

Case Nos. A10-1244 and A10-1331

State of Minnesota
In Court of Appeals

City of Minneapolis, a municipal corporation,

Respondent.

v.

Minneapolis Police Relief Association and
Minneapolis Firefighters Relief Association,

Appellants.

BRIEF AND ADDENDUM OF RESPONDENT

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STATEMENT OF THE ISSUES

- 1. Did the district court correctly rule that the Associations violated Minnesota Statutes § 69.77, subd. 11, when they unilaterally added extra items to their definitions of “salary” for purposes of calculating pension benefits without amending their bylaws and obtaining the City’s approval?**

The City moved for partial summary judgment and submitted a post-trial brief arguing that the Associations violated Minn. Stat. § 69.77 by including new salary items, without amending their bylaws, in calculating pension benefits. (Pl.’s Mem. Supp. Mot. Summ. J. 3, 24–28; Pl.’s Post-Trial Br. 1.) The district court concluded that the Associations’ addition of extra items violated the Associations’ bylaws and Minn. Stat. § 69.77. (ADD.25; ADD.47.) Appellants filed this appeal.

Apposite Legal Authorities:

Minn. Stat. § 69.77; Minn. Stat. § 423B.05; Minn. Stat. § 423C.02; Minn. Stat. § 423C.10; *Isaacs v. Am. Iron & Steel Co.*, 690 N.W.2d 373, 376 (Minn. Ct. App. 2004); *Indianhead Truck Line, Inc. v. Hvidsten Transp., Inc.*, 128 N.W.2d 334, 341 (Minn. 1964).

- 2. Did the district court correctly rule that the Associations overpaid pension benefits by miscalculating salary components in violation of the existing definitions of salary in their bylaws?**

The City moved for partial summary judgment and submitted a post-trial brief arguing that the Associations overpaid pension benefits by miscalculating salary components contrary to their bylaws. (Pl.’s Mem. Supp. Mot. Summ. J. 2–3, 17–24; Pl.’s Post-Trial Br. 2–7.) The district court concluded that the Associations overpaid pension benefits by adding salary components contrary to their bylaws. (ADD.25; ADD.47.) Appellants filed this appeal.

Apposite Legal Authorities:

Minn. Stat. § 69.77; Minn. Stat. § 423B.05; Minn. Stat. § 423C.02; Minn. Stat. § 423C.10; *Isaacs v. Am. Iron & Steel Co.*, 690 N.W.2d 373, 376 (Minn. Ct. App. 2004); *Indianhead Truck Line, Inc. v. Hvidsten Transp., Inc.*, 128 N.W.2d 334, 341 (Minn. 1964).

- 3. Did the district court abuse its discretion when it granted equitable relief enjoining the Associations to correct their benefit calculations and recoup overpayments back to June 9, 2000?**

The City’s complaint sought a permanent injunction, declaratory judgment, and requested “just and equitable” relief. (Compl. ¶¶ 1, 29(f).) The City raised the

recoupment issue in its opening trial statement and post-trial motions. (10/5/09 Tr. 28–29; Pl.’s Post-Trial Br. 16–29.) The district court ordered the Associations to recoup member overpayments from June 9, 2000, forward. (ADD.47–48.) Appellants filed this appeal.

Apposite Legal Authorities:

Minn. Stat. § 356A.04, subd. 1; § 555.08; *Mattson v. Underwriters at Lloyds of London*, 414 N.W.2d 717, 719 (Minn. 1987); *Theros v. Phillips*, 256 N.W.2d 852, 859 (Minn. 1977); *Frisk v. Bd. of Educ.*, 75 N.W.2d 504, 514 (Minn. 1956); *In re the Disability Earnings Offset of Mylan Masson*, 753 N.W.2d 755 (Minn. Ct. App. 2008).

STATEMENT OF THE CASE

Respondent City of Minneapolis (“City”) commenced suit on June 9, 2006, alleging that the Appellants Minneapolis Police Relief Association (“Police Association”) and Minneapolis Firefighters Relief Association (“Fire Association”)¹ were miscalculating and overpaying pension benefits. The Associations brought a Rule 12 motion to dismiss. The district court, the Honorable Janet Poston presiding, denied the Rule 12 motion by order dated January 24, 2007. The Associations appealed and this Court affirmed the denial of the motion to dismiss on April 15, 2008.

The City moved for partial summary judgment, and by order filed September 21, 2009, the district court granted in part and denied in part the City’s motion. The district court held that the Associations had miscalculated benefits in several ways and granted the City a declaratory judgment accordingly. The district court denied the City’s motion in part, finding disputed facts for trial concerning certain calculations. The district court denied the Associations’ motion for summary judgment and set the matter for trial.

¹ The Police Association and the Fire Association collectively shall be referred to as “the Associations.”

On October 5, 6, and 15, 2009, the parties tried the remaining issues to the bench and argued regarding the appropriate relief. The district court issued its original Findings of Fact, Conclusions of Law, and Order for Judgment on November 20, 2009. The district court granted declaratory and injunctive relief to the City, ordering the Associations to correct their benefit calculations in accordance with the court orders and to revise and resubmit their 2010 levy requests. The district court rejected the City's request for an injunction requiring the Associations to recoup benefit overpayments from their members.

The Associations appealed, and moved for a stay of the injunction pending appeal. The district court denied the Associations' motion for a stay. On December 23, 2009, the City moved for amended findings and conclusions on the issue of recoupment. In light of the City's motion for amended findings, this Court dismissed the Associations' appeal as premature. The district court held a hearing and received additional evidence from the parties' actuaries on the subject of recoupment. On May 17, 2010, the district court issued its Amended Findings of Fact, Conclusions of Law, and Order for Judgment. In addition to the relief previously granted to the City, the district court granted additional injunctive relief, ordering the Associations to recoup from their members benefit overpayments made from June 9, 2000, through December 31, 2009, to submit their recoupment plan to the City and the district court by June 4, 2010, and to commence recoupment by July 1, 2010.

On May 28, 2010, under the stipulation of the parties, the district court entered an order staying the commencement of recoupment pending appeal and freezing the

Associations' benefits at the May 28, 2010, levels. The Associations were required to submit their proposed recoupment plans to the City and the Court by June 4, 2010. Finally, the stipulated order provided that "the parties agree that no appeal will preclude the [district court's] ability to rule further on the issue of recoupment."

On July 15, 2010, the Associations filed their notice of appeal from the order granting injunctive relief in the May 17, 2010, Findings of Fact, Conclusions of Law, and Order for Judgment. On July 14, 2010, the district court issued an order directing the entry of final judgment, and entered judgment on July 15. On August 2, 2010, the Associations filed an appeal from final judgment. By order dated August 4, 2010, this Court consolidated the two appeals.

STATEMENT OF FACTS

1. Background

The Minnesota Legislature established the Police Association and Fire Association to maintain and administer pension benefits for its members, their surviving spouses, and dependents. *See* Minn. Stat. §§ 423B.04, 423C.02. "[A]ctive and retired members" of the police and fire departments control and operate both Associations. Minn. Stat. § 423B.04, subd. 1; Minn. Stat. § 423C.02, subs. 1 & 3. The Police Association board consists of nine members, seven of which are occupied by active and retired Police Association members and their surviving spouses. Minn. Stat. § 423B.05, subd. 1. The other two members are appointed by the Minneapolis City Council. The Fire Association board consists of up to ten member-selected positions and two City appointees. Minn. Stat.

§ 423C.03, subd. 1. The Associations are closed funds,² with fewer than 14 active employees in the Police Association and 27 active Fire Association employees. Minn. Stat. § 423B.01, subd. 2; Minn. Stat. § 423C.01, subd. 2. (See RA.33; RA.341.) There are increasingly fewer active employees to contribute funding for plan beneficiaries.

The Associations calculate their financial obligations annually. Minn. Stat. § 69.77, subd. 4. If the Associations do not have sufficient funds to cover pension benefits, the City is required to finance the difference. Minn. Stat. § 69.77, subds. 4 & 6. If the City does not include the full amount of its financial obligation in its tax levy, the Associations may require the county auditor to “spread a levy over the taxable property of the municipality in the amount of the deficiency certified by the officers of the relief association.” Minn. Stat. § 69.77, subd. 7(c); see *City of Minneapolis v. Minneapolis Police Relief Ass’n*, No. A07-420, 2008 WL 1747923, at *4 (Minn. Ct. App. April 15, 2008) (R.Add.-4) (“the county auditor is required to levy whatever amount is certified by the association”). In short, City taxpayers are required to cover any financial shortfalls for the Associations.

The Legislature enacted a statutory system of checks and balances to govern the Associations’ operations. See Minn. Stat. ch. 423B; Minn. Stat. ch. 423C; Minn. Stat. ch. 69; Minn. Stat. ch. 356; Minn. Stat. ch. 356A. The Associations’ bylaws constrain their benefit determinations, and state law requires that any bylaw amendment that increases retirement benefits is not effective until the City ratifies the change. Minn. Stat. § 69.77,

² The Associations closed to new members on June 15, 1980. (AA.179:3-4.) Since then, new police officers and firefighters become members of the Public Employees Police and Fire Fund. Minn. Stat. § 423A.01, subd. 1.

subd. 11. As part of this system, the Associations owe fiduciary duties not only to their members, but in equal measure to City taxpayers and the State. Minn. Stat. § 356A.04.

State law requires that the Associations set pension benefits based on the current salaries of active duty officers and firefighters. Minn. Stat. § 423B.01, subd. 20; Minn. Stat. § 423C.01, subd. 28; *see also Minneapolis Police Relief Ass'n*, 2008 WL 1747923, at *2 (R.Add.-3) (finding that the Associations do not “exercise discretionary power in compiling the compensation data and applying the formula” for the definition of “salary”). The Associations’ bylaws define the components of “salary” for their benefit calculations. (RA.12–13; RA.46.) After calculating each respective position’s current salary, the Associations divide the result by 80 to calculate a pension unit.³ Minn. Stat. § 423B.01, subd. 20; Minn. Stat. § 423C.01, subd. 28. Association members accrue pension benefit “units” based on their years of service. (AA.179:5–8.)

2. 1995 Litigation and Settlement

In 1994, the City disagreed with the Associations’ salary calculations. (AA.009–16.) Specifically, the City complained that the Police Association’s calculations erroneously included Shift Differential (extra pay for nighttime shifts), and expanded their salary computations to include the Sick Leave Pay Plan and the Semi-Annual Overtime Pay Plan. (AA.010–11.) The City objected to the Fire Association’s inclusion of Selection Premium (extra pay for working as a firefighter), the Sick Leave Pay Plan,

³ The same law firm (Rice, Michels and Walther, LLP) that calculates these units represents the Associations as legal counsel and legislative lobbyists, and represents Minneapolis’s police and firefighter unions. (AA.084:13-85:24; ADD.38, ¶ 4 n.2.)

and overtime pay in its salary calculations. (AA.011.) When the City refused to fund these disputed overpayments, the Associations asked the county to levy the unfunded amounts against the City's property taxes. (AA.012-13.) The county complied. (AA.013.) The City, in turn, sued the Associations challenging their salary calculations. (AA.009-16.) Individual beneficiaries were not party to the lawsuit. (AA.009.) On September 15, 1995, the City and the Associations reached a court-approved settlement. (AA.017-22.)

The 1995 Settlement Agreement prescribed salary calculations for 1995 through 1998. In addition, the Agreement required the Associations to amend their bylaws to define salary "to prevent future differences of opinion on the elements of compensation to be included in salary." (AA.019.) Bylaw amendments required City approval. (AA.019.)

The Agreement emphasized that items included as salary must be "payable under a collective bargaining agreement." (AA.019.) The parties agreed that police salary included base wages; Shift Differential; a uniform and professional allowance; longevity payments (a premium awarded to long-serving officers); 60 hours of accumulated compensatory time; work-out program payments; and the maximum Sick Leave Buy-Back Pay available to top grade patrol officers. (AA.020.) Firefighter salary consisted of base wages, including Fair Labor Standards Act overtime attributable to the regularly scheduled work period; Selection Premium; a uniform and professional allowance; longevity payments; an average of overtime actually worked by firefighters with 25 years

or more of service, up to 136 hours, in the immediately preceding year; and the maximum Sick Leave Buy-Back Pay available to first grade firefighters. (AA.019–20.)

Following settlement, the Associations amended their bylaws, adopting the Settlement’s salary definition. (AA.026–27, 29.) The City approved both bylaw amendments.

3. 2004–2005 State Auditor Reports

The State Auditor has authority to audit the Associations’ funds for compliance with statutes, bylaws, and other applicable rules. Minn. Stat. § 6.495. In 2004 and 2005, the State Auditor’s office issued letters to the Associations “identifying possible improprieties in the associations’ calculations of current salaries.” (R.Add.-2.)

For the year ending December 31, 2003, the State Auditor questioned the Police Association’s decision to pay Shift Differential in calculating compensatory time, sick leave, and vacation. (AA.090–91.) Where active police officers did not receive Shift Differential for comp time, sick leave, and vacation, the Auditor concluded that “neither should the unit value calculation for the [Police Association] include shift differential in those components.” (AA.091.) The Auditor also challenged that the Association included “new items” in its salary computations and paid out the maximum rates allowable under the collective bargaining agreement, not the “average amount paid to those top grade patrol officers who received the compensation item.” (AA.092.) The Auditor concluded that the Police Association’s calculations did not comply with its bylaws and the 1995 Settlement Agreement. (AA.090–92, 101–05.) The Auditor observed that, with its calculations, the Police Association “consistently seeks to maximize benefits for its

beneficiaries without regard to either the integrity of the fund to provide future benefits or the impact funding those benefits has on the taxpayers of the City of Minneapolis and the State of Minnesota.” (AA.91.)

Similarly, with respect to the Fire Association, the Auditor challenged the inclusion of Selection Premium when calculating vacation, sick leave, and holiday pay. (AA.125–26.) Where the City did not pay active firefighters Selection Premium for these components, the Auditor concluded that Association calculations did not reflect current firefighter salary. (*Id.*) In addition, the Auditor cited the Fire Association’s decision to use the maximum 136 hours of overtime in its unit calculation of benefits. (*Id.*) Because the Fire Association’s bylaws required the calculation to use “an average of overtime actually worked,” and the relevant firefighters only worked an average six hours of overtime, the Auditor concluded that the Fire Association’s calculations did not comply with its bylaws. (*Id.*)

4. The district court’s findings and conclusions

The district court’s findings and conclusions originate from its summary judgment, trial, and post-trial orders.

After hearing both parties’ motions for summary judgment, the district court concluded:

- The Police Association violated its bylaws by using Shift Differential in its calculation of Sick Leave Buy-Back Pay. (ADD.25.)

- The Fire Association’s overtime computation violated its bylaws by including 136 hours of overtime, instead of the average overtime actually worked by firefighters. (ADD.22.)
- Both Associations added new items to their definition of salary without amending their bylaws as required by Minn. Stat. § 69.77, as well as Minn. Stat. §§ 423B.05, subd. 2 & 423C.02, subd. 3. (ADD.20-22, 25.)

After a bench trial and post-trial motions, the Court issued its final order, incorporated its summary judgment conclusions, and held that:

- The Police Association violated its bylaws by including Shift Differential in its “calculation of the accumulated compensatory time.” (ADD.40, ¶ 18.)
- The Police Association properly included Shift Differential for 2,088 hours per year. (ADD.42, ¶ 34.)
- The Fire Association improperly included Selection Premium in calculating the Sick Leave Buy-Back Pay. This calculation violated its bylaws and Minn. Stat. § 423C.01, subd. 28, as well as Minn. Stat. § 423C.02, subd. 3, requiring the Fire Association adhere to its bylaws. (ADD.39, ¶ 13.)

In sum, the court concluded that just calculating the period from 2003 to 2009, the Police Association overpaid its beneficiaries \$35.3 million in benefits, and the Fire Association overpaid by \$17.3 million. (ADD.41, ¶¶ 27, 31.) These overpayments “resulted in an increase in [the City’s] required contributions to cover [the Associations’] respective unfunded liabilities.” (ADD.42, ¶ 35.)

The court ordered the Associations to recalculate pension benefits from June 2000 through December 2009 and resubmit their levy requests in accordance with the court's findings. (ADD.47, ¶ 2.) In addition to ordering prospective relief, the court ordered the Associations to recoup past benefit overpayments. (ADD.47, ¶ 3.) In ordering this relief, the court observed that the Associations' actuary testified that the Associations "have a fiduciary duty to collect benefit overpayments they made" to beneficiaries. (ADD.49.) The court ordered the Associations to develop a recoupment plan in accordance with "the standard of care customarily exercised by professional fiduciaries administering pension plans." (ADD.47-48, ¶¶ 3-4.) Under the court's order, none of the Associations' recouped funds will be paid to the City. The recoupment benefits the Associations' investment funds by reducing their unfunded liabilities. (ADD.48, ¶ 7.)

INTRODUCTION TO ARGUMENT

As the State Auditor determined and the district court properly confirmed, the member-controlled pension Associations have been overpaying benefits in violation of law. Minneapolis taxpayers are subsidizing this unlawful arrangement—paying millions of dollars of taxes they should not have been required to pay in order to foot the bill for benefits that the Associations should not have paid out. The Associations cannot avoid accountability for these overpayments by portraying themselves or their members as victims or invoking equitable defenses. The Associations continued their practices of overpaying benefits despite the State Auditor's 2003 and 2004 letters and the current suit. The district court judgment appropriately holds the Associations accountable for

calculating benefits correctly and remedying overpayments to which members were not entitled.

The actions of the Associations inflated the pension benefits paid and increased the financial obligation of taxpayers—imposing a real burden on City homeowners, a group that also includes retirees living on fixed incomes. For just the years 2003 to 2009, the Police Association overpaid benefits by approximately \$35.3 million and the Fire Association overpaid benefits by approximately \$17.3 million. (ADD.41, ¶¶ 27, 31.) The Police Association’s overpayments of benefits increased City taxpayers’ past financial obligations by approximately \$39.6 million and future financial obligations by an estimated \$62.4 million. (ADD.42, ¶ 39.) The Fire Association’s overpayments of benefits increased City taxpayers’ past financial obligations by approximately \$19.1 million and future financial obligations by an estimated \$24.4 million. (ADD.42, ¶ 38.) In making these overpayments, the Associations violated state law and the common-sense interpretation of their own bylaws. And the Associations disregarded the fiduciary duty that they owe to the taxpayers “who help to finance the plan.” Minn. Stat. § 356A.04, subd. 1.

STANDARD OF REVIEW

This Court reviews de novo the trial court’s legal rulings, including the grant of partial summary judgment in favor of the City and the application of law to undisputed facts. *Minnesota Voyageur Houseboats, Inc. v. Las Vegas Marine Supply, Inc.*, 708 N.W.2d 521, 524 (Minn. 2006) (stating that where district court applied law to undisputed facts, “the applicable standard of review is de novo”); *STAR Ctrs. Inc. v.*

Faegre & Benson LLP, 644 N.W.2d 72, 76 (Minn. 2002). If reasonable evidence exists to support the district court's findings of fact, an appellate court will not disturb them. *Rogers v. Moore*, 603 N.W.2d 650, 656 (Minn. 1999). "On appeal, a trial court's findings of fact are given great deference, and shall not be set aside unless clearly erroneous." *Fletcher v. St. Paul Pioneer Press*, 589 N.W.2d 96, 101 (Minn. 1999). The Associations agree that most issues in this appeal are legal issues, and that to the extent any findings of fact are in issue, they may not be set aside unless they are clearly erroneous.⁴

The granting of injunctive relief generally rests within the discretion of the trial court and will not be reversed absent an abuse of discretion. *Cherne Industrial, Inc. v. Grounds & Assocs., Inc.*, 278 N.W.2d 81, 91 (Minn. 1979).

LEGAL ARGUMENT

I. THE ASSOCIATIONS HAVE STATUTORY OBLIGATIONS TO DETERMINE PENSION BENEFITS USING THE DEFINITION OF "SALARY" IN THEIR BYLAWS.

A. State law requires that the Associations determine pension benefits based on the current salaries of active-duty officers and firefighters, using the definitions of salary in their bylaws.

The Associations are regulated by state law and have a legal duty to pay pension benefits to their members in accordance with the applicable statutory regime. Minn. Stat. § 423B.09, subd. 1; Minn. Stat. § 423C.05, subd. 1. State law requires that the Associations determine pension benefits based on the current salaries of active-duty officers and firefighters. Minn. Stat. § 423B.01, subd. 20; Minn. Stat. § 423C.01, subd. 28. Under the 1995 Settlement Agreement, the Associations amended their

⁴ Appellants' Brief at 18-19.

respective bylaws to include a definition of the term “salary” for use in the unit calculations.

The definition of the term “salary” is in the Associations’ bylaws. State law mandates that the Associations comply with the definition of “salary” that is in their bylaws. *See* Minn. Stat. § 423B.05, subd. 2 (“The affairs of the association must be regulated by its articles of incorporation and bylaws.”); Minn. Stat. § 423C.02, subd. 3 (“The board . . . shall manage, control, and operate the association, . . . according to this chapter, other applicable law, and . . . its bylaws.”); Minn. Stat. § 423C.10 (“A service pension . . . must be calculated under the laws, articles of incorporation, or relief association bylaws in effect” on the date that active employment is terminated); *see also Isaacs v. Am. Iron & Steel Co.*, 690 N.W.2d 373, 376 (Minn. Ct. App. 2004) (“Bylaws . . . must be obeyed by the corporation and its directors, officers, and shareholders.”). The Associations must calculate pension benefits in compliance with, among other things, their own bylaws. Minnesota law does not permit the Associations to act contrary to their bylaws.

The Associations’ addition of extra items to “salary” violated their bylaws. *See infra*, section II. Their additions to “salary” inflated the unit value, thereby increasing the benefits paid and the financial obligation of taxpayers. The Associations violated the statutory mandate to determine the current salary of a first grade police officer or firefighter, and to calculate the unit in compliance with the definition of salary set forth in their bylaws. *See infra*, section II.

B. State law precludes any amendments to the Associations' bylaws that increase benefits without the City's approval.

To increase the pension benefits, the Associations unilaterally expanded the definition of "salary" beyond the confines of their own bylaws, costing City taxpayers millions in unfunded liability. State law does not permit the Associations to raise their own benefits—while City and State taxpayers cover unfunded liabilities—without any financial controls. Minnesota law prescribes specific financial controls that the Associations disregarded when they unilaterally increased benefits.

The Police and Firefighters' Relief Associations' Guidelines Act provides the necessary controls against unilateral increases in benefits by member-controlled funds. Because the Associations' bylaws prescribe the definition of "salary" for calculating pension benefits, if the Associations wanted to add extra items to the definition of "salary" they must amend their bylaws. The Act requires the City's approval of any bylaw amendments that increase benefits:

Municipal approval of benefit changes required. *Any amendment to the bylaws or articles of incorporation of a relief association which increases or otherwise affects the retirement coverage provided by or the service pensions or retirement benefits payable from any police or firefighters' relief association enumerated in subdivision 1a is not effective until it is ratified by the municipality in which the relief association is located. The officers of the relief association shall not seek municipal ratification before obtaining either an updated actuarial valuation including the proposed amendment or an estimate of the expected actuarial impact of the proposed amendment prepared by the actuary of the relief association and submitting that actuarial valuation or estimate to the clerk of the municipality.*

Minn. Stat. § 69.77, subd. 11 (emphasis added).⁵

Before any increase or change in pension benefits, the statute requires that the Associations: (1) obtain an actuarial report or estimate of the actuarial impact of the change, (2) amend their bylaws, and (3) obtain City approval before any such change can become effective. The district court appropriately read this statute, concluding that “if [the Associations] want to increase the benefits paid to their beneficiaries, i.e. add new items to be included in the definition of salary, [they] must amend their respective bylaws or articles of incorporation, and [the City] must ratify such change in benefits.” (ADD.20.) Because the Associations did not follow the necessary procedure to increase benefits, the addition of “new items” to their definitions of salary was illegal and void.

The Associations attempt to confer on themselves a unilateral right to increase benefits without any oversight by pointing to language in their bylaws that says any new items of compensation granted in the collective-bargaining agreements “may be included in salary by action of” the Associations. This Court should reject the Associations’ attempt to interpret their bylaws in a manner that conflicts with state law. The trial court correctly discarded the Associations’ argument, reasoning that “[w]hile the bylaws do provide that new items of compensation ‘may be included in the salary by action’ of the

⁵ The Associations use an ellipsis to omit language from their block quote of section 69.77, subdivision 11. (App. Br. at 20.) The Associations’ ellipsis omits the phrase, “*or the service pensions or retirement benefits payable from any police or firefighters’ relief association,*” from the statute. Minn. Stat. § 69.77, subd. 11 (emphasis added). Putting the omitted language back in the statute, it plainly reads that any amendment to the bylaws which increases retirement benefits payable from any association is not effective until it is ratified by the municipality. *Id.* Since the Associations’ bylaws define “salary” for calculating pension benefits, bylaw amendments were necessary to add any extra items to salary to increase benefits.

[Associations], nothing in the bylaws says that the process outlined in Minnesota Statutes § 69.77, requiring board action and then City ratification, can be circumvented.” (ADD.21.) It is entirely consistent with the plain language of the bylaws to insist that the Associations must comply with state law. The Associations may seek to add new items of compensation. The action, however, must include a bylaw amendment, subject to City approval.

The Associations may not ignore or rewrite the financial controls provided by statute. Their bylaws must be construed in a way that makes them legal. Courts construe bylaws according to the rules governing the construction of contracts and statutes. *Isaacs*, 690 N.W.2d at 376. “Whenever possible, a contract must receive a construction that will make it lawful, and where there is a choice between a construction of illegality and one of legality, an intended contractual course of legality is to be presumed in the absence of proof of a purpose to the contrary.” *Indianhead Truck Line, Inc. v. Hvidsten Transp., Inc.*, 128 N.W.2d 334, 341 (Minn. 1964). The bylaws, therefore, must be construed to mean that the “action” meets the underlying requirements of state law.

The Associations ignore the fundamental requirement that their affairs be regulated by their articles and bylaws. *See* Minn. Stat. § 423B.05, subd. 2; Minn. Stat. § 423C.02, subd. 3; Minn. Stat. § 423C.10. The Associations’ bylaws prescribe the formula for calculating “salary.” The historical absence of bylaw definitions led to mischief and the 1995 lawsuit—which was settled by establishing these very bylaws. If the Associations want to change the formula to add new items to the definition of “salary”—thereby changing the financial obligations of City taxpayers—Chapters 423B

and 423C require bylaw amendments. And Minnesota Statutes § 69.77 dictates that the Associations may not amend their bylaws without an actuarial analysis and the City's ratification. The district court appropriately recognized that the Associations' violation of Minnesota Statutes § 69.77 does not result from their failure to amend their bylaws; rather, it stems from the Associations' "calculation of pension benefits that is contrary to the definition of salary contained in their bylaws." (ADD.43, ¶ 4; *see also* ADD.20.)

Section 69.77 provides a check against pensioners unilaterally changing their benefit formulas to increase benefits and the taxpayer obligation to underwrite the increases. It is irrelevant that the pension benefits increase, without bylaw amendments, every time the hourly rate of pay for active officers and firefighters increase. This is akin to a cost-of-living adjustment, much like the statutory cost-of-living adjustment in the State's PERA pension plan. The statutory regime allows for a benefit increase matched to the rate-of-pay increase for active employees. But the statutory regime does not allow the Associations to deviate from the bylaw formula for "salary" to increase benefits by changing the formula itself—adding extra items into the calculation.

Contrary to what the amicus curiae Minneapolis Retired Police Officers' Association says, the City does not control pension-benefit levels by negotiating the collective-bargaining agreement. First, the Public Employment Labor Relations Act prohibits the City and the unions from negotiating pension benefits. *See* Minn. Stat. § 179A.07, subd. 2 (describing a public employer's obligation to meet and negotiate with a public employee representative regarding the "terms and conditions" of employment); Minn. Stat. § 179A.03, subd. 19 (defining employment "terms and conditions" as

excluding “retirement contributions”). Second, but for the statutory regime outlined above, the City would have no control over which components of a collective-bargaining agreement that the Police Association elects to call “salary” or how it chooses to value those components.

C. The Associations had notice of a claim that they had violated Minnesota Statutes § 69.77.

The Associations wrongly argue that the complaint did not sufficiently plead a violation of Minnesota Statutes § 69.77 and incorrectly contend that “the district court did not address the issue of pleading.” (App. Br. 1.) In fact, the district court found that the Associations had notice of the claim. (ADD.20, at n.12.) Courts construe pleadings liberally in favor of the pleader and judge them by their substance and not their form. *Basich v. Bd. of Pensions of ELCA*, 493 N.W.2d 293, 295 (Minn. Ct. App. 1992). The district court noted that the complaint contains “several references to ‘violation of legal duties,’ ‘inconsistent with labor agreements,’ ‘violation of Minnesota Statutes,’ and specific reference to Minn. Stat. § 69.77.” (ADD.20, at n.12.) For example, the complaint alleged that the Associations “have acted contrary to the Police and Firefighters’ Relief Association Guidelines Act, Minn. Stat. § 69.77, and other applicable laws.” (AA.075, compl. ¶ 24.) The district court correctly concluded that the Associations had notice of a claim that they had violated Minnesota Statutes § 69.77.

II. THE ASSOCIATIONS OVERPAID BENEFITS BY ADDING EXTRA SALARY COMPONENTS AND MISCALCULATING SALARY COMPONENTS CONTRARY TO THEIR BYLAWS AND IN VIOLATION OF THEIR STATUTORY OBLIGATIONS.

A. The Police Association violated its bylaws by adding extra items and miscalculating components contrary to the definition of “salary” in its bylaws.

In its bylaws, the Police Association identifies specific items of compensation for its definition of salary. (RA.12–13.) In addition to the items listed in its bylaws, however, the Police Association improperly added the following compensation items to its definition of salary for purposes of calculating pension benefits: (1) Vacation Credit Pay, (2) Performance Premium, (3) Holiday Pay, (4) Corporal Pay, and (5) Overtime. (ADD.21; ADD.41, ¶ 29.) When changing the definition of salary, the Police Association did not provide the City with a report of the actuarial impact of the changes and did not present a proposed bylaw amendment to the City for ratification. The district court appropriately held that these five items that the Police Association added are contrary to the Police Association’s bylaws. (ADD.21; ADD.41, ¶ 29.)

Furthermore, for purposes of calculating pension benefits, the Police Association miscalculated two components of the definition of salary contrary to its bylaws. First, the Police Association violated its bylaws by including Shift Differential on the Sick Leave Buy-Back Pay component of salary in its calculation of the pension benefit. (ADD.41, ¶ 30; ADD.24.) Second, the Police Association violated its bylaws by including Shift Differential on the Compensatory Time Cash Out component of salary in its calculation of the pension benefit. (ADD.40–41, ¶¶ 18, 33.) Under the Police Association’s bylaws,

salary may only include these items to the extent that they are payable under the collective-bargaining agreement; and under the collective-bargaining agreement, the Shift Differential is payable only for hours worked. (RA.13.) Neither Sick Leave Buy-Back Pay nor Compensatory Time Cash Out represent hours worked. So Shift Differential may not be included in the calculation of those components of salary.

Police officers who work a night shift are entitled to additional pay called Shift Differential. The collective-bargaining agreement defines Shift Differential as follows: “Employees in the Department *who work a scheduled shift* in which a majority of the work hours fall between the hours of 6:00 p.m. and 6:00 a.m., *shall be paid a shift differential . . . for all hours worked on such shifts.*” (RA.74 (emphasis added).) By definition, Shift Differential is payable only for “hours worked.” (*Id.*) The Police Association’s bylaws define salary to include Sick Leave Buy-Back Pay, Compensatory Time Cash Out, and Shift Differential “to the extent they are payable under a collective-bargaining agreement[.]” (RA.13.)

The City does not pay police officers Shift Differential as a part of Sick Leave Buy-Back Pay or Compensatory Time Cash Out because they do not constitute hours worked. (RA.327–30; RA.74 (shift differential paid for “hours worked”).) But the Police Association included Shift Differential in calculating both of these components of salary. (RA.323–24.) By doing so, the Police Association increased the pension benefits.

Sick Leave Buy-Back Pay is a mechanism to allow officers to cash in some portion of their unused sick leave. The collective-bargaining agreement allows a police officer who has accumulated at least 480 hours of sick leave to receive payment for

accrued but unused sick leave. (RA.112–14.) Under the collective-bargaining agreement, accrued sick leave does not represent hours worked. But the Police Association includes Shift Differential in the hourly rate when calculating Sick Leave Buy-Back Pay.

Compensatory Time Cash Out is a mechanism to liquidate a police officer's bank of unused, accumulated compensatory time. An officer who works overtime may elect to be compensated in time off at a rate of 1.5 hours of compensatory time for each hour of overtime worked. (RA.87–88, § 10.02, subd. (b).) Officers who work overtime accumulate compensatory time throughout the year. Once per year, the City liquidates each officer's entire compensatory-time bank by making a cash payment. (*Id.*, subd. (c).) Compensatory Time Cash Out is not payment for hours worked. Therefore, the City does not include Shift Differential in the cash payment for this item of compensation. But the Police Association includes Shift Differential in the hourly rate when calculating Compensatory Time Cash Out.

The district court correctly concluded that the Police Association violated its bylaws by including Shift Differential on the Sick Leave Buy-Back Pay and the Compensatory Time Cash Out components of salary in the calculation of pension benefits. (ADD.40–41, ¶¶ 18, 30, 33; ADD.24.)

B. The Fire Association violated its bylaws by adding extra items and miscalculating components contrary to the definition of “salary” in its bylaws.

In its bylaws, the Fire Association identifies six specific items of compensation in the definition of “salary.” (RA.46 (listing items (a) through (f) in the definition of “salary”).) In addition to the items listed in its bylaws, however, the Fire Association

improperly added the following compensation items to its definition of salary for purposes of calculating pension benefits: (1) Health Club Dues, (2) Vacation Credit Pay, (3) Work Out of Grade, (4) Performance Pay, and (5) Holiday Pay. (ADD.21; ADD.41, ¶ 25.) When changing the definition of salary, the Fire Association did not provide the City with a report of the actuarial impact of the changes and did not present a proposed bylaw amendment to the City for ratification. The district court appropriately held that these five items that the Fire Association added are contrary to the Fire Association's bylaws. (ADD.21; ADD.41, ¶ 25.)

Furthermore, when determining pension benefits, the Fire Association miscalculated two components of the definition of salary contrary to its bylaws. First, the Fire Association violated its bylaws by including Selection Premium on the Sick Leave Buy-Back Pay component of salary in its calculation of the pension benefit. (ADD.41, ¶ 28.) Second, the Fire Association artificially inflated the benefits calculation by including the maximum amount of non-FLSA overtime (136 hours), rather using the *average* of non-FLSA overtime hours *actually worked*, as required in the bylaws. (ADD.41, ¶ 26; ADD.22.)

Selection Premium is additional pay for employees working in the job title of firefighter. The collective-bargaining agreement defines Selection Premium as follows: "A selection premium shall be payable in the amount and on the terms specified in the Salary Schedule . . . The selection premium *shall be payable only to employees working in the job title of Fire Fighter.*" (RA.199 (emphasis added).) By definition, Selection Premium is payable only for hours worked. (*Id.*) For the purpose of calculating benefits,

the Fire Associations' bylaws define salary to include Sick Leave Buy-Back Pay and Selection Premium "to the extent they are payable under a collective-bargaining agreement[.]" (RA.46.)

The City does not pay firefighters Selection Premium as part of Sick Leave Buy-Back Pay because those credits are not hours worked. (RA.342-43.) Sick Leave Buy-Back Pay for firefighters, like police officers, is a mechanism to allow firefighters to cash in accrued but unused sick leave. (RA.203-04.) By definition, Sick Leave Buy-Back Pay is not compensation for hours worked. But the Fire Association includes Selection Premium in its calculation of this component of salary.

Firefighters are eligible for two types of overtime payments under the collective-bargaining agreement. First, firefighters are paid overtime for every hour that their work shift exceeds the FLSA's straight-time hours maximum. (RA.201.) This type of overtime is known as FLSA Overtime and firefighters qualify for this because they regularly work 24-hour shifts. Second, firefighters are paid overtime when they are required to work beyond their scheduled shifts (e.g., they are held over past the end of the shift or are required to report early for a shift). (*Id.*) This second type of overtime is known as Non-FLSA Overtime and is the subject of dispute in this case.

For the purpose of calculating benefits, the Fire Association's bylaws define salary to include, "to the extent they are payable under a collective bargaining agreement," the following: "*an average of overtime actually worked* in excess of FLSA overtime amounts by firefighters with 25 years or more of service, *up to a maximum* of 136 hours, in the immediately preceding year[.] (RA.46 (emphasis added).) The plain language of the

bylaws requires the Fire Association to use an average of Non-FLSA Overtime hours “actually worked” by 25-year firefighters in the preceding year. (*Id.*) But the Fire Association simply inserts the maximum number of hours, 136, in its calculation each year, without regard to average of such overtime “actually worked” in the preceding year. (RA.281; RA.321–22.)

It is undisputed that in recent years the average Non-FLSA Overtime hours actually worked by 25-year firefighters is not even close to 136 hours. (AA.126.) In 2003, for example, only two of the 25-year firefighters worked overtime, and the average was only six hours. (*Id.*) Nevertheless, the Fire Association included 136 hours of Non-FLSA Overtime, resulting in the addition of \$4.31 to the unit value. (AA.125.) The State Auditor calculated that using 136 hours, instead of the average overtime hours actually worked (six hours), results in a net increase in unit value of \$4.12 or \$2,076 per year for members receiving 42 units. (AA.126.) The district court correctly found that the Fire Association “admits that it always uses 136 hours in its calculation, without regard to what hours were actually worked in the previous year. . . . This is contrary to the express language contained in the bylaws.” (ADD.22.)

III. THE CITY HAS NOT WAIVED—NOR CAN IT BE ESTOPPED FROM ASSERTING—THE STATUTORY REQUIREMENT THAT THE ASSOCIATIONS DETERMINE PENSION BENEFITS CONSISTENT WITH THEIR BYLAWS AND STATE STATUTES.

- A. The City is not estopped from claiming that the Associations must determine benefits in accordance with their own bylaws and state statutes.**

The Associations attempt to evade their accountability for violations of law by asserting that the City should be estopped from pursuing its claims. But government entities may not be estopped on the same terms as any other party. To estop the City, the Associations must establish the traditional elements of estoppel and that the City's conduct amounts to "wrongful conduct." *Brown v. Minnesota Dept. of Pub. Welfare*, 368 N.W.2d 906, 910 (Minn. 1985); *Ridgewood Dev. Co. v. State*, 294 N.W.2d 288, 292-93 (Minn. 1980). The City may be estopped only if it committed affirmative misconduct. *Concept Props., LLP v. City of Minnetrista*, 694 N.W.2d 804, 821 (Minn. Ct. App. 2005) ("a governmental entity will be estopped only if it committed affirmative misconduct"); *In re Westling Mfg., Inc.*, 442 N.W.2d 328, 332 (Minn. Ct. App. 1989) ("affirmative misconduct is required to estop the government"). "[T]hose who deal with the Government are expected to know the law and may not rely on the conduct of Government agents contrary to law." *Heckler v. Cmty. Health Servs. of Crawford*, 467 U.S. 51, 63 (1984); accord *Brown*, 368 N.W.2d at 912 (same). Because the Associations have no evidence of "affirmative misconduct" by the City, their argument for estoppel fails. Evidence of negligence or mistake does not rise to the level of affirmative

misconduct. *Prairie Island Indian Cmty. v. Minnesota Dep't of Pub. Safety*, 658 N.W.2d 876, 890 (Minn. Ct. App. 2003).

The City may not be estopped from enforcing the law and protecting taxpayers. Both the Minnesota Supreme Court and Court of Appeals have ruled that even when a government entity has presumably blessed an individual's entitlement to benefits—by its inattention or inactivity—in excess of what is authorized by law, the government is not estopped by that conduct from later denying entitlement to (and attempting to recover) those benefits. *See, e.g., Axelson v. Minneapolis Teacher's Ret. Fund Assoc.*, 544 N.W.2d 297 (Minn. 1996); *Bd. of Educ. of City of Minneapolis v. Sand*, 34 N.W.2d 689 (Minn. 1948); *In re Application for PERA Ret. Benefits of McGuire*, 756 N.W.2d 517 (Minn. Ct. App. 2008). When the law establishes duties, compliance with those duties “may not be the subject of a waiver or estoppel.” *Town Bd. of Marshan v. City of Hastings*, 298 N.W.2d 353, 356 (Minn. 1980); *see also Haak v. Bd. of Educ. of I.S.D. No. 625*, 367 N.W.2d 461, 464 (Minn. 1985) (holding that neither waiver nor estoppel precluded a school board from bringing claims regarding compliance with statutory requirements). These cases soundly defeat the Associations' estoppel and waiver arguments.

In *McGuire*, a retired city administrator appealed the decision of the Public Employees Retirement Association (“PERA”) to rescind his annuity payments. The PERA began paying benefits to the appellant in May 2005, and in July 2007, the PERA notified him that it would cease paying him and recover past payments of over \$100,000. The PERA's reason for terminating and recovering benefits was that the appellant had violated a statutory requirement that, in order to be eligible for benefits, an employee

must be completely and continuously separated from employment for 30 days. Despite the fact that the appellant had received benefits for more than two years *and* despite the fact that he specifically asked the PERA the very question that, if answered correctly by the PERA, could have avoided the improper payment, the Court ruled consistently with past decisions that the PERA was not estopped from rescinding and recovering the erroneous payments:

Minnesota courts have long held that estoppel cannot be applied when doing so would cause an agency to act outside the bounds of its authority. . . . The supreme court adopted this rule out of concern that a contrary rule would lead to chaos: *absent a prohibition against estoppel, states and municipalities would repeatedly find themselves bound by the unauthorized acts of officers and agents possessing only limited authority. . . . [R]egardless of the equities involved, a government agency's unauthorized act cannot be made effective by estoppel.*

McGuire, 756 N.W.2d at 519–20 (emphasis added) (citations omitted).

In *Sand*, the Minneapolis Board of Education brought an action to determine a teacher's status and eligibility for tenure under state law. For a number of years, the school district took steps indicating an intention to preserve the teacher's tenure rights. The teacher argued that, regardless of whether he had tenure rights under the law, he nevertheless acquired those rights because the school board represented that he had. The Supreme Court rejected this argument and held that the teacher could only have tenure consistent with that authorized by law:

School boards and school districts have only such powers as are granted by statute. Teacher tenure is the creature of statute, and no one can have a valid claim to tenure except as authorized by statute. *Estoppel cannot be invoked to confer upon a political subdivision of the state governmental power otherwise lacking.*

Sand, 34 N.W.2d at 695 (emphasis added). In *Axelson*, the Supreme Court similarly ruled that estoppel did not apply against the government. In that case, the Minneapolis Teachers' Retirement Fund Association ("MTRFA") denied a teacher's request to purchase retirement service credits for years when he was on a leave of absence. Challenging the denial, the teacher argued that he had relied on the representations of the MTRFA that he could purchase the credits at a later date. Finding no statutory authority and no authority in the plan documents to create such benefits, the Supreme Court reversed the Court of Appeals and held that "the doctrine of promissory estoppel is not applicable to Axelson's claims and therefore does not prevent the MTRFA from denying Axelson the right to purchase the retirement service credits." *Axelson*, 544 N.W.2d at 302.

Here, under the 1995 Settlement Agreement, the Associations amended their respective bylaws to include a definition of the term "salary" for use in the unit calculation for pension benefits. The Associations have a legal duty to calculate benefits in compliance with their own bylaws and may not determine salary inconsistent with the bylaws. State law prohibits the Associations from adding new items to the salary calculation without amending their bylaws and obtaining the City's ratification. Minn. Stat. § 69.77, subd. 11. The Associations must comply with these legal duties regardless of the City's past adoption of the tax levies.

The City had no authority to stop the tax levy of the full amount that the Associations certified. State law provides that if the municipality does not include the full amount of the minimum obligation of the municipality in the levy, the county auditor

must spread a levy in the amount of the deficiency certified by the Associations. Minn. Stat. § 69.77, subds. 5, 7(c). Indeed, when the City objected to funding the overpayments included in the 1995 levy certified by the Associations, they simply went to the County Auditor, who levied the full amount despite the City's objections. (AA.011-13.) This Court previously recognized that "the county auditor is required to levy whatever amount is certified by the association[s] and cannot provide the city with a remedy." (R.Add.-4.)

Even assuming for the sake of argument that the City improperly levied the taxes or failed to object, this conduct does not estop the City from claiming past violations or from seeking relief to require the Associations' compliance with their statutory and other legal obligations. *See Doris v. Police Comm'r of Boston*, 373 N.E.2d 944 (Mass. 1978) (holding that a city is not estopped from enforcing statutes due to its previous failure to attempt to enforce statutory provisions). Furthermore, any alleged acquiescence by City finance staff that the Associations' calculations were correct for the period between 1999 and 2003 is not binding on the City and also does not estop the City from attempting to rectify the Associations' past violations of the law. As the *McGuire* Court emphasized, the City cannot be estopped based on the actions of its employees. If they were estopped by such acts, municipalities would "repeatedly find themselves bound by the unauthorized acts of officers and agents." 756 N.W.2d at 519-20. City staff had no authority to waive the requirements of Minnesota Statutes § 69.77, and the City cannot be estopped from enforcing state law. No evidence indicates that the City's conduct amounted to "wrongful conduct." *Brown*, 368 N.W.2d at 910. The law could not be any clearer that the City staff's failure to recognize or identify the Associations' unlawful

salary calculations is not subject to estoppel. The courts' unambiguous holdings on this issue lead to only one conclusion: nothing the City did (or failed to do) would be legally effective to relieve the Associations of their present legal duties to determine benefits in compliance with the applicable bylaws and statutes.

The Associations, by asserting equitable defenses as a complete bar, are essentially claiming that if they broke the law, they did so for so long before being sued that their illegal acts are now legal and they have the right to continue to overpay benefits at taxpayer expense. As a matter of law, just because the Associations did not get caught violating the law in the past does not make illegal acts legal. Thus, the trial court correctly denied their motion for summary judgment.

B. The City has not waived its claims.

This Court should reject the Associations' arguments that the City waived its right to object to their unlawful salary calculations. The Associations have failed to show, as a matter of law, that the City waived any rights to object to their salary calculations. A waiver is an "intentional relinquishment of a known right, and it must clearly be made to appear from the facts disclosed." *Hauenstein & Bermeister v. Met-Fab Indus., Inc.*, 320 N.W.2d 886, 892 (Minn. 1982) (quotations omitted). The burden of proving waiver rests on the Associations. *Illinois Farmers Ins. Co. v. Glass Serv. Co.*, 683 N.W.2d 792, 798 (Minn. 2004) ("party alleging waiver must provide evidence that the party that is alleged to have waived the right possessed both knowledge of the right in question and the intent to waive that right").

The Associations did not meet their burden of proving the City's knowledge and intent to waive its rights. Nothing in the record supports the Associations' argument that the City "intentionally relinquished" any "known right." Instead, the facts show that after the City staff discovered the Associations' improper—and illegal—salary calculations in 2004, they diligently pursued an investigation of the practices and notified the Associations of their disagreement with the salary determinations. (ADD.15; RA.327–30; RA.342–45.) Thus, the City's intent beginning in 2004 is not a "clear and convincing" indication that the City intended to waive its right to object. While City staff had not identified the Associations' unlawful practices before 2004, this certainly did not rise to the level of a "voluntary relinquishment" of the right of the City to later challenge these practices. And again, the City had no right to stop the tax levy of the full amount that the Associations certified because "the county auditor is required to levy whatever amount is certified by the association[s] and cannot provide the city with a remedy." *Minneapolis Police Relief Ass'n*, 2008 WL 1747923, at *4 (R.Add.-4). The district court correctly concluded that the City did not waive its rights. (ADD.14.)

Even if this case involves claims between governmental entities, contrary to the Associations' contention, it does not lead to the conclusion that the City has waived its right to bring the current claims. Their reliance on *LOGIS v. Village of New Hope* is misplaced because that case involved claims by the city of New Hope arising out of a joint powers agreement with several other cities and the court restricted its holding to that factual scenario. 248 N.W.2d 316, 321 (Minn. 1976) ("when considering the relationship of municipalities with one another under a joint powers agreement"). This case does not

involve a joint powers agreement, so the *LOGIS* decision does not apply. Furthermore, the other cases cited by the Associations actually support the City's position that it did not waive any rights to assert its present claims.

In *Marshan*, the Supreme Court held that a city was not estopped from asserting that a township had failed to file objections to the annexation of land within the required 60-day statutory period because the “prerequisites that entitled one to a hearing before the Board are fixed by law and may not be the subject of waiver or estoppel.” 298 N.W. at 356 (emphasis added). Similarly, in *Haak*, the Supreme Court again concluded that neither waiver nor estoppel precluded claims by a governmental body regarding a failure to comply with certain statutory requirements. 367 N.W.2d at 464 (holding that neither waiver nor estoppel precluded the school board from asserting that appellants were not “teachers” under state law). Because the Associations’ duties to determine benefits are governed by state statute and by their own bylaws, those legal requirements may not be the subject of waiver or estoppel. *Marshan*, 298 N.W.2d at 356.

IV. THE CITY’S LAWSUIT TO ENFORCE THE ASSOCIATIONS’ BYLAWS AND STATE STATUTES IS NOT BARRED BY THE STATUTE OF LIMITATIONS OR LACHES.

A. The statute of limitations does not bar the City’s claims.

The district court properly rejected the Associations’ statute-of-limitations defense. The Associations have a ministerial legal duty—every year—to calculate pension benefits in compliance with the statute and their own bylaws. The new items that the Associations added to the definition of “salary” without a bylaw amendment violated the statutory regime. Each time, each year that the Associations breach their duties

constitutes a new violation of law for which the City may seek redress in the courts. *See Honn v. Nat'l Computer Sys., Inc.*, 311 N.W.2d 1, 2 (Minn. 1981) (“Where a money obligation is payable in installments, the general rule is that a separate cause of action arises on each installment and the statute of limitations begins to run against each installment when it becomes due.”); *Windschitl v. Windschitl*, 579 N.W.2d 499, 501 (Minn. Ct. App. 1998) (same); *Warner v. First Nat'l Bank*, 236 F.2d 853, 862 (8th Cir. 1956) (holding that, in the context of a series of wrongful acts committed at different times, the statute of limitations begins to run “upon each wrongful act at the time that it is committed”). This is not a matter of contract rights between private parties. It is a matter of repeated violations of law—law designed to protect taxpayers from the unchecked increases in liability. The Associations cannot acquire a vested right to violate the law now and in the future by simply getting away with it in the past. The trial court correctly held that the City acquired a cause of action each time that the Associations calculated pension benefits using a definition of salary contrary to their bylaws. (ADD.44, ¶ 6.) This Court should affirm district court’s determination that statute of limitations does not bar the City’s claims regarding any calculation of pension benefits that the Associations submitted after June 9, 2000. (ADD.44.)

B. The doctrine of laches does not bar the City’s claims.

Nothing in the record supports the Associations’ contention that the City delayed in asserting a “known right” at their expense. “Laches is an equitable doctrine applied to ‘prevent one who has not been diligent in asserting a known right from recovering at the expense of one who has been prejudiced by the delay.’” *Winters v. Kiffmeyer*, 650

N.W.2d 167, 169 (Minn. 2002) (quoting *Aronovitch v. Levy*, 56 N.W.2d 570, 574 (Minn. 1953)); see also *Gadey v. City of Minneapolis*, 517 N.W.2d 344, 348 (Minn. Ct. App. 1994) (same). The question is “whether there has been such an unreasonable delay in asserting a known right, resulting in prejudice to others, as would make it inequitable to grant the relief prayed for.” *Winters*, 650 N.W.2d at 170 (quoting *Fetsch v. Holm*, 52 N.W.2d 113, 115 (Minn. 1952)). Laches does not apply here because the City diligently pursued the Associations’ improper salary calculations after the State Auditor and City staff discovered them.

The City first discovered that the Associations were improperly calculating the base salary components in 2004, upon receipt of the State Auditor’s Management Letters. (ADD.15; RA.346; RA.350–52; RA.259–78; RA.279–87.) The district court correctly found that the City did not unreasonably delay in asserting a known right:

[The City] filed this suit on June 9, 2006, two years after [the City] discovered [the Associations’] miscalculation of pension benefits and after attempts to resolve the issues were unsuccessful. While there was a delay in the time from discovery to filing, there is no evidence said delay was unreasonable under the circumstances.

(ADD.43, ¶ 4.)⁶ The City’s attempts to resolve this matter without litigation should not be used against it. Moreover, as a matter of law the Associations cannot argue that they are prejudiced by the City’s insistence that they comply with their legal duties to determine benefits. This Court should affirm the district court’s determination that laches does not bar the City’s claims. (ADD.15; ADD.43.)

⁶ The district court’s findings of fact should receive “great deference,” and must “not be set aside unless clearly erroneous.” *Fletcher*, 589 N.W.2d at 101.

V. THE DISTRICT COURT DID NOT ABUSE ITS DISCRETION WHEN IT GRANTED INJUNCTIVE RELIEF TO CORRECT THE BENEFIT CALCULATIONS AND REQUIRED THE ASSOCIATIONS TO DEVELOP A PLAN FOR RECOUPING PAST OVERPAYMENTS.

In its complaint, the City sought a permanent injunction and declaratory relief to redress the Associations' alleged overpayments. (AA.069, ¶ 1.) Minnesota's Uniform Declaratory Judgments Act authorizes a court to grant such relief "whenever necessary or proper." Minn. Stat. § 555.08. The district court's grant of such equitable relief can be reversed only for an abuse of discretion. *Cherne*, 278 N.W.2d at 91 ("The granting of an injunction generally rests within the sound discretion of the trial court, and its action will not be disturbed on appeal, unless, based upon the whole record, it appears that there has been an abuse of such discretion.").

District courts are accorded "broad latitude in fashioning remedies to meet the particular needs of each case." *Bolander v. Bolander*, 703 N.W.2d 529, 548 (Minn. Ct. App. 2005). Indeed, the Minnesota Supreme Court has observed that equitable remedies must have flexibility to meet the requirements of each particular case:

A court of equity has the power to adapt its decree to the exigencies of each particular case so as to accomplish justice. It is traditional and characteristic of equity that it possesses the flexibility and expansiveness to invent new remedies or modify old ones to meet the requirements of every case and to satisfy the needs of a progressive social condition.

Beliveau v. Beliveau, 14 N.W.2d 360, 366 (Minn. 1944).

A court may grant permanent injunctive relief when a party has no adequate legal remedy and an injunction is necessary to prevent great and irreparable injury. *Jackel v. Brower*, 668 N.W.2d 685, 688 (Minn. Ct. App. 2003). As a general rule, the district court

may exercise its sound discretion in granting a permanent injunction. *See Standard Oil Co. v. Bertelsen*, 243 N.W. 701, 702 (Minn. 1932). A court, however, “has no discretion to deny a permanent injunction where the facts proved at trial require such relief.” *Theros v. Phillips*, 256 N.W.2d 852, 859 (Minn. 1977).

Applying these standards, the district court found the Associations’ overpayments “caused great and irreparable harm” to the City and the City had no adequate remedy at law to redress the Associations’ present or past overpayments. (ADD.42, ¶ 37, ADD.44, ¶ 9.) Accordingly, the court ordered the Associations to recalculate pension benefit unit values and submit a corrected 2010 levy request. (ADD.48, ¶ 6.) In addition, the court directed the Associations to recoup benefit overpayments made to members and beneficiaries from June 9, 2000 to the date the benefits are corrected. (ADD.45, ¶ 13.) The Associations must establish their own recoupment programs applying “the standard of care customarily exercised by professional fiduciaries administering pension plans in recouping overpayments.” (ADD.47, ¶ 3.) The injunctive order was the logical result of the district court’s findings and was in no manner an abuse of discretion.

A. The district court’s prospective relief order, requiring a correction of benefit calculations and current and future levy requests, was proper and well within the court’s discretion.

After ruling that the City met the requirements for a permanent injunction, the law required that the court enjoin the Associations to correct their calculations going forward. First, the district court properly determined the City had no adequate remedy at law. *Jackel*, 668 N.W.2d at 688. The district court concluded, and this Court affirmed, that Minnesota Statutes § 69.77 does not provide the City with any administrative remedies.

Minneapolis Police Relief Ass'n, 2008 WL 1747923, at *3 (R.Add.-4) (“We conclude that there are no administrative remedies available to the city under Minn. Stat. § 69.77.”)

Second, the district court described the great and irreparable harm facing the City if the Associations’ overpayments continued unchecked. (ADD.46, ¶ 20.) Specifically, the court cited evidence that Police Association overpayments increased the City’s future obligations by an estimated \$62.4 million, and Fire Association overpayments increased future obligations by an estimated \$24.4 million. (ADD.42, ¶¶ 38-39.) The court accurately concluded that continuing overpayments would “exponentially and improperly compound [the City’s] minimum obligations.” (ADD.46, ¶ 20.)

In contrast, the Associations can easily and inexpensively comply with the district court’s injunction. James Michels, who personally calculates the Associations’ unit values, testified that he could correct the unit valuations in a matter of hours. (Tr. 92:18-20; ADD.38, ¶ 4 n.2.)

Having made these findings, the district court did not abuse its discretion in ordering that the Associations correct their salary calculations to comply with the law and their bylaws.

B. The district court’s order, requiring the Associations to develop recoupment plans in accordance with the standard of care required by retirement plan fiduciaries, was proper and not an abuse of discretion.

In addition to ordering prospective relief, the district court ordered that the Associations develop a plan to recoup past overpayments from beneficiaries for the

benefit of their investment funds.⁷ The district court did not dictate the recoupment plans' elements other than to require that the Associations comply with the standards of care of plan fiduciaries. (ADD.47, ¶¶ 3–4.) The district court emphasized that Police Association overpayments increased the City's past financial obligations by approximately \$39.6 million, and Fire Association overpayments increased past obligations by approximately \$19.1 million. (ADD.42, ¶¶ 38–39.) In addition, the court correctly concluded the City had "no adequate remedy at law for [the Associations'] past overpayments." (ADD.44, ¶ 9.)

The district court properly rejected the Associations' argument that Minnesota Statutes § 69.77 provides an "adequate remedy at law," for past overpayments "of benefits to individual members and beneficiaries." (ADD.44, ¶ 9.) Section 69.77, subd. 8, provides that excess contributions by the City must be used to "amortize any unfunded actuarial accrued liabilities of the relief association." The point lost on the Associations, but not on the district court, is that there are no excess contributions. The Associations' failure to lawfully calculate benefits inflated the City's contributions, but those contributions were spent in the form of benefits that the beneficiaries were never entitled to receive. There are no excess contributions left to be amortized. Recovering contributions from the investment funds would only create a deficit that the City and its taxpayers would have to re-fund. (AA.180:20–24.) It would be the equivalent of the City

⁷ The district court expressly concluded that the City was not entitled to recover past excess contributions. (ADD.46, ¶17.) Any recouped overpayments will be kept for the exclusive benefit of the Associations' investment funds. The City never intended to recover overpayments for the City's treasury and has not appealed the district court's ruling on this issue.

immediately endorsing the check for any returned contributions back to the Associations. The district court understood that § 69.77, subd. 8, provides no adequate remedy and properly ordered the Associations to formulate plans to recoup past benefit overpayments.⁸

Recoupment is standard practice for retirement plans to recover past overpayments by reducing future benefits. *See, e.g., In re Disability Earnings Offset of Masson*, 753 N.W.2d 755, 756, 761 (Minn. Ct. App. 2008) (allowing 25 percent benefit reduction under PERA until overpayments recovered). The remedy is available without regard to the reason for the overpayment. *Teater v. SDM Eng'g Plastics*, No. 05-5779, 2006 U.S. Dist. LEXIS 28291, at *7–8 (E.D. Pa. May 11, 2006) (ERISA plan permits setoffs “to recoup overpayments caused by its own mistake”); *In re Delacruz*, 300 B.R. 669, 685 (Bankr. E.D. Mich. 2003) (permitting plan to recoup overpayments from future disability benefit payments); *Hoffa v. Fitzsimmons*, 673 F.2d 1345, 1354 (D.D.C. 1982) (“[W]hen a trustee overpays a beneficiary the trustee is entitled to recover the excess payment, even when it was the product of unilateral mistake on the part of the trustee.”). The district court’s order to recoup the overpayments mirrors an established equitable remedy, so routine as to be unremarkable, and falling well within the bounds of the court’s discretion.

⁸ Guidance for recoupment plans can be found in the regulations of the Pension Benefit Guarantee Corporation (PBGC). The PBGC regulations provide for recouping benefit overpayments only from future benefit payments with no more than a 10% reduction in any beneficiary’s payments. 29 C.F.R. § 4022.81–82. The City cited the PBGC regulations as an example of an appropriate type of methodology that the Associations could adopt in developing their recoupment plans. (*See* Pl.’s Post-Trial Br. 29.)

Not only do the Associations have the right to seek recoupment, they have an obligation to do so. As the Associations' own actuary, Mark Meyers, admitted, once the court concludes that the Associations overpaid beneficiaries, the Associations have a fiduciary duty to collect the overpayments. (ADD.42 ¶ 40; ADD.44 ¶ 10; RA.456–57.) Mr. Meyer's testimony and the district court's conclusion accurately reflect the case law. *See, e.g., In the Matter of Ret. Benefits of Robert W. Larson*, No. C07-95-2512, 1996 Minn. App. LEXIS 706, at *9–10 (Minn. Ct. App. June 11, 1996) (explaining PERA executive has a statutory duty to recover overpayments); *Masson*, 753 N.W.2d at 759 (emphasizing that PERA is “a public fund, and its preservation is in the public interest”). At least one court viewed the decision to forego recoupment as “inconsistent” with a fiduciary's high duty. *New York v. Ret. Bd. of the Teachers' Ret. Sys.*, 455 N.Y.S.2d 703, 705 (N.Y. Sup. Ct. 1982) (“It is the duty of the trustees to recover the overpayment as simply, expeditiously and inexpensively as possible and by foregoing the remedy of withholding they have breached their duty as trustees.”). As strong as the obligation to recoup overpayments may be in other settings, that obligation is, in a sense, tripled here. By express statutory mandate, the Associations owe a fiduciary duty, not just to the fund's beneficiaries, but to the taxpayers and to the State.

As fiduciaries, the Associations also need to protect the tax qualified status of the retirement funds. A retirement plan that pays benefits in excess of the benefits provided by the terms of the plan runs the risk of losing its tax qualified status. Rev. Proc. 2008-50, IRB 2008-35, Part III, § 5.01(2)(b). The only pre-approved remedy for correcting overpayments under IRS procedures is to recover the excess payments, either by seeking

direct payment from the affected beneficiary or by offsetting future benefit payments. Rev. Proc. 2008-50 at Part III, § 6.06(3) and Appendix B, § 2.04(1). While a detailed discussion of the IRS rules is beyond the scope of the issues at bar, the important message is this: recoupment is an approved procedure under the tax laws. Doing nothing is not.

The Associations contend that the district court erred by ordering recoupment, and do so largely by predicting a dire outcome if recoupment proceeds. The Associations' speculation is simply not germane here. The issue before this Court is far narrower than how the Associations have framed it. The only relevant issue for this Court is whether the district court abused its discretion by ordering the Associations to recoup payments consistent with "the standard of care customarily exercised by professional fiduciaries administering pension plans in recouping overpayments." (ADD.47, ¶ 3.) The district court merely ordered the Associations to do their job as fund fiduciaries.

The narrow scope of the relevant issue aside, the Associations' substantive arguments opposing recoupment are misplaced because (1) this Court has already determined the Associations adequately represent their beneficiaries' interests; (2) the district court's order does not implicate member due process rights; and (3) the law contemplates equitable recoupment when a plan breaches its fiduciary duties.

1. The Associations adequately represent their beneficiaries' interests.

On April 15, 2008, this Court held that the Associations could adequately represent their beneficiaries' interests. (R.Add.-4.) This Court concluded that, because the

beneficiaries collectively maintained the funds, the Associations represented “all of the individuals whose interests could be affected.” (R.Add.-5.) The Court further agreed with the district court that this matter is “primarily a dispute between the contributor to and the administrators of the pension funds about the proper method of calculating the contributor’s minimum obligation.” (*Id.*) The Court concluded individual beneficiaries were not indispensable parties to this litigation.

The law-of-the-case doctrine bars the Associations from relitigating associational standing. *See, e.g., Mattson v. Underwriters at Lloyds of London*, 414 N.W.2d 717, 719 (Minn. 1987) (“[I]ssues determined in a first appeal will not be relitigated in the trial court nor re-examined in a second appeal”). To sidestep this difficulty, the Associations attempt to reframe the issue and suggest that the order to develop recoupment plans vitiates this Court’s prior determination that the Associations adequately represent member interests.

To the contrary, the Associations remain the beneficiaries’ best advocates. *See, e.g., Frisk v. Bd. of Educ.*, 75 N.W.2d 504, 514 (Minn. 1956) (concluding teachers retirement group necessary party to litigate teachers’ retirement contributions); *see also Cal. Chamber of Commerce v. Simpson*, 601 F. Supp. 104, 106 (C.D. Cal. 1985) (holding the doctrine of associational standing applies in ERISA cases and “individual member participation [was] not required”). Minnesota law requires the Associations to administer pension funds for the benefit of their beneficiaries, survivors, and beneficiaries. *See* Minn. Stat. §§ 423B.04, subd. 2, 423C.02, subd. 1. Tellingly, the amicus brief submitted to this Court by Allen Berryman and Ronald Kastner, two beneficiaries who sought to

intervene in this appeal, offers the same arguments advanced by the Associations. (*See Berryman and Kastner Br. 3.*) The mere fact that a court orders a party to take a particular action does not affect or realign that party's interests.

Moreover, the beneficiaries' risk of reduced benefit payments has been in play from the very outset of this lawsuit—independent of any recoupment. The City's complaint sought "just and equitable" relief in response to allegations that the Associations overpaid member benefits. (Compl. ¶ 29(f).) Recoupment is the equitable remedy available to Minnesota's taxpayers for the Associations' past overpayments. *Geron v. Schulman*, No. 97-CV-8851, 2000 U.S. Dist. LEXIS 12576, at *161 (S.D.N.Y. Aug. 30, 2000) ("Recoupment is an equitable remedy."). Even if the district court awarded only prospective relief, beneficiaries faced reduced benefits in the form of halted overpayments. The Associations' complaint that the City has engaged in a "denouement worthy of Kafka" is nonsense—the City has always sought an equitable remedy in response to its overpayment claims and beneficiaries have always faced reduced payments.

2. The recoupment order does not implicate beneficiaries' due process rights.

Beneficiaries' due process rights are not implicated because beneficiaries have no right to overpayments. When a beneficiary is "not entitled to the benefit amount initially awarded him . . . [i]t is no detriment not to retain money that should never have been received." *Larson*, 1996 Minn. App. LEXIS 706, at *14 (permitting PERA to collect erroneous overpayments) (citations omitted); *see also Cassidy v. Adams*, 872 F.2d 729,

730 (6th Cir. 1989) (holding plaintiff “possessed no property rights in the overpaid benefits” which precluded “any violations of procedural due process [and] substantive due process”). Indeed, some courts have viewed overpaid beneficiaries as profiting from an effective interest-free loan. *See, e.g., Szydowski v. PBGC*, No. 4:05-CV-498, 2006 U.S. Dist. LEXIS 87986, at *25 (E.D. Mo. Apr. 7, 2006) (noting plaintiff was “effectively loaned the overpayments for several years without interest” and concluding plaintiff was not harmed by recoupment). In the ERISA context, courts have stated that beneficiaries have a “claim to benefits rather than the benefit itself” *Tucker v. GM Ret. Program*, 949 F. Supp. 47, 53 (D. Mass. 1996) (finding the “set-offs of retirement benefits in order to recoup benefits overpayments by the Program are allowable under ERISA”).

The gravamen of this dispute concerns the Associations’ illegal benefit calculation and the City’s resulting contribution burden. *See Minneapolis Police Relief Ass’n*, 2008 WL 1747923, at *4 (R.Add.-5) (summarizing this matter as “primarily a dispute between the contributor to and the administrators of the pension funds about the proper method of calculating the contributor’s minimum obligation”). Recoupment redresses the City’s complaint. The instant litigation does not, however, affect beneficiaries’ right to receive benefits. As it did in the 1995 Settlement Agreement, the City focuses on the Associations’ calculations. Member due process rights are not implicated.

More importantly, this Court cannot prejudge the due process adequacy of a recoupment plan that is not before this Court. The district court’s May 17, 2010, order grants the Associations latitude to craft a recoupment plan, limited at this point only by

the court's general charge that the Associations conduct themselves as professional fiduciaries would. (ADD.47, ¶ 3.) Appropriate recoupment procedures are situational. *See, e.g., Shannon v. U.S. Civil Serv. Comm'n*, 621 F.2d 1030, 1031 (9th Cir. 1980) (due process did not require prior oral hearings in benefit recoupment proceeding; written submissions sufficient under Civil Service statute); *Szydowski*, 2006 U.S. Dist. LEXIS 87986, at *30 (due process does not require a pension fund hold an in-person hearing prior to recoupment where facts are not disputed). The Association will be able to propose whatever procedural steps it believes are necessary or appropriate, consistent with its fiduciary obligations, including its fiduciary responsibilities to the taxpayers and the State.

3. Case law contemplates equitable recoupment where beneficiaries profited from overpayments at the taxpayers' expense.

The Associations argue that Minnesota's statutory framework does not explicitly provide for recoupment. The power to correct pension benefits, however, "need not rest on specific statutory authority." *Ret. Bd. of the Teachers' Ret. Sys.*, 455 N.Y.S.2d at 705 ("To hold that the board is without such power would mean that payments made in error could not be corrected by withholding subsequent payments, leaving the board with no alternative but to litigate to recover overpayments."); *see also Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504, 512 (1981) (ERISA plan may offset retirement benefits in an amount equal to worker's compensation payments despite a lack of express statutory authorization); *United States v. Wurts*, 303 U.S. 414, 416 (1938) ("The government's right to recover funds, from a person who received them by mistake and without right, is

not barred unless Congress has ‘clearly manifested its intention’ to raise a statutory barrier.”). In the trust context, courts have emphasized that “when a trustee overpays a beneficiary the trustee is entitled to recover the excess payment, even when it was the product of unilateral mistake on the part of the trustee.” *Hoffa*, 673 F.2d at 1354.

The Associations and amici curiae incorrectly suggest that recoupment would inequitably burden beneficiaries. They ask that the Court “weigh the equities” and “consider whether, under principles of equity or trust law, relief [i.e. recoupment] is unwarranted.” (See *Berryman and Kastner Br. 14-19*.) The district court, however, has already “weighed the equities.” This Court may not reverse the district court’s order absent a finding of abuse of discretion, which is certainly not present here.

In support of this equitable argument, the amici curiae rely heavily on two cases in which courts concluded that equity precluded recoupment. (*Id.*) In *Phillips v. Brink’s Co.*, 632 F. Supp. 2d 563, 566 (W.D. Va. 2009), a pension plan administrator failed to deduct plaintiff’s disability benefits for seven years. The Court emphasized that the plan breached its fiduciary duty to the beneficiary in “rubber stamping” erroneous benefit calculations. *Id.* at 574. Similarly, in *Phillips v. Mar. Ass’n-I.L.A.*, 194 F. Supp.2d 549, 551 (E.D. Tex. 2001), the court refused to reduce monthly payments with recoupment “when the overpayments were the result of a breach of fiduciary duty” to the beneficiaries. In both cases, plans breached fiduciary duties to their beneficiaries through their negligent failure to discover overpayments, and the courts barred equitable recoupment.

These cases are inapposite. The Associations did not breach their fiduciary duties to the beneficiaries. They paid the beneficiaries exactly what they intended to pay them. But the Associations breached their fiduciary duty to the taxpayers. The City alerted the Associations to the overpayments as early as 2004 and continually thereafter, but the Associations continued to issue overpayments. *See Phillips*, 194 F. Supp. 2d at 555 (“[I]t is critical to consider the circumstances surrounding the overpayments.”). Accordingly, the equities do not lie with the Associations or the beneficiaries. The equities lie instead with the taxpayers who must cover the overpayments unless they are recouped. The district court did not abuse its discretion in reaching this conclusion.

CONCLUSION

Respondent City of Minneapolis requests that this Court affirm the district court’s decision.

Respectfully submitted,

Dated: November 24, 2010

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CERTIFICATE OF COMPLIANCE

This brief complies with the word limitations of Minn. R. Civ. App. P. 132.01, subd. 3(a). The brief was prepared with Microsoft Word 2007 (using the Word 97–2003 file format), which reports that the brief contains 13,050 words.



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