is clearly stated in the statue." *Viking Constr. v. Hayden Lake Irrigation Dist.*, 149 Idaho 187, 192 (2010). It requires an immense amount of *chutzpah* to pretend, now, that the Idaho Supreme Court has given a new "spin" to legislation which has been judicially declared to be clear and unambiguous.

Finally, SIF loses sight of the forest for the trees in its argument that policyholders who have experienced losses should not receive a rate readjustment.[15] Public policy is determined by the Legislature and not by SIF. The Legislature's expression of the policy relative to dealing

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[15] This argument is misplaced if we are to be driven like sheep into the fold of the federal analysis. It does not address the exercise of the police power at all but, rather, is merely an expression of discomfort with the requirements of I.C. § 72-915.

with excessive surplus was created in 1917 and left in tact until 2009. There are situations in which an employers injury causing conduct is so egregious, *See, e.g. Dominguez v. Evergreen Resources, Inc.* 142 Idaho 7, 121 P.3d 938 (2005) that the Legislature might determine that public policy required some form of monetary consequence (loss of rate readjustment, assessment, direct action). However, the Legislature has not, prior to 2009 taken any action which would suggest that it prioritized this public policy over the policy inherent in the *pro rata* rate readjustment calculus it adopted in 1917. Until the adoption of SB1166aa, worker's compensation was clearly and unequivocally a no-fault system in which individual assessments were not authorized. As such what is the logic in permitting an employer who has suffered claims to be penalized by being deprived of a *pro rata* share of distributed rate readjustment?

In sum, not only does the retroactive repeal of I.C. § 72-915 constitute a substantial impairment of the contract of insurance but also the retroactive aspect of the legislation at issue cannot be seen to pass muster against any legitimate exercise of the police power. Special interest legislation does not trump specific constitutional protections.

6. Reasonable conditions are not apparent justifying the retroactive legislation.

We have left a third step following SIF's stumble on the first and second. Assuming, *arguendo,* that the retroactive effect of the repealing legislation is excused because the state does have a sustainable significant and legitimate public purpose in helping out SIF's special interests we now examine this third step, *i.e.,* whether the saddling of the legislation with a *retroactive* effect is of a character appropriate to any public purpose. It is not and the retroactive aspect of the repeal of I.C. § 72-915 cannot, therefore, be upheld on this analytical step alone.

SIF argues that there has been only some sort of "adjustment" of the "rights and

responsibilities of the contracting parties." Hardly. A mortal wound is not an "adjustment" of one's lifestyle. It is, by definition, fatal. So, too, the retroactive effect of this legislation is to wipe out completely the vested property interest that SIF's policyholders previously enjoyed and, indeed, to which they were entitled by virtue of I.C. § 72-915.

SIF, a quasi-governmental private insurance company,[16] has contracts with the State of Idaho and its agencies. In that sense, the state itself is a contracting party. In addition, and as has been previously discussed, SIF does have a quasi-public status in the state's jurisprudence. "Rather we believe the legislature sought to create a state managed insurance fund that operated, in many ways, like a private mutual insurance company." *Kelso, supra*, at 135. This lessens, considerably, the deference of a judicial body to legislative judgment as to the necessity and reasonableness of a particular measure as stated in *Energy Reserves*, 459 U.S. at 412-13, a case upon which SIF has relied.

SIF states in its briefing that the repeal of I.C. § 72-915 is a "narrow repeal." That may be true from the viewpoint of SIF. From the viewpoint of the policyholder, however, it is a complete and inexcusable elimination of an important term of the insurance contract.

SIF argues that the repeal has no impact on the express terms of the policies. It is perhaps tiresome to continue to refute this fundamental error but, out of an abundance of caution, it must be refuted. I.C. § 72-915 is an express term of the contract of insurance. It is incorporated into the contract of insurance. There is no doubt about this proposition and the fact that SIF continues to beat

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[16] Mr. Hall, SIF's advocate at the April 7, 2099 legislative hearing, expressed a belief that SIF is a "state agency." (R.190.) If Mr. Hall is correct, then the level of scrutiny increases both because the government is being self-protective and the impairment is complete or, if SIF is more of a statutorily-created corporation which sells insurance then we have the Legislature recognizing and coming to the aid of a special interest.

this drum shows that its arguments are drained of the subtle but critical distinctions necessary in analyzing what the Legislature has done.[17]

When SIF writes that the law has "merely been changed to conform with the methodology for calculating dividends that the Manager has used for years" (R.B., p. 36), a critical factor has been left out. The methodology for calculating dividends has been used by the Manager *illegally* for years. This SIF insensitivity to its own illegal conduct in the face of a mandatory, statutorily-imposed, methodology is really rather incredible after *Farber's* unanimous ruling. If there was a problem, prospective repeal would have been sufficient.

It is tiresome to reiterate the concepts put forth by Dairy Queen in the last few pages. But the solution to the SIF's transitory inconvenience and apparent chagrin occasioned by *Farber* is not to repeal the law retroactively. That is more than an "adjustment." It is overkill. The legislative action is simply not of a character appropriate to the public purpose behind the worker's compensation framework. A *retroactive* repeal is not necessary. It is not at all helpful to the general public but only to SIF in the sense that it blesses on an *ex post-facto* basis SIF's illegal conduct in derogation of the vested rights of many policyholders while benefitting those favored few who have somehow gained luster in the eyes of the Manager. If SIF wants to conduct its business in this fashion in the future, it may do so because I.C. § 72-915 is no longer on the books. But to go back in time through a bootstrapping effort to re-write history should be seen by this Court as not reasonable in the first or last instance.

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[17] Senator Goedde, eschewing even a fig leaf to cover this special interest bill, introduced the legislation and shamelessly advocated its adoption. Many losing defendants would love to re-write the law and exculpate themselves from illegal conduct by applying legislation retroactively. Simply put, that is what has happened here.

There are three principal reasons given by SIF to bolster its claim of a "legitimate public purpose." (R.B., p. 30.) Each of the three reasons is met by the prospective application of the legislation. Accepting, *arguendo*, SIF's justification for the legislation, the "adverse decision" of *Farber*, the need to "clarify" the law (to SIF's liking), and to allow SIF to operate efficiently are all met by the repeal of I.C. § 72-915 as it operates prospectively. SIF can now distribute rate readjustments as it pleases. There is no need for any retroactivity. With an unallocated surplus of about two hundred million dollars and a potential liability of, at most, $24 million, there is no "financial uncertainty." There is no need for any retroactivity to cure this non-problem. SIF does not want to honor its contractual obligations and that is at the heart of the matter. The retroactive "cure" is for a non-existent disease. It is not based upon reasonable conditions and is not of a character appropriate to any public purpose.

Since SIF is free to adjust rates prospectively, it will have great latitude in distributing these rate readjustments as it wishes. That being the case, SIF itself could respond appropriately to whatever it perceives to be the best solution to its problems, if they truly exist. If the state agency policyholders were given too much of a rate readjustment then SIF could reduce future readjustments to balance out the overpayment. There are, with the prospective repeal of I.C. § 72-915, an infinite number of possibilities limited only by the managerial acumen of SIF's leadership. Accordingly, retroactive repeal was not necessary.

D. MERE ADHERENCE TO REQUIREMENTS OF I.C. § 73-103 DOES NOT CAUSE THE SB 1166AA(3) TO BE CONSTITUTIONALLY RETROACTIVE.

SIF asserts that the legislature adhered to the legal requirements for declaring one of its acts to be retroactive. While it is true that the legislature fulfilled the statutory requirement of expressly

declaring the intention for the law to be eligible for retroactive application, that is not and never has been the issue on which this action turns. Moreover, unless the Idaho Constitution cannot properly be seen as part of Idaho Law, it is not correct for SIF to maintain that the "retroactive component of the repeal of I.C. § 72-915 followed Idaho Law until it is determined that the retroactive repeal is not prohibited by the Idaho Constitution.

E. THE LEGALLY APPROPRIATE EFFECTIVE DATE OF THE SB 1166AA HAS NOT BEEN DETERMINED BY THE RULING BELOW.

In addressing the Defendants Motion for Summary Judgment which made no request for a determination of the effective date of SB1166aa, the District Court gave absolutely no indication that it was giving any consideration to whether the "emergency" declaration in SB1166aa was legally sufficient to cause the bill to be effective when signed by the Governor as opposed to on July 1, 2009. Given that the Court found that retroactive application of SB1166 aa was constitutional the effective date of the bill is of no consequence. The same cannot be said however if this matter is remanded to the District Court on the basis that retroactive application of SB1166aa(3) is unconstitutional. At that point and only at that point will it become necessary for the District Court to consider the effective date of the bill. While SIF has cited cases which are at least the starting point in that analysis, the effort to have this Court decide a matter that SIF did not present to the District Court and that the District Court did not decide, is inappropriate.

III. CONCLUSION

The decision of the District Court was in error and should be reversed and remanded with instructions to enter partial summary judgment for Plaintiffs on the issue of the violation of

Art. I § 16 of the Idaho Constitution.

RESPECTFULLY SUBMITTED this 17th day of October, 2011.

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 17th day of October, 2011, 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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X HAND DELIVER

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____ OVERNIGHT MAIL

____ FACSIMILE **208-395-8585**

Bruce S. Bistline