TEAGUE P. PATERSON, SBN 226659
VISHTASP M. SOROUSHIAN, SBN 278895
BEESON, TAYER & BODINE, APC
483 Ninth Street, 2nd Floor
Oakland, CA 94607
Telephone: (510) 625-9700
Facsimile: (510) 625-8275
Email: tpaterson@beesontayer.com
vsoroushian@beesontayer.com

Attorneys for Plaintiff
AFSCME LOCAL 101

SUPERIOR COURT OF THE STATE OF CALIFORNIA

IN AND FOR THE COUNTY OF SANTA CLARA

AT SAN JOSÉ

SAN JOSE POLICE OFFICERS' ASSOCIATION, Plaintiff, v. CITY OF SAN JOSÉ, BOARD OF ADMINISTRATION FOR POLICE AND FIRE DEPARTMENT RETIREMENT PLAN OF CITY OF SAN JOSE, and DOES 1-10, inclusive, Defendants.	Consolidated Case No. 1-12-CV-225926 [*Consolidated with Case Nos. 1-12-CV-225928, 1-12-CV-226570, 1-12-CV-226574, 1-12-CV-227864, and 1-12-CV-233660*] **ASSIGNED FOR ALL PURPOSES TO: JUDGE PATRICIA LUCAS DEPARTMENT 2** **PLAINTIFF/PETITIONER AFSCME LOCAL 101'S PRE-TRIAL BRIEF** Hearing Date: July 22, 2013 Hearing Time: 8:45 a.m. Courtroom: 2 Judge: Hon. Patricia Lucas Complaint Filed: July 5, 2012 Trial Date: June 22, 2013
AND RELATED CROSS-COMPLAINT AND CONSOLIDATED ACTIONS	

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I. INTRODUCTION

On July 5, 2012, Plaintiff/Petitioner AFSCME Local 101 ("AFSCME" or "Union") filed its Complaint for Declaratory and Injunctive Relief and Petition for Writ of Mandamus, naming as defendants the City of San José ("City") and Debra Figone, in her official capacity as City Manager. AFSCME also named as Necessary Party in Interest the Board of Administration for the Federated City Employees' Retirement System ("System," "SJFRS," or "FCERS"). On February 11, 2013, it filed a First Amended Complaint for Declaratory and Injunctive Relief and Petition for Writ of Mandamus ("FAC"), naming the same parties.

Through this action, AFSCME challenges as unconstitutional an amendment to the City's Charter, commonly referred to as "Measure B," which was approved by a majority of the City's electorate on June 5, 2012. In the alternative, it seeks to *estop* the defendants from enforcing Measure B against the City's active employees.

II. PLAINTIFF/PETITIONER AFSCME LOCAL 101

AFSCME is a labor organization and the exclusive bargaining representative of two units of members employed by the City. The two bargaining units represented by AFSCME are the Municipal Employees' Federation ("MEF") and the Confidential Employees' Organization ("CEO"). In that regard, AFSCME bargains separate Memoranda of Agreement/Understanding ("MOU") governing the terms and conditions of its members' employment with the City.

Unable to reach agreement in the last round of negotiations, MEF and CEO have been without MOUs since 2011. However, for decades their MOUs entitled AFSCME members to the retirement benefits set forth in the San José Municipal Code ("SJMC" or "Code") with language similar to the following: "Current retirement benefits will continue during the term of this Agreement, except as described herein, and shall be set forth in the Municipal Code."

III. SAN JOSÉ FEDERATED RETIREMENT SYSTEM AND PLAN

The "1975 Federated City Employees Retirement Plan" or the "Federated City Employees Retirement Plan" ("Plan") is a defined benefit pension plan established by the City for its employees and administered by a Board of Administration under the auspices of the San José Federated Employees' Retirement System. (See San José Municipal Code § 3.28.010 ("SJMC" or "Code").) Its provisions are enumerated in chapters 3.16, 3.20, 3.24, and 3.28 of the SJMC. (SJMC § 3.28.010(B).)

The Plan is qualified under the Internal Revenue Code and established "pursuant to Sections 401(a) and 414(d) of the Internal Revenue Code, or such other provision of the Internal Revenue Code as applicable and applicable treasury regulations and other guidance of the internal revenue

service." The Plan is governed by a Board of Administration ("Board") which administers the Plan and is authorized to "fix and from time to time make such revisions or changes in the rates of contribution required of members and of the city as it may determine reasonably necessary to provide the benefits provided for by this retirement [P]lan." (SJMC § 3.28.010(D), 3.28.200.)

The SJMC sets forth provision of the City's pension and retiree health plan, as authorized by the Charter. The SJMC defines System "members" to include employees, retirees, and deferred-vested former employees. (*Compare* SJMC § 3.24.050(18) (defining "member") *with* SJMC § 3.24.050(5) (defining "employee").) AFSCME members automatically become members of the Federated City Employees' Retirement System upon becoming full-time City employees. (SJMC § 3.28.400 et. seq.) Even those starting as full-time employees who subsequently become part-time employees without a break of service retain their membership. (SJMC 3.28.560.)

AFSCME's members are not enrolled in the Federal Social Security Old Age, Survivorship, Disability Insurance program ("Social Security"), rather the SJFRS serves as an "alternative retirement system" or replacement for social security, pursuant to the Social Security Act and attendant federal regulations.

IV. MEASURE B

As referenced above, AFSCME challenges Measure B under the enumerated causes of action set forth in its First Amended Complaint as modified by the Court's Order Granting in Part and Denying in Part Defendant's Motion for Judgment on the Pleadings.

Generally, Measure B imposes significant detriments upon Federated members, including the following provisions.

Section 1506-A of Measure B requires employees who refuse to opt-into a "Voluntary Election Program" ("VEP") under Section 1507-A, must contribute up to sixteen percent of their pensionable pay to the System in order to pay up to 50% of the pension system's already-incurred unfunded accumulated actuarial liability ("UAL"). Members who are unable or unwilling to pay such additional amounts must are placed into the VEP and are not required to contribute towards the System's incurred UAL, but rather see a drastic reduction in benefits, including a lower pension accrual rate, an unfavorable redefinition of "final compensation" for purposes of determining their pension annuity, a reduction in the cost of living adjustment ("COLA"), and a later eligibility date for service retirement.

Section 1509-A redefines the eligibility requirements for disability retirement in a manner that makes it more difficult to retire in the event of disability. It also takes from the Board the authority to determine eligibility for disability retirement, and puts it in the hands of the City.

Section 1510-A gives the City authority to suspend COLA payments for up to five years upon declaring a "fiscal and service level emergency." This provision applies both to employees who opt-into the VEP and those who stay in the current Tier 1 or "legacy" plan. If the City chooses to restore the COLA, it unfixes it for those who remain in the Tier 1 plan and, for those who opt-into the VEP, it subjects it to the conditions set forth in the VEP provision (Sect. 1507-A).

Section 1511-A eliminates a "13th check benefit," the Supplemental Retiree Benefit Reserve ("SRBR") and returns the assets to the "appropriate retirement trust fund." The City has already implemented ordinances affecting the SRBR elimination.

Section 1512-A requires active employees to pay a minimum of fifty percent of the cost of all of the City's promised and vested retiree healthcare obligations, including both the normal cost and unfunded liabilities of active, retired and "deferred vested" members of the system. It also "unvests" the retiree health benefit and redefines "low cost plan" in a manner that is less favorable towards retirees.

Section 1513-A imposes certain requirement on the Board in administering the Federated Plan. Notably, it requires it to consider the City's economic interests equal to or greater than the interests of the System's beneficiaries.

Section 1514-A provides that in the event that Section 1506-A(b) is found illegal, employees' pay will be reduced up to a maximum of 16% of pay.

Notably, Measure B does not provide a single benefit to Federated members in exchange for these disadvantages.

V. AFSCME'S CLAIMS FOR RELIEF

AFSCME challenges the following provisions of Measure B:

- Section 1506-A, which substantially altered the pension plan ("Tier 1 plan") in which current employees participate,
- Section 1507-A, which established, pursuant to IRS approval, a Voluntary Election Program ("VEP") to serve as an alternative to the Tier 1 plan as altered by Measure B,
- Section 1509-A, altering the eligibility requirements of disability retirements,
- Section 1510-A, permitting the City to suspend Cost of Living Adjustment payments,
- Section 1511-A, eliminating the Supplemental Retiree Benefit Reserve ("SRBR"),
- Section 1512-A, making substantial changes to retiree healthcare,
- Section 1513-A, addressing actuarial Soundness for both pension and retiree healthcare, and
- Section 1514-A, savings clause penalizing a successful challenge to Section 1506-A, *supra*.

AFSCME's FAC alleges that Measure B violates the following provisions of the state Constitution:

- *Contracts Clause*: Cal. Const. Art. I sect. 9;

- *Bills of Attainder Clause*: Cal. Const. Art. I sect. 9;
- *Takings Clause*: Cal. Const. Art. I sect. 19;
- *Due Process Clause*: Cal. Const. Art. I sect. 7;
- *Pension Protection Act*: Cal. Const. Art. XVI sect. 17; and
- *Right to Petition Courts*: Cal. Const. Art. I sects. 2 and 3.

AFSCME also asserts causes of action for common law promissory and equitable estoppel.

Pursuant to these Constitutional provisions, AFSCME's FAC constitutes a facial challenge to Measure B. "A facial challenge to the constitutional validity of a statute or ordinance considers only the text of the measure itself, not its application to the particular circumstances of an individual." (*Tobe v. City of Santa Ana* (1995) 9 Cal.4th 1069, 1084.) Therefore, any assertion at trial with respect to how the City interprets or plans to implement Measure B is irrelevant and should be disregarded.

Each cause of action is briefed, for pre-trial purposes, below.

A. <u>Impairment of Contract</u>

Article I, section 9 of California's Constitution ("Contracts Clause") prohibits the state and its instrumentalities, including the City, from passing laws that impair contracts. Measure B violates the Contracts Clause with respect to its employees' promised pension, retiree health, and other retirement benefits.

1. Pension Law and the Contracts Clause

a. <u>Pension Benefits Are Afforded the Highest Level of Protection Under the Law</u>

Public pension benefits are created to serve "as an inducement to enter and continue in public employment" and to provide agreed subsistence to retired public servants who have fulfilled their employment contracts." (*Carmon v. Alvord* (1982) 31 Cal.3d 318, 325 n.4; *Bellus v. City of Eureka* (1968) 69 Cal.2d 336, 351; *Quintana v. Bd. of Administration* (1976) 54 Cal.App.3d 1018, 1021.) For public employees not enrolled in Social Security, public retirement systems are an obligation of the employer.

It was long ago established by our Supreme Court that "[t]he pension provisions of a city charter are an indispensable part of the contract of employment between a city and its employees, creating a right to pension benefits as an integral part of compensation payable under such contract, *which vests upon acceptance of employment*." (*Abbott v. San Diego* (1958) 165 Cal.App.2d 511, 517 (citations omitted) (emphasis added) ("*Abbott II*").)

Therefore, "upon acceptance of public employment [one] acquire[s] a vested right to a pension *based on the system then in effect"* and *"on terms substantially equivalent to those then*

offered by the employer …." (*United Firefighters v. Los Angeles* (1989) 210 Cal.App.3d 1095, 1102 (citations omitted) (emphasis in original) ("*LA Fire*"); *Pasadena Police Officers Assn. v. Pasadena* (1983) 147 Cal.App.3d 695, 703 ("*Pasadena Police*") (emphasis added).) The Contracts Clause protects the employee's reasonable expectations with respect to the pension benefits he/she will earn. (*Allen v. Bd. of Administration* (1983) 34 Cal.3d 114, 120; *Ass'n of Blue Collar Workers v. Wills* (1986) 187 Cal.App.3d 780 ("*Wills*") (right vested was "reasonable expectation" that city would meet statutory obligation to fund past-service liability).)

"This right arises before the happening of the contingency which makes the pension payable, and it cannot be constitutionally abolished by subsequent changes in the law." (*Wallace v. City of Fresno* (1954) 42 Cal.2d 180, 183 (citation omitted).) Furthermore, upon entering the workforce, the public servant obtains a vested contractual right to earn additional pension benefits pursuant to improved terms conferred during continued employment. (*Betts v. Bd. of Admin* (1978) 21 Cal.3d 492, 530.) As such, in the absence of "*clear* and *unequivocal*" language to the contrary, the public servant vests in the aforementioned expectations upon starting work. (*See Pasadena Police, supra,* 147 Cal.App.3d at 704 n.3 (citing *Bellus, supra,* 69 Cal.2d at 348-352; *see also Int'l Ass'n of Firefighters v. San Diego* (1983) 34 Cal.3d 292, 300-302 ("*SD Firefighters*").)

However, "[a]n employee's vested contractual pension rights may be modified prior to retirement for the purpose of keeping a pension system flexible to permit adjustments in accord with changing conditions and at the same time maintain the integrity of the system," providing such modifications are "reasonable." (*Allen,* 45 Cal.2d at 131.) To be sustained as "reasonable," alterations of employees' pension rights must bear some material relation to the theory of a pension system and its successful operation, *and changes in a pension plan which result in a disadvantage to employees should be accompanied by comparable new advantages*. (*Id*. (emphasis added).) "[I]t is advantage or disadvantage to the particular employees whose own contractual pension rights, already earned, are involved which are the criteria by which modifications to pension plans must be measured…." (*Abbott v. City of Los Angeles* (1958) 50 Cal.2d 438, 449 ("*Abbott I*").)

As such, any "reasonable modification" defense posed by the City here must clearly consider the detriment and commensurate advantages to the *individual employee*, and "benefits to other employees cannot offset detriments imposed upon those whose pension rights have accrued." (*Wisley v. City of San Diego* (1961) 188 Cal.App.2d 482, 486 ("*Wisley*") (citing *Abbott I,* 50 Cal.2d at 453).) Rather, under *Allen*, a disadvantage to an employee must be ameliorated by a comparable advantage to that *same employee*.

It has been long recognized that "[t]he benefits conferred under a pension system by changes which are made from time to time prior to the adoption of an amendment imposing a detriment 'have no bearing upon the reasonableness' of the detriment so imposed; such benefits become a part of the vested rights of the employees when conferred." (*Abbott II, supra,* 165 Cal.App.2d 517, 518 (citing *Abbott I, supra,* 50 Cal.2d at 449).) Therefore, the City's employees have earned a vested right to any additional benefits the City may have granted them after their commencement of their employment by the City.

Importantly, Measure B does not purport to provide City employees with any sort of benefit in exchange for the detriments it imposes upon them.

b. REAOC Does Not Apply to the Constitutional Question with Respect to Pensions

AFSCME anticipates that the City will argue that pension benefits vest in accordance with the principles stated in the California Supreme Court's decision in *Retired Employees Assn. of Orange County, Inc. v. County of Orange*, (2011) 52 Cal.4th 1171, 1186-87 ("*REAOC*"). However, *REAOC* is of limited value with respect to pensions because it evaluates whether retirees had a vested right to participate in a health insurance pool that included active employees, and held such a right could exist through an implied contractual term. The case neither involved nor discussed pensions or the social-security status of the plan participants. In fact, *REAOC* does not rely on any of the landmark pension cases discussed previously, and courts that have considered *REAOC* have not applied it in the pension context, with *City of San Diego v. Haas,* (2012) 207 Cal.App.4th 472, being no exception.[1]

In fact, *REAOC* recognized the protected status of pensions and then considered whether other types of retirement benefits received similar heightened protection. (*REAOC, supra,* at 1190 (citing *Cal. League of City Employee Ass'ns. v. Palos Verdes Library Dist.* (1978) 87 Cal.App.3d 135 (recognizing protected nature of pensions and holding longevity pay was similarly protected).) REAOC then provided guidance as to how to define the vested components of non-pension retirement benefits. Of course once deemed vested, they are protected in the same way pension benefits are, pursuant to the Contracts Clause. The *REAOC* Court's analysis is not surprising given the limited question of retiree-health "pooling," and its holding is inapposite here with respect to pension benefits because "under California law there is a strong preference for construing governmental pension laws as creating contractual rights for the payment of benefits." (*Walsh v. Board of Administration* (1982) 4 Cal.App.4th 682 (citing cases).)

[1] *Haas* does not generally apply *REAOC* to pensions, as it involved new hires who had not acquired vested rights. (*Id*. 480-81, 495.)

c. Federal Authorities are Not Relevant to AFSCME's Claim

AFSCME also anticipates that the City will attempt to confuse this case by relying on federal Contracts Clause cases. However, California's Constitution affords greater protections to the vested rights at issue in this case than does the federal Constitution. The court in *Walsh* explained the distinction between the protections afforded by each of the Constitutions as follows:

> There is nothing inherent in government retirement plans which compels the conclusion that they are protected against modification under the federal Constitution. For example, federal laws which create pension plans are considered to be social and economic legislation and the pension plans are not contractual in nature and thus may be modified or even eliminated. On some occasions the United States Supreme Court has upheld modification of state pension plans under the contract clause. *However, under California law there is a strong preference for construing governmental pension laws as creating contractual rights for the payment of benefits. Where it is feasible to do so the enactment of a governmental pension plan should be construed as guaranteeing full payment to those entitled to its benefits with the provision of adequate funds for that purpose.*

(*Walsh*, 4 Cal.App.4th at 697 (citations omitted, emphasis added).)

2. Extent of Measure B's Impairment of Vested Rights

a. Alterations to the Defined Benefit System

As described, above, AFSCME members automatically become members of the Federated City Employees' Retirement System upon becoming full-time City employees. (SJMC § 3.28.400, *et. seq*.) Measure B makes substantial changes to the System and the benefits afforded thereunder, as discussed below.

i. Suspension and Reduction of COLA

Sections 1507-A(b)(v), 1507-A(e)(iii), and 1510-A of Measure B constitute an unconstitutional impairment of contract by impairing employees' and retirees' right to a fixed three percent annual COLA. A COLA is inflation protection; without it, assuming inflation occurs as it always has, the real value of the pension annuity -- and its ability to provide adequate retirement security and income protection -- is diminished over time.

California courts have repeatedly held that COLA benefits are protected by the Contracts Clause in the same way that any other retirement security pension provisions are protected. (*LA Fire*, *supra*., 210 Cal.App.3d 75 (charter amendment placing a 3% cap on COLA deemed unconstitutional as applied to police and fire fighters hired prior to enactment of charter amendment because plaintiffs had vested right not only to benefits substantially similar to those in effect when they accepted public employment, but also to additional benefits offered later by the employer); *Pasadena Police, supra,* 147 Cal.App.3d at 702 ("The 1981 amendments to the COLA provisions were obviously

disadvantageous to the employees. They substantially limited and reduced the protection which had previously been offered by a pension fully adjustable to changes in the cost of living. The city makes no claim that this detriment was compensated by comparable new advantages. Under the test laid down by the Supreme Court in *Allen*, and repeatedly reaffirmed by the Supreme Court, the 1981 amendments substantially reducing the cost of living benefits of the pension plan are invalid."); *Wills, supra,* 187 Cal.App.3d at 780.) Other state and federal courts have reached this conclusion. (*See, e.g. Hayden v. Hayden* (1995) 284 N.J.Super. 418, 665 A.2d 772, 774–75 ("post-retirement [COLA] increases are as much a part of the pension as the amounts initially established by the pension system on retirement"); *cf. United States v. Will* (1980) 449 U.S. 200, 229 (cost of living adjustment to judicial salaries vested when it took effect; applying U.S. Const. art. III, § 1); *Williams v. Rohm and Haas Pension Plan* (7th Cir. 2007) 497 F.3d 710, 713 (if pension plan entitles annuitant to COLA, it must also provide COLA's actuarial equivalent to participant who chooses instead to receive pension in form of one-time lump sum distribution).)

It is no surprise that courts recognize that COLA benefits are an integral component of a pension annuity and an integral part of the pensioner's expectations. This is especially true where employees are not covered by Social Security (which includes a COLA escalator). In other words, not only is the Federated system the only retirement security AFSCME's members have, it is also the only inflation insurance they have. In Accordance with GASB rules and sound actuarial principles, the System's COLA benefit is funded through employee and employer annual "normal cost" contributions. Thus, employees and pensioners have contributed towards the cost of their COLA benefit throughout their employment; to the extent the COLA benefit may have been increased by the City, any cost associated with such increases would, in accordance with GASB rules and sound actuarial practices, be "smoothed" over an ensuing five-year period for funding purposes.

The SJMC specifically recognizes the COLA benefit as a pension allowance. (*See* SJMC § 3.44.160(A)(1).) In 2006, the Plan's COLA provision was amended to a *guaranteed* three percent annual adjustment. (SJMC§ 3.44.160; City Auditor's Report (Sept. 2010), p. 14.) Section 1507-A(b)(v) of Measure B "unfixes" the benefit and caps it at 1.5% per fiscal year for employees forced into the VEP. As a result, there is no guarantee that participants in the VEP will even receive the lower 1.5% annual COLA, nor that this rate will keep pace with inflation. (Historically, 1.5% annual COLA is far below inflation rates as calculated by the Bureau of Labor Statistics.) These same provisions apply to those retiring for a service connected disability retirement, as Section 1507-A(e)(iii) states that COLA provisions for such individuals "will be the same as for the service retirement benefit in the VEP."

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Furthermore, Section 1510-A of Measure B grants the City Council the discretionary authority to suspend for up to five years all COLA payments to all retirees--whether they stayed in the Tier 1 plan or transitioned to the VEP--upon adopting a resolution declaring a "fiscal and service level emergency." Measure B does not define what constitutes a "fiscal and service level emergency," and, therefore, appears to leave that determination to the discretion of the City Council. In the event that the City suspends payments in such a fashion, in the event that it restores *all or part* of the COLA after suspending it, Measure B caps it at three percent for those staying in the Tier 1 plan and 1.5% for those in the VEP. It appears as though the COLA rates would not continue to be a fixed percentage, as they were prior to Measure B. All of these changes significantly diminish City employees' vested reasonable pension expectations.

Measure B's COLA amendments substantially impair members' pension expectations without providing a commensurate benefit. As such, sections 1507-A(b)(v), 1507-A(e)(iii), and 1510-A of Measure B constitute unconstitutional impairments on contract in contravention of Cal. Const. Art. I sect. 9.

ii. Elimination of SRBR Benefit

Section 1511-A of Measure B eliminates an established pension benefit and its trust account, and then raids the *res* of the trust account to offset the City's general funding obligations. The SRBR is a "13th Check" benefit, a form of inflation protection available to retirees in the event that excess earnings exist in the operating account of the System after payment of all administrative costs and expenses. The allocation to the SRBR benefit consists of 10% of the excess earnings remaining in the System's operating account (the other 90% are deposited in the System's general fund). (SJMC § 3.28.340(D).) The SRBR benefit is not unique to FCERS, and in fact, was predicated on similar benefits offered under other California public pension systems.

California Trust law, contained in the state Constitution's Pension Protection Act (Art 16, sect. 17) as well as the SJMC, prohibits eliminating and appropriating the assets of the SRBR. By its terms, the SRBR was created for the benefit of Federated retirees, and "shall be used only for the benefit of retired members, survivors of members, and survivors of retired members." (SJMC § 3.28.340(E)(1); *see also* SJMC § 3.28.340(E)(2).) Article 16, section 17(a) of the Constitution, states: "The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system." (*See also Keitel v. Heubel* (2002) 103 Cal.App.4th 324, 337 (discussing elements of express trust); *City of Palm Springs v. Living Desert Reserve* (1999) 70 Cal.App.4th 613, 619 ("The legal title of the res or corpus of any

1 trust is held by the trustee, but the beneficiaries own the equitable estate or beneficial interest").)

2 Measure B provided for the elimination of the SRBR benefit and authorized the transfer of the
3 SRBR Trust Fund's assets to offset the City's general obligations to fund benefits. In that regard,
4 when the City liquidated the Fund in 2012, it incurred a fiscal-year budget savings of approximately
5 $17 million; that is, the SRBR funds offset what it would have otherwise been required to pay into
the retirement system for that year.

6 The City has relied on *Claypool v. Wilson,* (1992) 4 Cal.App.4th 646, to argue the elimination
7 of SRBR and suspension of COLA are permissible. (*Id*. at 674.) In *Claypool*, the court held it was
8 constitutional to eliminate a separately funded COLA trust where the funds were absorbed into the
9 pension system, but only because in doing so the pension system also adopted a commensurate
10 COLA benefit. (*Id*. at 658). Thus the *Claypool* court noted, "[T]he saving of public money is not an
11 illicit purpose if changes in the pension program are accompanied by comparable new advantages to
the employee." (*Id*.) Here, SRBR is eliminated but no replacement benefit is adopted.

12 In a similar case, *Wayne County Employees Retirement System v. Charter County of Wayne,*
13 (Mich.App. May 9, 2013) 2013 WL 1920732, a Michigan appellate court found unconstitutional the
14 liquidation of an SRBR-type benefit, an "Inflation Equity Fund" or "IEF," that provided occasional
15 13th checks predicated on excess investment earnings, even though the law did not mandate annual
16 distributions to retirees. The Court noted the fund "can be accurately characterized as a vested
17 reserve belonging and in relationship to the Retirement System's participants as a whole, outside the
18 reach of [the county], to be used to assist retirees and survivor beneficiaries in fighting the devaluing
19 of the dollar by inflation." (*Id*.) For that reason, the court disapproved of the County's liquidation of
20 the fund to pay its annual required contribution to the amortized cost of pension system unfunded
21 liabilities, which the court described thusly: "Instead of honoring and protecting the IEF in
22 connection with its designed purpose, the County Board improperly invaded the assets of the IEF to
23 lessen its financial burden with respect to [Annual Required Contributions]… dipped into assets that
had already been set aside for a particular purpose pursuant to the requirements of previous
provisions of the IEF Ordinance." (*Id*. at *17).

24 Similarly *McCall v. State,* (1996) 640 N.Y.S.2d 347, 219 A.D.2d 136, 142, is instructive. In
25 that case, a new statute "grant[ed] State and municipal employers a credit to be assessed against" a
26 Supplemental Reserve Fund ("SRF"), and which the court found unconstitutional because, although
27 the SRF was "a separate fund" and not used to pay benefits, it was "indisputably an asset of the
28 retirement system" and was subject to the power of the trustee "to hold, manage and invest the assets
contained therein for the benefit of the members and beneficiaries of the retirement systems…" (*Id*.

at 140 (citations omitted).)

Here, the SJMC provides that the City Council retains discretion over the distribution of SRBR assets, the SJMC and resolutions set forth a process by which SRBR distributions to retirees are made from the SRBR Trust "if any" assets are held in the trust. The City Council does not retain ultimate discretion, but rather must administer the retirement trust in accordance with fiduciary principles arising under the Article 16 of the Constitution. Therefore, although the Municipal Code provides discretion to "determine the distribution," it does not mean the benefit is entirely discretionary or that a contractual obligation has not arisen. Under California law, an obligation under a contract is not illusory if the obligated party's discretion must be exercised with reasonableness or in good faith. (*Storek & Storek, Inc. v. Citicorp Real Estate, Inc.* (2002) 100 Cal.App.4th 44, 61; *Third Story Music, Inc. v. Waits* (1995) 41 Cal.App.4th 798, 806 ("the implied covenant of good faith is also applied to contradict an express contractual grant of discretion when necessary to protect an agreement which otherwise would be rendered illusory and unenforceable.").) Here, the fact that the SRBR establishes a trust for the exclusive behalf of retirees, to which Article 16 of the Constitution imposes fiduciary obligations, the discretion conferred to designate the amount of benefit must be exercised in good faith and in accordance with fiduciary principles.

Importantly, the SJMC does not confer discretion to discontinue or eliminate the SRBR trust account or the benefit itself. Nor does "the greater power imply the lesser power," an argument rejected in *Legislature v. Eu* (1991) 54 Cal.3d 492, 528-534, where the electorate attempted to terminate the Legislators' Retirement Law ("LRL") with respect to incumbent legislators. In that case, the "lesser power" reserved to the legislature to limit retirement benefits payable to legislators, did not imply the greater power to terminate them, and so completely repealing a benefit was unconstitutional. (*Id.; Kern v. City of Long Beach* (1947) 29 Cal.2d 848.) As such, Section 1511-A of Measure B constitutes an unconstitutional impairment of contract.

iii. Redefinition of Disability Benefit

AFSCME members do not receive disability insurance through Social Security, and have no other disability insurance than that afforded under the Federated System's disability provisions. Measure B constitutes an unconstitutional impairment of contract by impairing their vested disability retirement expectations.

For employees forced into the VEP plan, Measure B reduces the maximum benefit that a disabled employee may receive, eliminates items of compensation that were previously incorporated into the disability annuity formula, and reduces the COLA percentage. (*Compare* SJMC section 3.28.1210 *with* Measure B section 1507-A(e).)

Also, prior to Measure B, an employee working for the City who became disabled was entitled to a disability pension if the disability prevented the employee from performing the duties required of her in her position, or within other positions of the same classification where there was a vacancy. Employees who suffered a workplace injury resulting in disability were entitled to a service-connected disability pension of no less than 40% of final pay but up to 75% of final pay depending on the total number of years of service at the time of the disability retirement. (SJMC § 3.28.1280). Non-service connected disability benefits were computed at a lower scale than service connected disabilities. (*See* SJMC § 3.28.1300.)

While reducing the disability benefit under the VEP, for all employees Measure B imposes deeper restrictions on what is considered a "Disability." In short, it restricts the eligibility for disability retirement to those whose disability is either expected to last more than one year or will result in death and who cannot perform *any* jobs for the City as a result of disability (Measure B section 1509-A), even if there is no vacancy in the classifications within the City. In a way, this permits the City to manipulate its disability pension liabilities by determining whether there are openings in such classifications. Further, for employees forced into the VEP, the amount of the benefit is dramatically reduced under Section 1507-A(e) of Measure B which limits service-connected disability to fifty percent of pay and non-service connected disability to twenty-five to fifty percent of pay, depending on years of service. Prior to Measure B the retirement board had authority over all pension eligibility determinations, including disability pensions, whereas Measure B revokes that authority and grants it to a medical review panel. (Section 1509-A(c).)

As discussed above, a public employee's pension constitutes an element of compensation, and a vested contractual right to pension benefits accrues upon acceptance of employment; this "*principle applies with equal force to disability pensions*." (*Gatewood v. Board of Retirement* (1985) 175 Cal.App.3d 311, 319-20 (emphasis added); *Cochran v. City of Long Beach* (1956) 139 Cal.App.2d 282, 286 (applying *Allen* to change in disability retirement); *see also Newman v. City of Oakland Retirement Bd*. (1978) 80 Cal.App.3d 450, 458, ("It is well settled that retirement benefit rights including pensions whether for age and service, disability or death are vested.").) In fact, the court in *Frank v. Board of Administration* (1976) 56 Cal.App.3d 236 stated:

> No reason exists in plaintiff's case to apply a different rule to disability retirement benefits than to service retirement benefits. We therefore hold that the *plaintiff acquired a vested contractual right to a reasonable disability retirement pension when he entered upon performance of his employment contract with the state*.

(*Id*. at 241–243 (emphasis added).)

As such, changes to a disability benefit are treated no differently under *Allen* and its progeny than any other component of a pension annuity. For example, in *Babbitt v. Wilson* (1970) 9 Cal.App.3d 288, 290, a city attempted to change a disability retirement benefit from two-thirds of salary to one-half of salary, which was held invalid as to employees who had worked under the older more generous system. (*Id*.; *see also Pasadena Police, supra,* 147 Cal.App.3d at 703.)

The same principle applies in this case. Measure B's changes to the disability retirement benefit applicable to current employees runs afoul of this established doctrine. For the aforementioned reasons, Sections 1507-A(e) and 1509-A constitute unconstitutional impairments of contract.

iv. Imposition of Liability for City's Unfunded Liabilities

Prior to Measure B, neither the City Charter nor its Code required employees to make contributions towards the City's pension UAL; in fact, the Code explicitly placed this responsibility upon the City. However, Section 1506-A of Measure B requires that active employees who wish to remain in the Tier 1 plan and retain those benefits already earned, must contribute up to an additional sixteen percent of their pensionable pay towards financing up to fifty percent of the City's pension UALs. Therefore, Section 1506-A of Measure B constitutes an unconstitutional impairment of contract.

aa. Background to Obligation for Active Employees to Finance Tier 1 UALs

The City claims that its pension systems have substantial UALs. With this backdrop, it has drastically cut its workforce through layoffs, reductions in force, early retirements, and wage cuts. As a result of the smaller group of active employees within the Federated System. By imposing on them the obligation to shoulder previously-incurred UALs, a smaller number of active employees are required to shoulder the burden attributable to the City's general pension obligations owed as a result of experience associated with the benefits of retired and deferred-vested members (and their survivors).

This additional financial burden is considerable, especially given the fact that AFSCME's members have already received a twelve percent pay reduction over the last four years. Moreover, the obligation imposed by Measure B to pay system unfunded liabilities does not distinguish between the unfunded liabilities attributable to active, deferred-vested, or retired System members; active members are on the hook for financing all such UALs, despite the fact that there may be no one left in the Tier 1 plan to contribute towards their benefits once they retire. In fact, active members have already made contributions towards their own prior service as part of their normal cost contributions. They are now being forced to contribute towards UALs attributable to the same prior service.

bb. Impairment of Vested Right to Not Pay Pension UALs

Long ago, our Supreme Court recognized that "[t]he pension provisions or a city charter or ordinance form an integral part of the employment contract." (*Kern, supra,* 29 Cal.2d at 852.) "Therefore, when the ordinance establishing the pension plan can reasonably be construed to guarantee full payment to those entitled to its benefits regardless of the amount in the fund established by the pension plan, then [courts] are … required to construe the provisions liberally in favor of the applicant so as to carry out their beneficent policy." (*Bellus, supra,* 69 Cal.2d at 351 (citing case).) This is because courts "reject any theory that the provisions of the charter were designed to create an appearance of granting pensions while at the same time withholding the benefits by providing inadequate funds." (*England v. City of Long Beach* (1945) 27 Cal.2d 348.) As a result, courts refuse to allow municipalities to evade their pension contribution obligations in the absence of explicit authority permitting them to do so.

Both *Bellus, supra,* 69 Cal.2d at 336, and *England, supra,* 27 Cal.2d at 343, presented the question of whether a municipality was required to cover its retirement systems' unfunded liabilities in the absence of clear language absolving it of such responsibility. In both cases, the Supreme Court held that a municipality was required to pay a pension from a source other than a retirement fund even where there was not enough money in the fund to meet the obligation. The court in *Wills* succinctly summarized *Bellus* as follows:

> The city in *Bellus* was faced with a statutory scheme that permitted increases in the pension payments by employees only after they had voted for increases. If the employees failed to vote for increases, their pension was reduced in a pro rata manner to cover the deficiency between available funds and accrued benefits. The city asserted in *Bellus* that it could only finance the unfunded debt after the employees had voted for increased contributions. The Supreme Court rejected this argument. It found that a charter city, possessed of plenary powers to adopt pension systems, was liable for pension payments which it had led its employees to reasonably expect. The *Bellus* court acknowledged that the insufficiency within the pension fund may have resulted from mere oversight. Nevertheless, the court found that the city bore a continuing obligation to contribute to the fund and to fulfill unfunded claims set up by the pension system.

(*Bellus*, 187 Cal.App.3d at 790.)

In interpreting *Bellus*, the court in *Pasadena Police* recognized that "in the absence of a *clear and unequivocal* declaration in the pension provisions that benefits are payable only to the extent of available funds from specified contributions, the liability to pay promised pension benefits is a general obligation of the city." (147 Cal.App.3d at 704 n.3 (emphasis added).) Importantly, the *Bellus* court stated:

> [W]e must reject any argument 'that if a general obligation had been intended, the voters would have stated specifically that the city should levy a tax sufficient to cover all pension payments…. The rationale underlying the rule of construction [] that the City's liability for pension payments is not limited to the pension fund *unless the pension plan clearly specifies that limitation* - and the general rule the pension plans must be liberally construed to promote their beneficent purpose, rests on the same duty of fair dealing and obligation to protect the reasonable expectations of those whose reliance is induced that underlie the rules of construction in favor of the insured in insurance cases….

(*Bellus,* at 350 (emphasis added).) The court went on to conclude that:

> [A] charter city, possessed of plenary power to adopt a pension system imposing upon it a general obligation, cannot escape liability for those pension payments which it has led its employees reasonably to expect. In this respect it is no different than any other employer or public service institution which induces reliance upon a contract which may reasonably be interpreted to afford that protection which has been impliedly promised. We recognize that the City will not be so obligated if the pension plan which it adopts, either in the ordinance itself or the statutory scheme which it incorporates, *clearly and explicitly limits its liability to the fund which the pension plan establishes. In the absence of such a limitation … we must conclude that the City of Eureka bears a general obligation under the pension ordinance.*

(*Id*., at 352 (emphasis added).)

Likewise, in *England*, the city withheld pension payments from the petitioner because "payments due to pensioners have greatly exceeded the sums paid into the pension fund." (*England*, 27 Cal.2d at 344.) However, the Supreme Court held that the obligation to fund the benefits was a general obligation of the City because "there was no language in the charter which *expressly* limit[ed] pension payments to the money in the pension fund or to the particular items mentioned as source." (27 Cal.2d at 347 (emphasis added).) In *Bellus* and *England*, the Court concluded that while the ordinances and laws at issue in those cases set forth a method for funding the defined pension benefit, they "were not intended as qualification or limitation but that the pension fund was created, and payments ordered made therefrom, simply as an orderly and customary means of administering city moneys." (*Id*; *Bellus, supra,* 69 Cal.2d at 350.) For its part, the *England* court stated:

> [T]he employee involved here was required to contribute a portion of his salary to the pension fund. Although provision was made for substantial pensions, *the inadequacy of the provisions for maintenance of the pension fund was not apparent from the face of the charter…. [T]he charter did not expressly limit the obligation of the city to the payment of pensions from the pension fund. It would be obviously unjust to make the payment of pensions dependent upon the solvency of a particular fund, thereby depriving employees of the benefits of the system,* ***unless we were compelled to do so by a clear, positive command in the charter****.*

(27 Cal.2d at 348 (emphasis added).) The reasoning of these cases applies with equal force to AFSCME's claims related to the takings clause and the imposition of an obligation to pay for pension

and retiree health UALs imposed on employees by the City.

While a municipality may not shirk from its pension responsibility when faced with pension unfunded liabilities, it also is not required to share with its employees "a plan's surplus--even if it is partially attributable to the investment growth of their contributions." (*Hughes Aircraft v. Jacobson* (1999) 525 U.S. 432, 433.) At the same time, the municipality may not pass its debt onto its employees by requiring them to pay increased pension contributions unless clearly authorized to do so by the charter or municipal code in effect at the time the employees commenced working. (*See Allen, supra,* 45 Cal.2d at 128; *England, supra,* 27 Cal.2d at 348; *Bellus, supra,* 69 Cal.2d at 352.)

Similarly, where a municipality is without explicit authority to raise the basis of the employees' contribution rates, the employees are only required to contribute at the rate in place during the time they were originally employed. (*See Wisley, supra,* 188 Cal.App.2d at 484-85 (affirming trial court's judgment that increases in contribution rate were unconstitutional and stating that "[t]he [trial] court concluded that the maximum amount that could legally be deducted from the employees' gross pay was that percentage which was in effect at the time each of the individual plaintiffs was originally employed").) This is because vested pension rights include not only the benefits payable at retirement but also the scope of a member's contribution obligation as defined under the terms of the contract in place at the time he/she began working.

This doctrine goes back to the seminal holding in *Allen*, in which the court held unconstitutional the city's action of increasing the amount of each employee's contribution from two percent to ten percent of his salary. (*Allen*, 45 Cal.2d at 128.) The court held that this change was unlawful because it "constitute[d] a substantial increase in the cost of pension protection to the employee without any corresponding increase in the amount of the benefit payments he will be entitled to receive upon his retirement." (*Id*. at 131.) In discussing *Allen,* the court in *Pasadena Police* stated:

> [W]here the employee's contribution rate is a fixed element of the pension system, the rate may not be increased unless the employee receives comparable new advantages for the increased contribution. An increase in an employee's contribution rate operates prospectively only and in effect reduces future salary, yet in *Allen* the Supreme Court struck down such a change on the ground that it modified the system detrimentally to the employee without providing any comparable new advantages. The contribution rate cases, including *Allen* itself, are wholly inconsistent with defendants' argument that *Allen* means only that comparable new advantages must be provided when benefits already earned are modified retroactively.

(147 Cal.App.3d at 702-703 (citing cases).)

Likewise, the aforementioned "contribution rate cases" also undermine the City's argument

that its plenary power over wages allows it to drastically and substantially re-draft the pension Plan's means of determining contributions on either a prospective or retroactive basis. The effect of requiring additional contributions associated with unfunded liabilities is no different than retroactively imposing changes to pension plan contributions. If the City could not increase contribution rates prospectively under *Allen*, it certainly cannot do it retroactively with respect to the FERS's unfunded liability.

Courts in other jurisdictions are of the same mind. In *AFT Michigan v. State*, the state passed a statute requiring "that public school districts and other reporting units withhold three percent of each employee's wages and remit the amount" to a designated trust to help finance retiree health benefits. (*AFT Michigan v. State* (2012) 297 Mich.App. 597, 604.) In holding that the statute violated the state and federal Contracts, Takings, and Due Process clauses, the court observed the following, and cited numerous cases with similar holdings:

> Many courts have held that impairments of governmental employees' contracts by the state that have indefinite or permanent application clearly violate the Contract Clause. *Oregon State Police Officers' Ass'n v. State*, 323 Or. 356, 918 P.2d 765 (1996) (striking down a state statute that required public employees to contribute six percent of their salaries to retiree benefits contrary to their contract); *Opinion of the Justices*, 364 Mass. 847, 864, 303 N.E.2d 320 (1973) (striking down legislation increasing present employees' contributions to retiree benefits without an increase in the subject employees' own retirement benefits as "presumptively invalid" under the Contract Clause); *Singer v. City of Topeka*, 227 Kan. 356, 369, 607 P.2d 467 (1980) (holding that a statute mandating an in-crease in public employees' contributions to their retirement plan without a commensurate increase in benefits "is an unconstitutional impairment of contract rights"); *Marvel v. Dannemann*, 490 F.Supp. 170 (D.Del., 1980); *Hickey v. Pittsburgh Pension Bd.*, 378 Pa. 300, 106 A.2d 233 (1954); *Allen v. City of Long Beach*, 45 Cal.2d 128, 287 P.2d 765 (1955).

(*Id.* at 616.)

Here, the City points to Section 1505(c) of its charter, which specified a three (employee) to eight (City) pension contribution ratio related to "current service or current service benefits" and suggests that an absence of a reference to a specific contribution ratio for UALs is indicative of the fact that none existed; therefore, it argues, it could set employee pension UAL contributions rates as it saw fit. This argument attempts to turn the enunciations of the Supreme Court in *Allen*, *Bellus*, and *England* on its head, by suggesting that only a clear and explicit statement that it could not do so should prevent it from eliciting contributions from its employees towards UALs. However, those cases require the exact opposite: "a clear and unequivocal declaration in the pension provisions" that the City is authorized to increase its employees' pension contributions. (*See Pasadena Police, supra,* 147 Cal.App.3d at 704 n.3.)

Furthermore, Section 1505(c)'s specification that the contribution ratio "does not apply to any contributions required for or because of any prior service or prior service benefits" is also unhelpful to the City's case. "Prior service" is defined as "all city service rendered by a member prior to July 1, 1951." (SJMC § 3.24.1000(D).) Therefore, it is not synonymous with UAL.

The San José Municipal Code is filled with provisions which require the *City* to cover the cost of its pension and other retirement benefit UALs. (See SJMC §§ 3.24.570, 3.24.730, 3.28.710, 3.28.880.) For example, SJMC sect. 3.28.710 states:

> The normal rate of contribution required of members shall be such that, based on interest and mortality tables and other relevant actuarial data, the total amount of normal contributions which will be required of members under the provisions of this chapter will be sufficient to pay, when due, three-elevenths of the amount of all pensions … which are and will become payable under this system on account or because of current service rendered on or after July 1, 1975; provided and excepting, however, that if and when, from time to time, the members' normal rate of contribution is hereafter amended or changed, *the new rate shall not include any amount designed to thereafter recover from members or return to members the difference between the amount of normal contributions theretofore actually required to be paid by members and any greater or lesser amount which*, because of amendments hereafter made to this system *or as a result of experience under this system*, said members should have theretofore been required to pay in order to make their normal contributions equal three-elevenths of the abovementioned pensions, allowances and other benefits which are or will become payable on account or because of current service rendered on or after July 1, 1975, and before the effective date of the new rate.

(Emphasis added.) Similarly, the City's numerous retirement handbooks indicate that it is liable for covering the cost of the System's UALs.

AFSCME understands that the City intends to rely on *SD Firefighters, supra,* 34 Cal.3d 292, to justify increasing its employees' contribution rates. But that case was decided in accord with the principles outlined above and does not justify the City's action. The court in *SD Firefighters* held that the city did not violate the Contracts Clause when it raised its employees' contribution rates *pursuant* to language within its municipal code and charter that clearly authorized it to do so upon the advice of an actuary. (*Id*. at 303 ("[T]he system does *explicitly* provide for both setting and *revising* of employee contribution rates upon the basis of the actuarial information and revisions thereto.") (emphasis original) ("*SD Firefighters*").) The court in *Pasadena Police* said the following about the *SD Firefighters* decision:

> There, as here, the contribution rate required of the employees was substantially increased based upon the advice of the retirement system's actuary that, pursuant to the new guidelines of the profession, salary inflation be taken into account. The Supreme Court rejected the employees' argument that the increase in the contribution rate impaired their vested contract rights. The court held the increase *was authorized*

> *by the express provisions* of the retirement system which provided for an actuarially based rather than a fixed contribution rate.

(147 Cal.App.3d at 711 (emphasis added).) This case is very different. First, while the Charter explicitly requires the actuarial soundness of the Police and Fire Retirement System, it does not require the same of the Federated System. (*Compare* Charter sect. 1504(c) *with* Charter sect. 1505.) Also, the San José Charter does not explicitly grant the City with the power to raise its employees' contribution rates, and the Charter's purported "Reservation of Rights Clause" is not the type of clear and explicit language required to support an increase in employee contribution pursuant to the *SD Firefighters* case. Rather, the SJMC explicitly vested the *retirement board* and not the City, to change contribution rates related to pension. Section 3.28.200 of the Code states:

> Upon the basis of any or all of such investigations, valuations and determinations, the *board* shall adopt such mortality, service and other tables, actuarially assumed annual rate of return, and other actuarial assumptions as it may deem reasonably necessary, and, subject to such limitations as are set forth elsewhere in this chapter, *it shall fix and from time to time make such revisions or changes in the rates of contribution required of members and of the city as it may determine reasonably necessary to provide the benefits provided for by this retirement plan.*

(Emphasis added.) Additionally, as will be demonstrated *infra,* SJMC sect. 3.28.880 specifically authorizes only the Board to change pension and retirement contribution rates towards funding UALs.

v. *The Hobson's Choice "Voluntary Election Plan"*

The VEP provisions set forth in Section 1507-A of Measure B are unconstitutional because they reduce vested pension benefits. Together, Sections 1506-A and 1507-A require employees to opt-into the second tier benefits (Tier 2) under the VEP plan or alternatively forego a large portion of their wages by staying in the Tier 1 legacy plan as amended by Section 1506-A.

<u>aa. The VEP Does Not Present a Voluntary Choice and So Is Invalid</u>

Although couched as a "voluntary" election, choosing the VEP option does not constitute an objectively voluntary decision. Rather, Section 1507-A presents a City employee with two bad choices, and the only real option is in deciding which of those two bad choices will put him/her in a less worse-off position. In pertinent part, Section 1507-A states: "Employees who opt into the VEP will be required to sign an irrevocable election waiver … acknowledging that the employee irrevocably relinquishes his or her existing level of retirement benefits and has voluntarily chosen reduced benefits, as specified below."

Although there are few case law authorities that consider the obvious: whether the Orwellian-named "voluntary" plan really provides a voluntary choice where failing to make one choice leads to a severe penalty, some Courts have considered the term "voluntary" within the unemployment compensation benefits context. In such cases, employees were forced to choose between a "voluntary" and detrimental change of circumstances or remaining in the same situation and incurring a detriment. The court described such "voluntary" Hobson's choices as a "semantic sleight-of-hand that is irreconcilable with our charge to narrowly confine disqualifying exceptions . . . *This is compulsion*." (*Nielson v. Employment Sec. Dept. of State*, (1998) 93 Wash. App. 21, 37-38 (emphasis added).) In *Pettypool v. Arizona Dept. of Economic Sec.* (1989) 161 Ariz. 167, where an employee presented with the "choice" of signing a Disciplinary Action Record ("DAR") that would reduce his wages, or not sign it which would act as a resignation, the court stated:

> Claimaint [sic] argues that *the employer presented him with a Hobson's choice*. He could either sign the DAR or not sign it. If he did, he would forfeit a portion of wages that he had already earned. If he did not sign the DAR, he would be deemed to have resigned. Since signing the DAR was a patently unreasonable alternative, claimant argues that the employer forced him to resign. Thus, claimant concludes that the DAR was effectively a request for resignation. *We agree*.

(*Id*. at 170 (emphasis added).) Here, employees who refuse to relinquish their right to receive the pension benefit to which they have worked toward and contributed are subject under the VEP provisions to a wage excise of up to sixteen percent. (Section 1506-A(b).) Employees already suffered a twelve percent wage reduction in 2010, and many simply cannot afford the assessment remaining in their plan requires under Measure B's VEP provisions.

Just as was the case in *Nielson* and *Pettypool*, the "option" that Measure B purports to offer is anything but "voluntary." This is especially troubling here because this case involves constitutionally-protected vested rights: the vested right to a pension on terms similar to those when work commenced as well as a right to a pension "*based on the system then in effect*." (*LA Firefighters, supra,* 210 Cal.App.3d at 1102; *Pasadena Police, supra,* 147 Cal.App.3d at 703.) Not only does the VEP alter the terms of pension that were in effect when most AFSCME members commenced work for the system, but it is also not the same pension plan to which they earned a vested right when they started. For this reason the VEP constitutes an impairment of contract.

Importantly, a waiver of such a Constitutional right must be freely, voluntarily, and intelligently made. (*See In re Johnson* (1956) 62 Cal.2d 325, 335.) Measure B does not present such an option. As demonstrated above, it hardly suffices to merely label the choice as "voluntarily," where it is objectively clear that it is not.

bb. All Provisions of the VEP Constitute an Unconstitutional Impairment of Contract

Measure B's VEP Tier 2 plan constitutes a significant impairment of vested pension rights because it:

- Increases the service retirement age from fifty-five to sixty-two (Section 1507-A(b)(iii));
- Raises eligibility for service retirement from thirty years of service by six months annually) (Section 1507(A)(b)(iv));
- Reduces the pension annuity formula with respect to such employees' future service from 2.5% per year of service to 2% (Section 1507-A(b)(i));
- Redefines the average compensation on which the pension annuity is formulated from the highest twelve consecutive months to the average of highest three years of pay (Section 1507-A(b)(vi));
- Increases the number of hours that constitute a year of service from 1,739 to 2,080 (Section 1507-A(b)(vii));
- Reduces survivorship benefits available for death before retirement as well as for a spouse or domestic partner and/or children designated at the time of retirement (Section 1507-A(d)(i), (d)(ii)); and
- Significantly extends the minimum service or vesting requirements.

And as previously demonstrated, it reduces inflation protection by capping the COLA at 1.5% and redefines the criteria for a disability benefit. (Sections 1507(b)(v), (d), (e).)

Any attempt by the City to justify subsections (b)(iii) and (b)(iv) of Section 1507-A under authority of *Miller v. State* is unavailing. (*Miller v. State* (1977)18 Cal.3d 80.) That case involved a challenge to a government code amendment that lowered the mandatory retirement age. The court held that public employment is held by statute and not contract and that the legislature could reduce the tenure of a civil servant. As such, the plaintiff's pension rights were not impaired. (*Id*. at 813, 814.) This case is different. In *Miller*, the reduction in the mandatory retirement age resulted in the plaintiff's inability to satisfy the conditions precedent to receiving a maximum pension benefit. However, unlike the instant case, the age and service retirement formula provisions in *Miller* were not changed to the plaintiff's detriment. In addition, *Miller* focused on the fact that public employment is governed by statute, rather than contract, and public employees have no contractual right to continued employment in this state. However, by increasing the years of service requirement, as subsection b(iii) and b(iv) of Section 1507-A do, the City not only altered the employment right but also changed the conditions of the contract itself; that contract included decades of MOUs between the AFSCME bargaining units and the City as well as the relevant provisions of the SJMC incorporated into their terms. (SJMC 3.28.1200, et seq.)

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Therefore, the legal authorities discussed in previous sections apply with equal force to the "Hobson's Choice" imposition of the VEP plan. Under such authorities, Section 1507-A constitutes a substantial impairment of the pension contract with no commensurable benefit to the employees.

b. Alterations to Retiree Health Benefits

Section 1512-A of Measure, pertaining to retiree healthcare, constitutes an impairment of contract by:

- "unvesting" the right to retiree health benefits; changing the definition of "lowest cost plan" in a way that reduces the promised subsidy towards the premium of retiree health; and
- leaving open the possibility that employees will contribute towards more than fifty percent of the cost of retiree health; and
- requiring active employees to contribute towards the City's unfunded liabilities ("UALs") with respect to retiree health.

Because Measure B fails to provide its affected employees with a commensurate benefit to offset these detriments, Section 1512-A is an unconstitutional impairment of contract.

Like pension benefits, retiree health benefits may be considered deferred compensation, and an employee can become contractually vested in those benefits upon accepting employment. (*Thorning v. Hollister School District* (1992) 11 Cal.App.4th 1598, 1605-1606); *Sappington v. Orange County Unified School District* (2004) 119 Cal.App.4th 954; *see also* 83 Ops.Cal.Atty.Gen 14, 2000.) Once vested, an employee gains "an irrevocable interest in the benefit," which is treated as a form of deferred compensation in this state. (*REAOC, supra,* 52 Cal.4th at 1189 fn.3; *Thorning, supra,* 11 Cal.App.4th at 1605-1606.)

The California Supreme Court recently held that a public agency may create a vested right to retiree healthcare through express contact language, implied terms of a contract, or an implied contract, if there is no statutory prohibition against such arrangements. (*REAOC, supra,* 52 Cal.4th at 1179.) Such is the case even when a contract is replete with explicit durational language or does not include vesting language. (*Sappington, supra,* 119 Cal.App.4th at 951, 955.) Therefore, a vested right can be created even if the public agency does not state its intent to do so in a resolution, ordinance, or other formal legislation. (*See generally, REAOC, supra,* 52 Cal.4th at 1171.)

A memorandum of understanding ("MOU") between a union and public agency can serve as a contract creating a vested right, that once approved becomes a contractual obligation which is "binding and constitutionally protected" and must be interpreted to "execute the mutual intent and purpose of the parties." (*REAOC, supra,* 52 Cal.4th at 1182 (citations omitted).) This is especially true where, as here, the MOUs are adopted by the City Council. In order to determine what a public

agency promised its employees, courts look to the contract and intrinsic evidence to determine whether the parties intended to create a vested right. (*REAOC, supra,* 52 Cal.4th at 1191.)

Courts recognize that public employees may earn vested contractual rights to retirement benefits by ordinance even in the absence of a MOU recognizing such rights. (*See Wills, supra,* 187 Cal.App.3d at 791 ("Pension laws enacted by city ordinance constitute contract rights in California."); *Thorning, supra,* 11 Cal.App.4th at 1598 (involving retiree health).) Therefore, with respect to vested rights, there is no difference between deferred compensation granted through a Memorandum of Understanding or through a statute or ordinance. A constitutionally protected vested right can be created through both methods. (*See County of Orange v. Assoc. of Orange County Dep. Sheriffs* (2011) 192 Cal.App.4th 21, 29-30, 46-47 ("*OCDSA*"); *Wills, supra,* 187 Cal.App.3d at 791; *Thorning, supra,* 11 Cal.App.4th at 1598.)

In holding that the promised retiree health benefits were protected against unilateral termination by the agency in the same manner as pension benefits, the *Thorning* court stated, "The principle that an employee begins earning pension rights from the first day he starts employment is not limited simply to pension cases but extends to other types of benefits." (*Thorning, supra,* 11 Cal.App.4th at 1606, 1607 (citation omitted).) *Thorning* was a case involving retiree health.

i. AFSCME Members Earned a Vested Right to Retiree Health Upon Commencing Employment With the City

Section 1512-A(b) of Measure B is unconstitutional because it attempts to un-vest a benefit in which AFSCME members have a vested right. The *Thorning* court held that the following policy granted the vested retiree health benefits in that case: "Any members retiring from the Board after at least one full term shall have the option to continue the health and welfare benefits program if coverage is in effect at time of retirement …." (11 Cal.App.4th at 1604-1605.) Similarly, the *Sappington* court concluded that language stating that the employer "shall underwrite the cost of [medical insurance] for all employees who retire" created a vested right to subsidized medical benefits.

Even though neither clause contained language explicitly recognizing a vested right or specifying that the right would exist in perpetuity, it was sufficient to create a vested right. Such is the case here, where the City clearly promised AFSCME members a right to receive retiree medical benefits upon meeting certain enumerated conditions.

Decades of MOUs between the City and its AFSCME bargaining units entitled AFSCME members to the retirement benefits set forth in the City's Municipal Code with language similar to the following: "Current retirement benefits will continue during the term of this Agreement, except as

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described herein, and shall be set forth in the Municipal Code." Since 1984, the SJMC promised each individual member that he/she was "eligible to participate in a medical insurance plan sponsored by the city provided that the member satisfie[d] the following requirements:

> 1. The member retires for service or disability pursuant to the provisions of this chapter; and
>
> 2. The member applies for medical insurance coverage at the time of his or her retirement in accordance with the provisions of the medical insurance plan, and agrees to pay any applicable premiums.

(SJMC § 3.28.1970.) Pursuant to Section 3.28.1950 of the Code, a member could be "entitled to medical insurance coverage in an eligible medical plan, as specified in Section 3.28.1970, if the member satisfies the requirements of Subsection A., Subsection B., or Subsection C." In relevant part, subsection A of 3.28.1950 stated that a member qualified for retiree health benefits if he/she retired for service of disability and was "entitled to fifteen or more years of service." To this day, these provisions remain in the San José Municipal Code.

These provisions unambiguously granted members a vested promise to retiree healthcare upon retiring for service or disability with fifteen years of service credit. Accordingly, those who took a job with the City after 1984 when the benefit was created under the Federated System relied on this promise of deferred compensation in accepting less pay than was offered in the private sector. For decades, employees relied on this promise within the Municipal Code and the consistent representations by the City while staying in its employ.

As was the case in *Thorning*, that right to the expectation of health benefits vested in AFSCME members upon their first day of work. Failing to recognize a vested right on the part of San Jose employees would create an inequitable and unconstitutional paradox: while employees are required to contribute towards retiree health from the day they started working for the City, they were not guaranteed the benefit towards which they were paying. (*See* SJMC 3.28.385(C).) The court in *AFT Michigan*, in holding unconstitutional the state law unilaterally imposing upon teachers a three percent increase in contributions into a retiree healthcare funding account, stated:

> We cannot envision a court approving as constitutional a statute that requires certain individuals to turn a portion of their wages over to the government in return for a 'promise' that the government will return the monies, with interest, in 20 years when the government retains the unilateral right to 'cancel' the 'promise' at any time and does not even agree that, if they do so, the monies taken will be returned. School employees cannot constitutionally be required to 'loan' money to their employer school districts, with no enforceable right to receive anything in exchange and without even a binding guarantee that the "loan" will be repaid."

(*AFT Michigan,*297 Mich.App. at 635.)

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In this case, the anti-vesting language of Section 1512-A(b) gives the City that very power to discontinue the benefit for those who paid its UALs. Specifically, Measure B adds to the Municipal Code the following provision related to retiree health benefits: "No retiree health plan shall grant any vested right" and granting the City the right to "amend, change or terminate… [the] plan." (Section 1512-A(b).) Prior to Measure B the city recognized the vested nature of retiree health benefits, and, as a matter of law, such benefits are vested, and therefore their reduction or purported "unvesting" constitutes an impairment of contract. Further, because employees who have contributed their wages to the retiree health plan, and understood that by doing so they would receive the benefit upon retirement, Measure B impermissibly takes a property right and substantially undermines the contractual expectations of employees. Therefore, the anti-vesting language within Section 1512-A(b) of Measure B constitutes an impairment of contract as applied to anyone who started working for the City prior to its effective date, or who is required to contribute their wages to the retiree health program.

The fact that AFSCME's locals have been without an MOU governing their employment since 2011 does not change this outcome for several reasons. First, members earned a vested right to receive retiree health on their first day of work. (*Thorning, supra,* 11 Cal.App.4th at 1606, 1607 (citation omitted).) Therefore, anyone who commenced work prior to 2011 was already vested in this right because "[r]ights which accrued or vested under [an] agreement will, as a general rule, survive termination of the agreement." (*Litton Financial Printing Div. v. Litton Business Sys. Inc.* (1991) 501 US 190, 207; *Thornton v. Victor Meat Co.* (168) 260 Cal.App.2d 452, 471; *see also Butchers' Union Local 229 v. Cudahy Packing Co.* (1967) 66 Cal.2d 925, 932.)

Whether by MOU or the SJMC, AFSCME members were explicitly granted retiree health benefits, which may not be unvested as Measure B purports to do.

ii. Employees Were Vested in the Right to a Subsidy of the Premium to the Lowest Cost Health Plan and the Right Not to Pay for the City's Unfunded Liabilities

Since 1984, the SJMC granted to AFSCME members the right, upon fulfilling the conditions set forth in SJMC sects. 3.28.1950 and 3.28.1970, to receive a subsidy for the premium of retiree health as long as they enrolled in what the Code defined as a "lowest cost plan." The SJMC also guaranteed that employees would contribute towards no more than fifty percent of the normal costs of retiree health and that only the retirement board would adjust the contribution rates attributable to retiree health. Because the SJMC explicitly granted these rights, they became a part of the express contract with the City. (*See REAOC, supra,* 52 Cal.4th at 1171.) Furthermore, Federated members

became entitled to the aforementioned rights by virtue of their vesting in the expectation of receiving retiree health benefits upon fulfilling the requisite conditions. Therefore, Section 1512-A of Measure B is unconstitutional insofar as it impairs these rights.

"[U]pon acceptance of public employment [one] acquire[s] a vested right to a pension *based on the system then in effect*" and "on terms substantially equivalent to those then offered by the employer …." (*LA Fire, supra,* 210 Cal.App.3d 1095, 1102 (citations omitted) (emphasis in original); *Pasadena Police, supra,* 147 Cal.App.3d at 703.) In this case, retiree health benefits--like pension benefits--are also a form of deferred compensation to which AFSCME members earned a vested right upon accepting employment. Therefore, it follows that the employees' vested right to retiree health benefits is also based upon the system that was in effect at the time of acceptance and the employees are entitled to benefits substantially equivalent to those in place when they accepted employment with the City. The following sections discuss benefits in place when the employees starting work with the City, which were also granted to them by express contract through the Municipal Code.

iii. Employees Had Vested Right to Having the City Subsidize the Premium of the Lowest Cost Retiree Health Plan as Defined by the Code

The SJMC, at section 3.28.1980(B)(1), has always required the City to subsidize the cost of retiree health in an "amount equivalent to the lowest of the premiums for single or family medical insurance coverage, for which the member or survivor is eligible and in which the member or survivor enrolls under the provisions of this part, which is available to an employee of the city at such time as said premium is due and owing." According to this express contract, employees could expect that upon retirement, the City would cover the entirety of their retiree health premiums as long as they enrolled in the lowest cost plan available to active employees and in which they were enrolled. Pursuant to the language of the SJMC, the "lowest cost plan" was one which the retiree qualified for and enrolled, even if there was a lower cost plan available to active employees for which the retiree did not qualify.

Section 1512-A(c) of Measure B redefines "low cost plan" with respect to retiree healthcare benefits as "the medical plan which has the lowest monthly premium available to any active employee in either the Police and Fire Department Retirement Plan or the Federated City Employees' Retirement System." In doing so, the City eliminated the requirement that the "lowest cost plan" be the one in which a particular retiree was actually eligible to enroll. As a result of Measure B, the "lowest cost plan" may be one for which the retiree does not even qualify. Therefore, if the premium of the lowest cost plan available to actives is below that of the lowest cost plan in which the retiree is actually eligible to enroll, the retiree must pay the difference between the premiums. (See SJMC

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3.28.1980(B)(2).) Given the fact that healthcare is more expensive for retirees than it is for active employees (*see generally, REAOC, supra,* 52 *Cal. 4th* at 1171), AFSCME members can no longer expect a full subsidy of the cost of the premium for retiree health in the event that they enroll in the lowest cost plan for which they are eligible.

Importantly, upon passage of Measure B, the City adopted a "High Deductible Health Plan," ("HDHP") option for its active employees which offers limited benefits and only after the employee has paid a significant annual deductible. The plan, by imposing a high deductible, essentially shifts to the employee the premiums the City would otherwise be required to pay its insurance carrier for equivalent coverage. It cannot be said, therefore that the "cost" of the plan is lower, even though the premiums paid by the City may be. Because the HDHP comes with a lower premium, as a result of shifting the cost onto a high employee-paid deductible, the City has now predicated its retiree health contribution rates on the HDHP insurance premium, even though few active employees elect it, as do even fewer retirees. The effect is that the City has drastically reduced the premiums it applies towards the retiree healthcare benefits that retirees and active employees enjoyed, while directly shifting the cost onto them through the high deductible. Whereas, in the past, the retiree health premium was based on a Non-Deductible HMO plan, it is now computed with respect to the HDHP. The unfairness of this arrangement is patent, especially in light of the fact that the City has told employee the retiree health benefit is "vested" and that the City will continue their benefits with no cost to them. This change in the nature of the benefits, applicable to current, vested employees and retirees, substantially undermines the retiree health benefit to which employees have contributed and that the City is obligated to provide.

Because Federated members earned a vested right to the retiree health benefit permitted under SJMC 3.28.1980(B)(2) upon retirement, and a meaningful benefit at that, Measure B unconstitutionally impairs that contractually-based expectation.

iv. Employees Had Vested Right to Pay No More Than Fifty Percent of the Normal Cost of Retiree Health

A substantial increase in an employee's contribution rate towards retirement benefits that is not explicitly permitted under the terms of the retirement system is an unconstitutional impairment of contract. *(Compare Allen, supra,* 45 Cal.2d at 131 (change not permitted by charter or city code) *with SD Firefighters* (1983) 34 Cal.3d 292, 300-302 (change permitted by charter and city code).)

Since 1984, the SJMC required members to contribute towards fifty percent of the cost of retiree health, required the City to pay all UAL for retiree health, and exclusively authorized the retirement board to adjust contribution rates with respect to retiree health. (SJMC 3.28.385(c).) That

provision stated: "Contributions for other medical benefits *shall* be made by the city and the members in the ratio of one-to-one." (Emphasis added.)

Section 1512-A(a) of Measure B now impedes this contractual right by requiring that "[e]xisting … employees … contribute a *minimum* of 50% of the cost of retiree healthcare, including both normal cost and unfunded liabilities." (Emphasis added.) Therefore, Section 1512-A(a) is unconstitutional insofar as it requires its employees to finance more than half the cost of retiree health. Through the SJMC, the City only specifically reserved its right to adjust funding ratios to comply with the requirements of 401(h) trust; the funding status of the trust is not at issue in this case. (SJMC 3.28.1995.) Therefore, Measure B impermissibly alters employees' contributions expectations with respect to retiree health.

v. Measure B Impermissibly Requires Members to Pay Towards the Unfunded Liabilities Associated With Retiree Health

Measure B imposes an obligation on active employees to contribute a "minimum" of 50% of the cost of the City's entire OPEB liabilities (Section 1512-A(a).) Prior to Measure B, such obligations were born by the City. Also, because Measure B purports to "unvest" retiree health benefits, and eliminate any obligation to actually provided the benefits to retirees, it imposes on active employees the obligation to make payments to the City's plan that quite possibly exceed the value of benefits they, themselves, will receive. Therefore, it imposes on employees the obligation to make contributions to the system's retiree health fund and does not distinguish between the unfunded liabilities attributable to active, deferred-vested or retired system members. Rather, a reduced number of active employees--those who have remained in city service after layoffs, early retirements and wage cuts--are required to shoulder unfunded liabilities with respect to benefits obligations for System members who left employment with a vested pension and are now working elsewhere or who have retired.

Recently, in *AFT Michigan*, a Michigan court of appeals described a similar arrangement as improper because "while the fund in question funds retiree health care benefits for present retirees, the active employees whose wages are taken have no vested right themselves to the receipt of health care benefits upon their own retirement." (*AFT Michigan*, 297 Mich.App. at 605.)

In any event, the SJMC expressly placed upon the City the burden for financing unfunded liabilities associated with the retiree health plan. Section 1512-A(a) is unconstitutional insofar as it impairs a member's vested right to not have to contribute towards these UAL. In *Wills*, a city began withholding money from its employee's paychecks to help finance its COLA-related unfunded liability attributable to retirees, "currently active past service members, and future service active

members." (187 Cal.App.3d at 780, 784.) The city's municipal code placed on the city the responsibility for making "contributions for all amounts necessary to fund current and past service liability for all pensions and all other benefits allowable under the retirement system." (*Ibid*.) The court concluded that the city's "retirement system is one, actuarially based, integral system" and that "the COLA fund is merely a different part of a single overall pension plan." (*Id*. at 789.) That "reveale[d] an intention by the city to cover past unfunded liabilities not only for the pension system but for the COLA system as well." (*Id*.at 789.) Notably, the court stated, "Although a COLA system was not in effect at the time these two sections were enacted, the city has manifested an express intent to cover past unfunded liability in the entire pension system." (*Ibid*.)

AFSCME's case is even stronger than *Wills* because the City incurred responsibility for financing all UALs with respect to retiree health. Here, the Federated pension and retiree health funds were also part of a single overall retirement plan known as the "Federated City Employees Retirement Plan" which included the provisions set forth in Chapters 3.16, 3.20, 3.24, and 3.28 of the Municipal Code. (SJMC § 3.28.010(B).) Chapter 3.28 included provisions related to pensions and retiree health.

Here, prior to Measure B, the City was required to finance the UALs for all benefits conferred under the plan, including OPEBs. S JMC sect. 3.28.850 required that the City make, after July 1, 1975, "current service contributions" to the system as a percentage of compensation earned. "Said percentage shall consist of the sum of two rates, the first being the one which is hereinafter referred to as 'city's regular current service rate of contribution,' and the second being the one which is hereinafter referred to as '*city's current service deficiency rate of contribution*.'" (*Id*. (emphasis added).) With respect to the City's current service deficiency rate of contribution, SJMC sect. 3.28.880 states that it:

> shall be such as may hereafter be necessary to make up, over a period of thirty years, any existing deficiency in the amounts of current service contributions theretofore contributed by members and by the city for the payment of the cost of ***all allowances and other benefits*** which are or will become payable to members on account of current service rendered before the effective date of the latest deficiency rate, such deficiency being that resulting from amendments hereafter made to this system ***or as a result of experience under this system.*** *Until the amount accumulated in the retirement fund from contributions of members and the city on account of current service equals the present value of all amounts thereafter payable from the retirement fund on account of current service*, *the city* ***shall*** *make monthly (or biweekly, if members contribute biweekly) contributions, to make up any deficiency,* ***at the current service deficiency rate established by the retirement board.*** Such rate shall be established and from time to time changed by the retirement board, whenever necessary, to accomplish the above-specified objective.

(Emphasis added.) Section 3.28.850 appears to require that the City solely finance the unfunded liabilities of the System for "all allowances and other benefits" attributed to "current service," or "all city service rendered by a member *after June 30, 1951*." (SJMC 3.24.1000(C) (emphasis added).)

It is clear that SJMC sect. 3.28.850 is not limited to pension benefit financing and that it also governs the City's obligations with respect to the UAL related to retiree health. Had the City intended to limit this section to the financing of UAL, it certainly would have done so. First, Chapter 3.28 of the Code specifically refers to "pensions" throughout, and specifically distinguishes pension benefits and allowances from "other benefits." In fact, SJMC sect. 3.28.900 specifically distinguishes pensions from "other allowances" and "other benefits": "The City's prior service rate of contribution .... will be sufficient to pay, when due, all pensions, *allowances and other benefits* which are or will become payable under this system on account of prior service rendered prior to July 1, 1975." (Emphasis added.)

Furthermore, the Code also created a universal "retirement fund" called the "San José Federated City Employees Retirement Fund" ("SJCERF") into which contributions towards pensions and other retirement benefits were paid and out of which benefits were funded. (SJMC § 3.28.300.) Subsequently, the City specifically established the 401(h) retiree medical benefits sub-account within the pension trust. (SJMC § 3.28.380(A).) It even permitted the *co-mingling* of funds within the 401(h) "with other monies in the retirement fund solely for the purposes of investment." (*Ibid*.)

Finally, it is evident that the City treated its pension and OPEB obligations as one and the same. For example, the City's "Comprehensive Annual Financial Report[s]" for the Federated System included financial statements and analyses of both pension and OPEB health benefits. Therefore, like in *Wills*, it is clear that the pension and retiree health funds were part of the same overall retirement plan. Also similar to *Wills*, it is clear that the SJMC required the City, and not its members, to finance any OPEB UALs for service rendered after June 30, 1951.

vi. Measure B Impairs On Members' Right to Have Contribution Rates Adjusted Exclusively by Retirement Board

The SJMC, as incorporated into decades of MEF and CEO MOUs, provided that AFSCME members working after 1984 earned an express contractual right to having their retiree health contributions adjusted solely by the retirement board. Therefore, upon commencing employment, AFSCME members could reasonably expect to be held responsible for contributing towards fifty percent of the retiree health normal costs and that the board would retain exclusive authority to

compel increased contributions towards those normal costs. Furthermore, they could reasonably expect the Board to only compel the City to increase contributions towards retiree health UALs. At all times pertinent to this litigation, prior to Measure B, the retirement board acted within its authority granted by the Code and only required that Federated members contribute towards the City's normal costs of retiree health on a one-to-one basis. Measure B impairs these rights by requiring members to make contributions of fifty percent or more towards retiree health UALs.

The Retirement Board is an entirely different entity than the City of San José. Pursuant to the state Constitution, "The retirement board of a public pension or *retirement system* shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system. The retirement board shall also have sole and exclusive responsibility to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries." (Cal. Const. art. XVI, § 17(a) ("Pension Protection Act") (emphasis added).) As previously discussed, pension and retiree health benefits are provided under the same City retirement plan; therefore, the Pension Protection Act also applies with respect to the Board's authority over retiree health, and the Board is solely responsible for administering the retiree health plan. Therefore, neither the City nor its electorate may usurp that authority in contravention of its employees' reasonable retirement expectations. (*See Hudson v. Bd. of Administration* (1997) 59 Cal.App.4th 1310, 1330-1332; *OCDSA, supra,* 192 Cal.App.4th at 21.)

Consistent with these constitutional principles, the SJMC vested in the retirement *board*, and not the City, the authority to adjust contribution rates related to retiree health and other benefits. (SJMC §§ 3.28.200, 3.28.385.)[2] It also authorizes the Board to adjust the *City's* contribution rates towards retiree health UAL. (See SJMC 3.28.880.) However, nowhere does it grant the City or the retirement board a right to compel contributions from its employees towards retiree health UAL.

Despite this, section 1512-A(a) of Measure B requires that active employees "contribute a minimum of 50% of the cost of retiree healthcare, including *both normal cost and unfunded liabilities*." (Emphasis added.) Because the electorate adjusted City employees' contribution rates and foisted upon them responsibility for financing retiree health UALs--despite the fact that only Board could do so -- Measure B further impairs the right to only have the retirement board affect contribution rates with respect to retiree health.

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[2] Any argument that SJMC 3.28.755 gave the *City* authority to require members to make additional contributions must be rejected because section 3.28.755 is a recent City enactment and does not affect the vested rights of employees that were realized when they started working prior to its promulgation. Also, SJMC 3.28.385 is specific with respect to retiree medical benefits while SJMC 3.28.755 applies to "retirement benefits" in general. The more specific provision applies.

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vii. 2009 Retiree Health Contract Does Not Eliminate Vested Rights Prior

Any argument that the Union's agreement for its members to pay towards the City's UALs in 2009 justifies Measure B's retiree health funding provisions is misplaced. First, those members who started work with the City prior to the execution of that agreement earned a vested right upon commencing employment; as previously explained, that right included having the City pay towards its retiree health UALs. Once vested in that benefit, the right could not be defeated by the City without providing its employees with a commensurate benefit. Because it did not provide any such benefit, that agreement was invalid with respect to such employees. Secondly, as will be discussed below, a union cannot bargain away its members' constitutionally vested rights. (*See San Bernardino Public Employees Assn. v. City on Fontana* (1998) 67 Cal.App.4th 1215, 1255 ("*Fontana*").) Finally, the doctrines of estoppel should prevent that agreement from setting precedent in the future.

At the time the Union agreed to those terms, it did so in part because of the following attendant circumstances: a guaranteed salary increase for the remaining year of the contract, a healthy economy, and the healthy financial situation of the City. AFSCME was unaware of the approximately 20% reduction in staffing and drastic reductions to compensation (reduced pay, increased health benefit cost, etc.) that the City would affect in the future. The effect of these changes had a material impact on the significance of the 2009 agreement and resulted in significantly greater costs to active employees under that agreement. Further, the Union was unaware of the City's future plans to design Measure B and put it to the voters. As a result of these intervening events, the 2009 agreement was never fully implemented by the City and, indeed, key provisions have been abandoned by the parties. It is AFSCME's position that the parties are no longer operating under the agreement, if they ever were.

vii. Extrinsic Evidence Demonstrates a Contract Granting Vested Rights to Retiree Health

Even if the MEF and CEO MOUs combined with the SJMC did not expressly grant the contractual rights discussed above, it is clear that these rights vested by means of an implied contract or as the implied terms of an express contract for retirement benefits.

Courts may look to extrinsic evidence and the parties' course of conduct in determining whether the parties' intended to create vested rights. (*See Sappington, supra,* 119 Cal.App.4th at 954-55; *see also REAOC, supra,* 52 Cal.4th at 1191.) Here, there is substantial extrinsic evidence demonstrating that the retiree health benefits discussed herein were vested.

For example, in 2009, Debra Figone, the City Manager and a named defendant in this case, circulated a memorandum to all City employees in which she referred to retiree health as a "'vested

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benefit' similar to the pension benefit itself" and that the City would "not be recommending changes to retiree healthcare benefits (as specified in the Municipal Code) for current employees or current retirees at this time." This demonstrates that the City itself considered the benefits vested and this representation induced reliance by its employees.

Retirement handbooks, annual factsheets, and brochures distributed to City employees by its Retirement Services department reiterated facts such as: employees were eligible for retiree health after fifteen years of service upon service or disability retirement and that the City would cover the entirety of the premium for the lowest cost plan available to active employees and for which they were eligible. Human Resources reiterated these facts to new employees during their orientations. In fact, in its brief in support of its Motion for Summary Adjudication, the City stated that, with respect to its failure to specify a specific contribution rate for retiree health unfunded liabilities, it "was simply not focused on the unfunded liabilities at the time of the legislation." (City's MSA, p. 32:6-7.) This fact demonstrates that the City did not intend for its employees to finance its retiree health UAL when it promulgated the relevant Code sections.

For the these reasons, Section 1512-A of Measure B constitutes an unconstitutional impairment of contract and should be stricken in its entirety.

3. City's Anticipated Defenses

a. Measure B is Not a "Reasonable Modification"

Measure B's provisions bear no material relation to the theory of a retirement system or its successful operation; they simply allow the City to escape from its obligation to provide its employees with these forms of deferred compensation with which it previously enticed them; furthermore, the charter amendment provides no comparable advantage. It is not enough to state that the pension system is underfunded, even severely so, to justify a reduction of vested rights. This has long been the case under California law, as summarized in *Abbott II*:

> [Defendants] contend that the cases at bar are distinguishable from the cited case because the change in question was necessary to make the city's pension program actuarially solvent and economically sound. This conclusion is based upon an actuarial study and report. It is argued that the reasons for this change bring these cases within the rule of *Kern v. City of Long Beach*, 29 Cal.2d 848, 855, and *Allen v. City of Long Beach*, 45 Cal.2d 128, which recognizes the authority to change pension benefits, even though rights have vested, in order to 'maintain the integrity of the system.' This argument neglects consideration of the requirement that any such change must be reasonable and must be related to the integrity of the system as applied to the vested rights under consideration. There is no showing in the instant cases that the amendments under consideration "bear any material relation to the integrity or successful operation or to the preservation or protection of the *pension program applicable to these plaintiffs*.

(*Abbott II, supra,* 165 Cal.App.2d at 519 (internal citations omitted) (emphasis in original)); *see also Pasadena Police, supra,* 147 Cal.App.3d at 704 n.3 ("However, in the absence of a clear and unequivocal declaration in the pension provisions that benefits are payable only to the extent of available funds from specified contributions, the liability to pay promised pension benefits is a general obligation of the city. *Suggestions of fiscal emergency have been rejected on the particular facts of several cases*.") (citations omitted) (emphasis added).)

In a subsequent case, again considering the validity of changes made to the San Diego pension plan, the Court of Appeal reiterated that a detrimental pension modification is only "reasonable" if it comes with a commensurate benefit with respect to the particular plan participant, holding "[t]he validity of attempted changes in vested pension rights depends upon the advantage or disadvantage to the individual employee whose rights are involved, *and benefits to other employees cannot offset detriments imposed upon those whose pension rights have accrued*." (*Wisley, supra,* 188 Cal.App.2d at 486 (citing *Abbott I, supra,* 50 Cal.2d at 453.) The *Wisley* court continued:

> It is obvious that the increase in the percentage of the employee's contribution to the retirement fund is a detriment, and it is undisputed in this case that by successive amendments these contributions were gradually increased from 1 per cent to 8 per cent. It thus becomes necessary to ascertain whether these detriments have been accompanied by commensurate benefits to the employees. While the defendants concede that the 1935 amendment did nothing more than increase the salary contribution from 2 per cent to 4 per cent and conferred no commensurate benefit to the employees, the defendants contend that through the years there has been a continual expansion of pension benefits for all employees and that these expanded benefits make the increases in salary contributions reasonable.

(*Id*. at 486.)

Simply, a fiscal desire on the part of a governmental agency to reduce the cost of the obligations it has undertaken does not justify impairment of a contract. This is especially so where the agency is responding with respect to its own affairs and contracts, as a "market participant," and not as a regulatory entity. Courts have repeatedly rejected such justifications for reducing pension and retirement benefits under the contracts clause. (*See Pasadena Police Officers, supra,* 147 Cal.App.3d at 704 n.3; *see also United States Trust Co. v. New Jersey* (1977) 431 U.S. 1; *Allen, supra,* 45 Cal.2d at 133; *Abbott II, supra,* 50 Cal.2d at 455; *Wisley, supra,* 188 Cal.App.2d at 487; *Frank, supra,* 56 Cal.App.3d at 246.)

<u>b. The City's "Reservation of Rights" Argument</u>

The City contends that employee retirement benefits may be reduced without violating the contracts clause because the Charter contains purported "reservation of rights clause" ("Clause"). The City's argument is that the retirement benefits "contract" cannot be breached if the provisions of

the "contract" allow for its amendment. The argument fails as a matter of fact and law, and was more fully briefed in AFSCME's Opposition to the City' Motion for Summary Adjudication of this particular issue. In any event, the Clause is inapplicable to retiree health and could not prevent the vesting of such benefits.

i. The Clause Did Not Prevent the Vesting of Any Benefits

Factually, the charter provision does not *clearly and unequivocally* indicate to employees that their pension benefits are subject to diminution, as is required pursuant to *Bellus*, *England*, and other cases previously discussed. In addition, the legislative history of the particular charter provision indicates that its intent was to allow for increases in benefits to provide flexibility, or with respect to establishing other, second-tier plans, as necessary, for future employees. The legislative record, when properly construed, demonstrates that at the time the various parties and constituents understood the provision to mean new plans could be adopted, but employees could not be pushed into a lesser term after having worked under a superior plan. As discussed above, at the time the provision was added to the Charter, California recognized a right to receive the pension benefit promised upon commencing employment, and so the Clause must be interpreted consistently with this constitutionally-derived rule.

Importantly, the California Supreme Court has already rejected the exact argument now raised by the City. The City relies on a single authority for its central defense to Measure B, *Walsh,* 4 Cal.App.4th 682, which considered changes to the Legislative Retirement Law ("LRL"), a retirement system "unique" among governmental pension systems. (*Id*. at 698.) During both Walsh's and Eu's service under the LRL, the State Constitution contained an "express reservation of rights clause" which permitted the limitation of benefits under the LRL. (Cal. Const Art. IV, sec. 4, par. 3.) However, this reservation of rights applied only with respect to Walsh, and not Eu's service. The courts reached different conclusions in each case by recognizing the factual and historical genesis of each, which the *Walsh* court summarized:

> The LRL does appear unique among California governmental pension plans. In this state governmental pension plans are typically funded by (1) the creation of an actuarially based retirement fund; (2) a provision for continuous appropriations or continuing obligations of the governmental entity; or (3) some combination of both," and yet, at the time Walsh served under the LRL "the Legislature did not create an actuarially based fund and did not provide for continuous appropriations for the payment of benefits. Instead, funding for the payment of benefits under the LRL was left to future year-to-year appropriations.

(4 Cal.App.4th at 698.) Thus, at that time the LRL was not a *pension system*, rather:

> The LRL, as it was enacted and during the period of Walsh's service, was unique in more ways than one. For one thing, the benefit and eligibility criteria of the LRL were

> under the direct control of the very persons who expected to receive benefits under it. For another thing, the LRL and its numerous amendments were enacted without any attempt to create an actuarially based fund or to provide continuing appropriations for its benefits, and thus the LRL was not subjected to comprehensive planning with respect to the benefits which would become payable and the source of funds to pay them. As a result the LRL was peculiarly susceptible to the possibility of conferring unwarranted windfall benefits to its members and of creating an unreasonable drain on the public fisc.

(4 Cal.App.4th at 702). However, "[i]n the mid-1970's the Legislature began to reform the LRL into an actuarially sound pension system. The legislative efforts in this regard included reducing benefits under the LRL to those consistent with a sound pension system, the creation of an actuarially based fund for the payment of future benefits, and, in 1977, the enactment of a continuing appropriation to support the payment[s]" all of which occurred "well after Walsh's service ended and cannot apply to him." (4 Cal.App.4th at 698 n. 5). In any event, The *Walsh* court directly addressed its holding in light of the earlier *Eu* decision (although Eu's service under the LRL was well after Walsh's):

> As we have previously noted, in 1977 the Legislature enacted a continuing appropriation in support of the LRL. We have no doubt that incumbent members of the Legislature at the time of the [enactment] had contractually vested pension rights under the LRL which would be protected under the contract clause. The question whether a former member of the Legislature acquired a contractual right to wholly unmodifiable pension benefits when he served during a time when the LRL was neither actuarially funded nor supported by a continuing appropriation, was not a question which was implicated in the *Legislature v. Eu* decision.

(4 Cal.App.4th at 700 n. 6 (citations omitted.))

The *Eu* court held that a "reservation of rights" clause did not prevent vesting of pension rights for incumbent legislators. It noted that the fact that the Constitution provided that "[t]he Legislature may, prior to their retirement, limit the retirement benefits payable to Members of the Legislature ...." neither stated nor implied that these rights are [] deemed inchoate and unprotected from impairment by the initiative process." (54 Cal.3d at 592.) Importantly, the Supreme Court noted: "*Significantly, we have never suggested that the mere existence of article IV, section 4, precludes legislators from acquiring pension rights protected by the state or federal contract clauses*." (*Ibid*. at 529 (citing *Allen, supra,* 34 Cal.3d at 119-120) (emphasis added).) This conclusion in fact accords with *Allen*, which held:

> [N]ot only is the existing law read into contracts in order to fix their obligations, but the reservation of the essential attributes of continuing governmental power is also read into contracts as a postulate of the legal order. The contract clause and the principle of continuing governmental power are construed in harmony; although not permitting a construction which permits contract repudiation or destruction, the impairment provision does not prevent laws which restrict a party to the gains 'reasonably to be expected from the contract. Constitutional decisions 'have never given a law which imposes unforeseen advantages or burdens on a contracting party constitutional immunity against change."

(34 Cal.3d at 120 (citations omitted).) Courts have since summarized the rule in *Allen*: "We must not overlook the qualifying rule, however, that the nature and extent of respondent's statutory obligation 'must be ascertained not only from the language of the pension provisions but also from the judicial construction of this or similar legislation at the time the contractual relationship was established.'"(*Newman,* 80 Cal.App.3d at 457-58 (quoting *Kern,* 29 Cal.2d at 850).)

To allow an exception to these doctrines, under a general, unspecific, reservation of rights clause, would damage these established constitutional principles, essentially allowing employees to embark on a contract, to labor under that contract, but have no ability to enforce that contract because of an alleged reserved power to amend. In other public contract contexts, such reservation of rights clauses are considered adhesion contracts and are rejected as a means of avoiding application of the contracts clause. (*See Blair v. Pitchess* (1971) 5 Cal.3d 258, 275-76; *Alameda County v. Ross* (1939) 32 Cal.App.2d 135, 144.)

ii. In Any Event, the Clause Did Not Affect to Retiree Health Benefits

Even if the court determines that the Clause prevented the vesting of pension benefits, it could not have done so with respect to retiree health. Article XV of the City's Charter governs the City's retirement systems includes Sections 1500 and 1503, which respectively address the City's duty to provide retirement systems and to continue existing retirement systems. These sections, which include language the City believes constitutes the reservation of power, must be construed in harmony with the remaining provisions in Article XV. For example, Sections 1505(a) and (b), which respectively address minimum service and disability retirement requirements, apply exclusively to traditional pension benefits. Additionally, the current service contribution rates set forth in Section 1505(c) of the Charter are inconsistent with those established for the retiree health program. Furthermore, when the Charter was adopted in 1965, there was no retiree health program in place. Therefore, in adopting the 1965 Charter, it appears as though the voters were concerned with traditional pension benefits, did not contemplate retiree health benefits, and did not intend for the aforementioned Clause to apply to a future retiree health benefit. In fact, up until this litigation, the City never communicated to Federated System members it's supposed right to amend retiree health benefits pursuant to these charter provisions.

Further evidence of the fact that the clauses did not apply to retiree health is the fact the SJMC specifically reserves to the City only the right to adjust retiree medical and dental funding ratios to comply with the requirements of the retiree health section 401(h) account. (SJMC §§ 3.28.1995, 3.28.2045.) If the clauses within the Charter did, in fact, apply to retiree health, than these Code provisions would be unnecessary. Furthermore, the fact that the City specifically reserved its

rights with respect to these provisions and not others further demonstrates that it has no such reservation of rights with respect to other aspects of retiree health.

Finally, even assuming the reservation of rights Clause extends to retiree health, the City cannot rely on these clauses to deny benefits to those who have already performed or substantially performed enough service to qualify for such benefits. (*Suastez v. Plastic Dress-Up Co.* (1982) 31 Cal.3d 774, 780; *Creighton v. Regents* (1997) 58 Cal.App.4th 237; *Kistler v. Redwoods Comm. College Dist.* (1993) 15 Cal.App.4th 1326).)

iii. "Course of Conduct" / Past Negotiation of Pension and OPEB

AFSCME anticipates the City to contend that the pension benefits and UAL contribution requirements cannot be vested because they are subject to negotiation under the Meyers-Milias-Brown Act ("MMBA") and that in the past the unions have negotiated increased pension contributions. With respect to AFSCME, this is factually incorrect: AFSCME has never proposed or agreed to a reduction of benefits or increased pension contributions with respect to active employees. There is nothing in the record to contradict this fact.

In addition, the 2010 Municipal Code amendment, section 3.28.755, providing authority for a one-time increase to contributions with respect to certain unions who agreed to such, did not involve AFSCME; nor was it applicable to AFSCME. That the City negotiated a one-time additional contribution with other municipal unions has no bearing on AFSCME or its member's expectations with respect to the pension benefits. Moreover, it has no bearing on whether the City may unilaterally impose a general UAL cost-sharing obligation.

Further, the City's argument is incorrect as a matter of law. In essence, the City argues that because Government Code section 3505.7 provides that a public employer may "impose" changes to the terms and conditions of employment after exhausting its duty to bargain in good faith, and because retirement benefits are a term and condition of employment subject to bargaining, the City may change pension benefits however it likes (provided it has exhausted its duty to bargain). This formulation is not only an unprecedented and remarkable extension of the reach of the MMBA, but it is legally incorrect.

First, California's vesting doctrine is constitutionally derived, whereas the MMBA is a legislative enactment subject to the authority of the Legislature. Unions may not negotiate away their members' vested constitutional rights. (*See Fontana, supra,* 67 Cal.App.4th at 1255; *Phillips v. State Pers. Bd.* (1986) 184 Cal.App.3d 651, 660, *disapproved on other grounds in Coleman v. Dep't of Pers. Admin* (1991) 52 Cal.3d 1102, 1123, n.8); *see also Soc. Servs. Union v. Bd. of Supervisors* (1990) 222 Cal.App.3d 279, 287.)

Secondly, the Legislature cannot pass laws that impair Constitutional protections. California's vested rights doctrine with respect to retirement benefits was recognized well before public employees were accorded the right to collectively bargain by the legislature when it passed the MMBA in 1968.

Simply, the requirement to bargain over terms and conditions of employment has only ever been subservient to the Constitution, its guarantees and protections. While no union can bargain away vested rights, the converse is not true: vested rights can be established as a result of the bargaining process. (*REAOC, supra,* 52 Cal.4th at 1179.) But that is not the *only* way they can arise, and no contractually-protected rights can be eliminated or reduced through bargaining, as that is beyond the power of either the employer or the union.

iv. The City's "Prospective Changes" Argument

The City has contended (as has a purported *amicus*) that pension changes affecting only prospectively-earned benefits are exempted from the *Allen* and California's vested rights doctrine. The court in *Pasadena Police, supra,* 147 Cal.App.3d at 695, dismantled this argument. That court considered a change that was "prospective only," in that it did not reduce or eliminate previously-earned COLA adjustments but only froze the COLA. (*Id*. at 702). The court noted that the amendments to the COLA provisions were "obviously disadvantageous" as they "substantially limited and reduced the protection which had previously been offered by a pension fully adjustable to changes in the cost of living." The court rejected the defendants' argument that the amendments did not impair vested contract rights of active employees because they purported to be prospective as irreconcilable with *Allen* and its progeny, noting that, for example, "One of the amendments invalidated in *Allen* increased each employee's contribution to the retirement system from 2 percent of his salary to 10 percent." (*Id*. at 102.) The *Pasadena Police* court added:

> On the same page on which the Supreme Court announced its comparable new advantages test, it invalidated the increase in contribution rate, because '[t]he provision raising the rate of an employee's contribution to the city pension fund from 2 per cent of his salary to 10 per cent obviously constitutes a substantial increase in the cost of pension protection to the employee without any corresponding increase in the amount of the benefit payments he will be entitled to receive upon his retirement.' In other words, where the employee's contribution rate is a fixed element of the pension system, the rate may not be increased unless the employee receives comparable new advantages for the increased contribution.

(*Id*. at p. 703 (citing multiple cases).)

The *Pasadena Police* court continued: "This statement indicates the employee has a vested right not merely to preservation of benefits already earned pro rata, but also, by continuing to work until retirement eligibility, to earn the benefits, or their substantial equivalent, promised during his

prior service.... The language in *Carman*, '[T]erms substantially equivalent to those then offered' must refer to the rule of *Allen* that while benefits are not absolutely fixed, changes detrimental to the employee must be offset by comparable new advantages." (*Pasadena POA* at p. 703 (internal cites omitted).)

Prospective changes made by Measure B, including the VEP changes, are irreconcilable with *Allen* and progeny, and are therefore unconstitutional.

v. Argument Regarding Plenary Power Over Compensation

The City contends that its authority over matters of employee compensation permit it to make adjustments to compensation for the purpose of shoring-up its unfunded liabilities. In doing so, the City has relied on cases permitting adjustments to employee contributions. In all such cases, however, adjustments have comported to the theory of the particular pension system - that is an independent actuarial valuation has permitted adjustments to normal cost contributions.

The Federated System includes a method for adjusting normal cost contributions in relation to the plan's actuarial experience. These adjustments have only ever been made on a going-forward basis. Courts have rejected the City's contention that its authority to set compensation allows it to adjust the means of pension funding on a prospective basis, specifically in *Eu* the Court noted:

> Petitioners and respondent PERS contend, however, that pension rights fall into a different category than salary rights. Although a state officer may have no protectable right to continuation of his former salary from term to term, nonetheless on commencing to serve the state the officer thereupon acquires a vested right to earn, through continued service, additional pension benefits in an amount reasonably comparable to those available when he or she first took office. According to petitioners, that right is not extinguished when one term of office ends and another commences. To hold otherwise, petitioners argue, could unduly penalize public officers who serve elective or appointive terms. We agree with petitioners.

(54 Cal.3d at 530-31 (internal citation omitted).) As described in *Allen*, a dynamic between pension and salary exists:

> In so defining such [pension] allowances, the LRL thus contemplated retirement benefits which would vary with current legislative salaries, presumably in order that retirees, like current legislators, could maintain a fairly constant standard of living despite fluctuations in living costs. Implicit in this scheme was the assumption that legislators' salaries periodically would be adjusted to reflect current costs of living.

(34 Cal.3d at 117).

Here the wage excises are linked directly to pension plan experience and, namely UALs which under the Municipal Code were always a general obligation of the City. Wage excises pegged to pension experience or foregoing rights that were already earned and promised by the City bear little relation to the setting of compensation for ongoing work performed.

B. Bill of Attainder

Measure B constitutes an unconstitutional Bill of Attainder because Section 1506-A punishes those who do not opt-into the VEP, and because Section 1514-A singles out for punishment those who attempt to challenge Measure B. California's Constitution, Article I, section 9 prohibits the state and its instrumentalities, and, thus, the City, from passing bills of attainder. "In modern application the definition is that '[a] bill of attainder is 'a legislative act which inflicts punishment without a judicial trial.' [Citations.]'" (*California State Employees' Assn. v. Flournoy* (1973) 32 Cal.App.3d 219, 224-225, *cert denied by* 414 U.S. 1093 ("*CSEA*") (quoting *Department of Social Welfare v. Gardiner* (1949) 94 Cal.App.2d 431, 433); *see also United States v. Lovett* (1946) 328 U.S. 303, 315-16 ("[L]egislative acts, no matter what their form, that apply . . . to easily ascertainable members of a group in such a way as to inflict punishment on them without a judicial trial are bills of attainder prohibited by the Constitution"); *Cummings v. Missouri* (1866) 71 U.S. 277, 323 ("A bill of attainder is a legislative act which inflicts punishment without a judicial trial. If the punishment be less than death, the act is termed a bill of pains and penalties. Within the meaning of the Constitution, bills of attainder include bills of pains and penalties").)[3]

AFSCME's members have earned a vested right to receive a certain level of pension benefit, which is property protected under California's due process, takings and contracts clauses. These benefits are also a form of deferred compensation: compensation that is earned and vested, but the receipt of which is deferred until retirement. (*See O'Dea v. Cook* (1917) 176 Cal. 659, 661-62 (where "services are rendered under [ ] a pension statute, the pension provisions become a part of the contemplated compensation for those services..."); *REAOC,* 52 Cal.4th at 1185.)

Measure B requires city employees either to "voluntarily" accept diminished pension benefits or to accept a wage tax pegged to the City's level of already-incurred general unfunded liabilities associated with the City's pension system. (Measure B, §§ 1506-A, 1507-A.) Thus, Measure B explicitly imposes either a forfeiture of property or a monetary penalty on a select class of individuals. Such forfeitures and penalties are firmly within the category of "pains and penalties" covered by the Constitution's bill of attainder clause. (*See, e.g., CSEA, supra,* 32 Cal.App.3d 219, 224) (forfeiture of property satisfies definition of attainder).) Moreover, Measure B's explicit imposition of a monetary penalty on that subclass of individuals who do not voluntarily agree to a reduction in their constitutionally-protected pension benefits itself constitutes a bill of attainder.

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[3] Although Petitioner's action arises exclusively under California law, we refer to federal law and decisions because California courts rely on precedent interpreting the California attainder clause's federal counterpart. (*See, e.g. CSEA, supra*, 32 Cal.App.3d at 224-29.)

Accordingly, Measure B taken as a whole constitutes a bill of attainder, and, its provision imposing a wage tax or penalty on those who do not voluntarily accept diminished pension benefits is also itself a bill of attainder. (Measure B, §§ 1506-A, 1507-A.)

In determining whether a legislative act inflicts punishment, courts will look beyond the narrow historical meaning of bills of attainder, and will apply two additional tests. First, a "motivational" test, examining "whether the legislative record evinces a[n] … intent to punish." (*Nixon v. Administrator of Gen. Servs.* (1977) 433 U.S. 425, 478.) And, second, a "functional test … analyzing whether the law under challenge, viewed in terms of the type and severity of burdens imposed, reasonably can be said to further nonpunitive legislative purposes." (*Id.* at 475-76.)

1. The Motivational Test: The City Intended to Punish City Employees and AFSCME Members with Measure B

Testimony and documentary evidence indicates a purpose of the City's in enacting Measure B was to punish AFSCME and those employees who do not agree to a reduction to their earned and promised pension benefits. The City has sought to punish AFSCME's members, among others, because AFSCME and its members have refused to voluntarily forego pension rights as previously demanded by the City, and, they have filed unfair labor practice charges against the City before the Public Employees Relations Board. The City's intent to punish is reflected in internal City communications which describe a substantial percentage of City employees as "totally useless" or "marginally employed" and state that "benefit and salary reductions are less important" than other City objectives, and statements by the City and its agents indicating that they are waging a "war" on AFSCME. The relevant testimony and documentary evidence will also establish that the Court cannot rely on, or credit, the various carefully-crafted self-serving non-punitive declarations of intent in the "Intent" section of Measure B. (*Cf. Eu, supra,* 54 Cal.3d at 492 (court relied on declarations of intent of particular legislative act where it had "no reason to dispute the accuracy" of those declarations).)

2. The Functional Test: Viewed in Light of the Type and Severity of the Burdens it Imposes, Measure B Cannot Reasonably Be Said To Further Non-Punitive Legislative Purposes

"The requirement of punishment is most clearly satisfied when a punitive purpose is conjoined with a characteristically punitive sanction, such as a fine." (*Club Misty, Inc. v. Laski* (7th Cir. 2000) 208 F.3d 615, 617 (emphasis added); *see also Antonio v. Wards Cove Packing Co., Inc.* (9th Cir. 1993) 10 F.3d 1485, 1496 ("Aside from expected examples such as death, imprisonment, fines, or confiscation…").) In the instant case, the intent, purpose and effect of Measure B is, in part,

to impose a fine on those employees who refuse to relinquish their constitutionally-protected right to receive their earned and promised pensions: Measure B is properly understood as a punishment imposed with a corresponding intent to punish.

The court will also hear testimony and review documentary evidence regarding the extreme burden that Measure B places on the class of individuals that it targets; both those who would accept a reduction in their pension benefits, and those who would not accept such a reduction and would, accordingly, face a wage tax or fine. This further supports a finding that Measure B functions as a punishment. (*Nixon, supra,* 433 U.S. at 475-76 (acknowledging that determination of whether legislative act can reasonably be said to further non-punitive purposes must take account of "severity" of burdens imposed).)

Finally, where "there are plainly less burdensome alternatives by which [the] legislature … could have achieved its legitimate nonpunitive objectives" that fact weighs in favor of finding the legislation to constitute an improper bill of attainder. (*Con. Edison v. Pataki* (2d Cir. 2002) 292 F.3d 338, 354 ("*ConEd*") (citing *Nixon, supra,* 433 U.S. at 482).) The Court will hear testimony regarding fairer and less burdensome methods that were available to the City, and that would have allowed the City to achieve any non-punitive objectives. For example, as part of the negotiations over Measure B with the City, a coalition of federated unions, including AFSCME, presented the City with a "Grand Bargain" proposal designed to result in substantially similar cost-savings to the City as Measure B without causing AFSCME members the same detriment. However, the City only gave the proposal a cursory review and, soon afterwards, declared impasse with respect to negotiations over Measure B. Subsequently, AFSCME filed an Unfair Practice Charge with the California Public Employment Relations Board ("PERB"), and the PERB has since issued a complaint based on the City's alleged failure to bargain in good faith over Measure B. This all supports an inference of punitive intent.

Because Measure B severely burdens a group of City employees through the imposition of forfeitures and penalties, including fines which are recognized as being characteristically punitive, when many fairer alternative measures were proposed, and could have been adopted, which would have achieved any non-punitive objectives the City had, there can be no question that Measure B fails the functional test.

a. Hobson's Choice Requirement to Relinquish Constitutional Rights

Measure B's VEP wage excise/penalty provisions, discussed above, imposes an up-to sixteen percent wage excise on employees who do not "voluntarily" relinquish their right to receive their earned and promised pension. This wage deduction amounts to a confiscation of property: the wages

the employees would otherwise expect to earn and receive are used to offset the City's general obligations. The sixteen percent wage penalty is meaningful, especially in light of the twelve percent wage decreases imposed by the City over the past four years, and in light of the additional 16% retiree health contributions towards UAL. The penalty is imposed where other, fairer methods exist. Further, it singles out employees who do not agree to forego their constitutionally-protected right to receive their earned pension benefit. As explained above, many employees simply cannot afford to suffer an additional double-digit wage cut.

b. Imposition of Excise If Measure B Challenge is Successful

Section 1514-A provides that if any of Measure B's terms are "determined to be illegal, invalid or unenforceable as to current employees," current employees' salaries shall be reduce by "an equivalent amount of savings." This provision of Measure B imposes a punishment on employees if they or their bargaining representatives challenge Measure B's wage excise, and serves no other purpose.

3. Additional Indicia of Punitive Intent

A bill of attainder may be found where the City has a punitive intent. Petitioner AFSCME has filed unfair practice charges with PERB relating to its imposition of (1) lower wages; (2) refusal to agree to voluntarily reduce pension benefits for active employees; and (3) challenging elimination of sick-leave payouts. Further, in drafting Measure B and placing the measure on the ballot, the Sixth District Court of Appeal determined the ballot language to be "charged," "biased" and not neutral. In addition, Senior City personnel have described a large percentage of City employees as "totally useless" and "marginally employed" and that the City is at "war" with city employee unions, including Petitioner.

Finally, while Measure B's stated intent indicates it is intended to save city funds, with respect to AFSCME members, the City had already imposed a 12% wage reduction with respect to "total compensation," mere months before proposing the ballot measure that ultimately was designated as Measure B. In bargaining, and prior to imposition of the 12% wage deduction, the City announced that its goal was to seek a 10% reduction in "total compensation" that it indicated included retirement benefits. Therefore, the portions of Measure B describing its intent are at odds with the City and Mayor's announced goals regarding reduction in employee compensation including retirement benefits.

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C. Taking of Private Property Without Just Compensation or Due Process

Measure B also constitutes an unconstitutional taking of property without just compensation or due process. A public entity may not take private property for public use in the absence of just compensation. (Cal. Const. art I § 19.) Nor may a public entity pass regulations having the effect of depriving individuals of their property, as did the City through Measure B. Further, California's Constitution, Article I, section 7, provides "A person may not be deprived of … property without due process of law." Measure B also constitutes an unconstitutional takings and violates employees' rights to substantive due process guaranteed by the California Constitution by taking their vested property rights without affording them a comparable advantage or commensurate benefit or compensation.

Courts have held that a legislature may not transfer funds from one retirement system to another, as doing so violates the due process clause. (*See, e.g. Association of State Prosecutors v. Milwaukee County* (1996) 199 Wis.2d 549, 564 [544 N.W.2d 888, 894] ("we hold that vested employees and retirees have protectable property interests in their retirement trust funds which the legislature cannot simply confiscate… we conclude that the transfer of funds from the County Plan to the State Plan … takes property without due process of law"); *People ex rel. Sklodowski v. State* (1994) 162 Ill.2d 117, 151 [642 N.E.2d 1180, 1194] (Transfer of pension funds "substantially impaired pension benefits."); *Sgaglione v. Levitt* (1975) 37 N.Y.2d 507, 512 [337 N.E.2d 592, 594-5] ("Although not essential to this conclusion is the salient fact that the reserve funds contain sums at some time paid regularly or specially by contributing employees. These employee-contributed funds, therefore, are not any longer State or municipal funds raised solely by the tax-levying power.").)

With respect to the federal and Michigan Takings Clauses, the court in *AFT Michigan* stated:

> The law is … equally clear that where the government does not merely impose an assessment or require payment of an amount of money without consideration, but instead asserts ownership of a specific and identifiable "parcel" of money, it does implicate the Takings Clause. Indeed, the United States Supreme Court has termed such actions violations 'per se' of the Takings Clause.

(297 Mich.App at 618 (holding that withholding of additional monies for state workers to fund retiree health constituted unconstitutional impairment of contract, taking and violation of due process).)

Where Measure B seeks to impose excises on employees to pay for the benefits of others, or to offset the system's UALs which otherwise are a general obligation of the City, it constitutes a transfer of funds, and liabilities, in violation of the takings clause.

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1. “Unvesting” of Benefits

Measure B inserts language that purports to eliminate vesting of retirement benefits. (Section 1512-A(b); *see also* Sections 1504-A, 1505-A.) “To ‘vest’ means ‘[t]o confer ownership (of property) upon a person’ or ‘[t]o invest (a person) with the full title to property.’ (Black's Law Dict. (9th ed., 2009).)” (*Vespremi v. Tesla Motors, Inc.* (Cal. Ct. App., May 5, 2011, A127008) 2011 WL 1713497; see also *Poore v. Simpson Paper Co.* (9th Cir. 2009) 566 F.3d 922, 926 (“vested means permanently fixed and unalterable.”).) Property cannot be taken without due process or just compensation under the Constitution, and therefore to the extent Measure B seeks to “unvest” any employees’ or retirees’ vested rights without compensation or due process, it constitutes an unconstitutional taking.

Further, under California law, employee benefits are a form of deferred compensation. (*LA Fire, supra,* 210 Cal.App.3d at 1102-1103.) Compensation is fixed and becomes the employees’ property once earned. It must be fixed, ascertainable and not subject to revocation. Finally, where the pension system operates as an alternative to social security, federal law requires the benefits may not be subject to alienation once accrued. Measure B’s “unvesting” language conflicts with federal and state law.

2. Wage Excises

Employees’ salaries are specific funds in which they unquestionably have a property interest. (*Sims v. United States* (1959) 359 US 108, 110 (“it is quite clear, generally, that accrued salaries are property.”).) As stated in *AFT Michigan*, involving a 3% wage excise for retiree health funding:

> Clearly, the government has “taken” three percent of plaintiff employees' wages in the dictionary-definition sense of the word. The state does not dispute that the school districts are taking possession of wages that, by contract, belong to plaintiff employees and are sending them to state-mandated funds as employer contributions. The question, however, is whether this action constitutes a “taking” as it has been defined for purposes of the Fifth Amendment and its Michigan constitutional counterpart. We conclude that it does.

(297 Mich.App. at 617.)

The *AFT Michigan* court also noted that the defendant State sought “to blur the issue by repeatedly arguing in their briefs that it is only fair for those who receive a health care benefit to help pay for it. This principle, however, is as irrelevant as it is self-evident” because “the statute does not provide that the monies obtained by the involuntary collection of three percent of the workers' wages will be used to fund the retiree health care benefits of those whose wages are being taken.” (*AFT Michigan, supra,* 297 Mich.App. at 607-08). Importantly, the court noted:

> We cannot envision a court approving as constitutional a statute that requires certain individuals to turn a portion of their wages over to the government in return for a “promise” that the government will return the monies, with interest, in 20 years when

> the government retains the unilateral right to "cancel" the "promise" at any time and does not even agree that, if they do so, the monies taken will be returned. School employees cannot constitutionally be required to "loan" money to their employer school districts, with no enforceable right to receive anything in ex-change and without even a binding guarantee that the "loan" will be repaid.

(*Id*. at 608).

Similarly, Measure B's attempt to "unvest" vested benefits, with respect to current employees, retirees and deferred-vested members, constitutes an impermissible taking without due process of just compensation because vested rights to benefits, which themselves are a form of deferred compensation, are property rights.

3. Hobson's Choice VEP Plan

Measure B seeks to require employees to forego their vested pension rights or suffer an up to a sixteen percent wage reduction. Vested rights are a form of property. Here, no due process or just compensation is provided; rather, the City seeks to force relinquishment of constitutional rights by imposing a wage deduction on those who do not agree to do so.

4. "Poison Pill" Provision Requiring Wage Excise In Event of Successful Legal Challenge

For the same reason the VEP wage excise constitutes a taking. Section 1514-A of Measure B, which requires compensation reductions in the event that portion of Measure B is struck down, also constitutes a taking without due process.

D. <u>Pension Protection Act ("PPA")</u>

The California Constitution gives public sector retirement systems the "sole and exclusive fiduciary responsibility" over the system's assets and its administration. (Cal. Const. art. XVI §§ 17, 17(a).) It also requires system assets be held in "trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries…." (Cal. Const. art. XVI § 17(a).) It further provides that "the retirement board of a public pension or retirement system shall have plenary authority and fiduciary responsibility for investment of moneys and administration of the system…" subject to specified conditions. (Cal. Const. art XVI § 17). Also, the Retirement Board "shall have the sole and exclusive fiduciary responsibility over the assets of the public pension or retirement system[,]" and "it shall also have the sole and exclusive responsibility to administer the [S]ystem in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries." (*Id*.) Furthermore, the "assets of [the System] are trust funds and shall be held for the exclusive purposes

of providing benefits to participants in the [System] and their beneficiaries and defraying reasonable expenses of administering the [S]ystem." (*Id*.)

A Retirement Board's "duty to its participants and their beneficiaries shall take precedence over any other duty." (Cal. Const. art XVI § 17(b).) Further, the Board's "exclusive fiduciary responsibilit[y] … to provide for actuarial services in order to assure the competency of the assets of the" System. (Cal. Const. art XVI § 17(e); *see also* SJMC § 3.28.350(B).)

A public agency may not usurp the authority vested in a retirement board of a public retirement system. (*See Hudson v. Bd. of Administration*, 59 Cal.App.4th at 1332.) In *Hudson,* retired city employees petitioned to require the Public Employees' Retirement System ("PERS") to include certain converted benefits in calculating their pension benefits, or alternatively, to pay amounts equal to what they should have received had PERS included the converted benefits. (*Id*. at 1316-17.) In relevant part, the court held that the city's adoption of a resolution authorizing its city manager to convert benefits to salary did not estop PERS from excluding converted benefits from calculation of retirement benefits because "the acts of one public agency will bind another public agency only when there is privity, or an identity of interests between the agencies," and concluded that there was not such privity between the parties. (*Id*. at 1330 (citation omitted).) The Court noted:

> The City's … objective was to save money by inducing employees to retire early. To attain that objective, it was willing to pay employees salaries they would not have merited until later, if at all, for the express purpose of securing for them higher pension benefits than they otherwise would have received. PERS, on the other hand, opposed such arrangements as a matter of policy, as it repeatedly stressed even before it took the position they were not authorized by PERL. Its interest was in ensuring that pension benefits, and the contribution levels on which they were based, accurately reflected actual compensation over the beneficiary's years of employment.

(*Id*. at 1330.) The Court concluded it could not "*permit the City to usurp PERS' statutory authority to determine compensation for retirement purposes*.'" (*Id*. at 1331-32 (emphasis added).)

Here, the City's Municipal Code has recognized the obligations imposed by the PPA. Namely, the SJMC grants the Retirement Board exclusive control over investing and administering of the retirement fund assets. (SJMC § 3.28.310), and indicates such assets are "held for the exclusive purposes of providing benefits to members of the plan and their beneficiaries and defraying reasonable expenses of administering the plan." (SJMC § 3.28.350(A).) Specifically, SJMC Section 3.28.350(B) commands:

> *The board shall discharge its duties with respect to the plan solely in the interest of, and for the exclusive purposes of providing benefits to, members of the plan and their beneficiaries, maintaining the actuarial soundness of the plan in a manner consistent with Article XVI, Section 17 of the California Constitution* (the "1992 California Pension Protection Act"), and defraying reasonable expenses of administering the

plan. *The board's duty to the members and their beneficiaries shall take precedence over any other duty.*

(Emphasis added.)

Several of Measure B's provisions are inconsistent with these mandates and usurp the Board's exclusive authority over its retirement System in violation of the PPA.

1. Assertion of Discretion Over COLA

Pursuant to the Municipal Code, the COLA is a benefit enhancement to the City's pension allowance. (*See* SJMC § 3.44.160(A)(1).) For this reason the Board -- and not the City -- had sole and exclusive fiduciary responsible over administering and investing the COLA funds for the benefit of participants. As such, not only was the City without power to decrease employees' COLA benefits, but Measure B also contravened the PPA's command that the pension assets be used for the benefit of its employees.

The Municipal Code itself is further evidence of the Board's exclusive authority of the COLA funds. Because the COLA is subject to the same Code provisions as the pension benefit, the Board exercises exclusive control over investing and administering the COLA funds within the Federated System and holds the assets for the exclusive purpose of providing benefits to the System's beneficiaries. (SJMC §§ 3.28.310, 3.28.350(A).) Furthermore, pursuant to the specific COLA provisions within the City Code, the Board was exclusively permitted to, amongst other things, adjust members' COLA contribution rate and invest COLA monies (SJMC § 3.44.100(B)(1), B(2), 3.44.140(B).) In fact, prior to the granting of the fixed three percent COLA in 2006, the Board was required to determine the relevant consumer price index ("CPI") for purposes of determining the corresponding COLA benefit for that year. (SJMC § 3.44.040.)

2. Liquidation of SRBR Fund

Established principles of trust law, contained in the Constitution and the SJMC, prohibit eliminating and raiding the assets of the SRBR. The SRBR trust fund was created for the benefit of Federated retirees. The SJMC specifies that it "shall be used only for the benefit of retired members, survivors of members, and survivors of retired members." (SJMC § 3.28.340(E)(1); *see also* SJMC § 3.28.340(E)(2).) This mandate accords with section 17(a) of the PPA, which states: "The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system." (*See also Keitel,* 103 Cal.App.4th at 337 (discussing elements of express trust); *City of Palm Springs,* 70 Cal.App.4th at 619 ("The legal title of the res or corpus of any trust is held by the trustee, but the beneficiaries own the equitable estate or

beneficial interest"). By eliminating the trust and diverting the corpus to offset the City's liabilities, Measure B violates the PPA.

3. Adjusting Retiree Health Contribution Rates

As discussed more thoroughly above, the City, through Section 1512-A(a) of Measure B, requires its employees to contribute a minimum of fifty percent costs the normal cost and unfunded liabilities of its retiree healthcare plan. However, pursuant to the PPA and the SJMC, the Board, and not the City, is authorized to adjust contribution rates. (*See* SJMC § 3.28.350, 3.28.385, 3.28.880.) Therefore, Section 1512-A(a) violates the PPA.

4. Imposes City's Interests On Retirement Board's Fiduciary Duties

Measure B requires the Board to administer the Federated System to "minimize any risk to the City and its residents…." (Section 1513-A(a).) This command is a violation of the PPA. The California Supreme Court has held that "even assuming article XVI, section 17 creates a duty to minimize employer contributions, it cannot be construed to require [a retirement board] to manage the retirement system in a way which would favor an employer over the beneficiaries to whom it owes a fiduciary duty." (*Sacramento v. Public Employees Retirement System* (1991) 229 Cal.App.3d 1470, 1493 ("*Sacramento PERS*").) This is precisely what Measure B does. Measure B was designed by the City on the basis of its alleged fiscal crisis, and it was sold to the voters as a means to "provide its citizens with Essential City Services" which have "been and continue[] to be threatened by budget cuts caused mainly by the climbing costs of employee benefit programs, exacerbated by the economic crisis." (Section 1501-A.) While Measure B says that it was designed to "provide reasonable … post employment benefits" to retirees (Section 1502-A), nothing within Measure B provides its employees or retirees with an advantage; as such, it directly contravenes the PPA by making it near impossible for the Federated Board to administer the retirement System in the best interests of its beneficiaries; the only party Measure B benefits is the City itself. *Sacramento PERS* forbids such an outcome. (*See* 229 Cal.App.3d at 1493.)

In addition, Section 1513-A of Measure B sets forth certain requirements on the Board with respect to its maintenance of the actuarial soundness of the plan. In doing so, Section 1513-A(a) requires the Board to "minimize any risk to the City and its residents" and to be "prudent and reasonable in light of the economic climate" when adopting retirement plans pursuant to Measure B. Not only do such requirements contravene the PPA's command that such plans be administered in the interest of its beneficiaries, but it also usurps the Board's plenary power and exclusive fiduciary responsibility to provide for actuarial services and make investment decisions (as mandated by PPA).

Measure B further imposes on the Board's authority over actuarial matters, as granted it by the SJMC. (SJMC §§ 3.28.155, 3.28.160, 3.28.170, 3.28.200, 3.28.300, 3.28.350(B) ("The Board shall … maintain[] the actuarial soundness of the plan in a manner consistent with [the PPA].") Importantly, the SJMC gives the Board authority over setting actuarial assumptions related to the System:

> Upon the basis of any or all of such investigations, valuations and determinations, *the board shall adopt* such mortality, service and other tables, actuarially assumed annual rate of return, and *other actuarial assumptions* as it may deem reasonably necessary, and, subject to such limitations as are set forth elsewhere in this chapter, it shall fix and from time to time make such revisions or changes in the rates of contribution required of members and of the city as it may determine reasonably necessary to provide the benefits provided for by this retirement plan.

(SJMC 3.28.200 (emphasis added).) Through Measure B, the City impedes upon the Board's constitutional command--a command it recognized at one time through the SJMC.

E. <u>Right to Petition</u>

"The people have the right to … petition government for redress of grievances" (Cal. Const. art. I § 3). Section 1514-A of Measure B, the Measure's "Savings" clause, states:

> In the event [Section 1506-A(b)] is determined to be illegal, invalid or unenforceable as to Current Employees (using the definition in [Section 1506-A(a)]), then, to the maximum extent permitted by law, an equivalent amount of savings shall be obtained through pay reductions. Any pay reductions implemented pursuant to this section shall not exceed 4% of compensation each year, capped at a maximum of 16% of pay.

This clause imposes a cost or risk upon the exercise of the right to petition the courts for redress, and its purpose and effect is to chill the assertion of constitutional rights by penalizing those who choose to exercise them. The provision further deters members from challenging Measure B, by imposing an unreasonable, burdensome penalty for successfully invoking the Constitutional right to petition the courts.

"The right of access to the courts is indeed but one aspect of the right of petition" (*California Motor Trans. Co.* v. *Trucking Unlimited* (1972) 404 U.S. 508), but it is "among the most precious of the liberties safeguarded by the Bill of Rights." (*United Mine Workers* v. *Ill. Bar Assoc.* (1967) 389 U.S. 217, 222.) Further, this corollary right has "a sanctity and a sanction not permitting dubious intrusions." (*Thomas* v. *Collins* (1945) 323 U.S. 516, 530.)

In *California Teachers Assn. v. State of California* (1999) 20 Cal.4th 327 ("*CTA*"), the Supreme Court found that a statute imposing one-half the cost of an administrative hearing on unsuccessful teachers violated the right to petition by inhibiting free access to judicial review. (*See*

also Long Beach v. *Bozek* (1982) 31 Cal.3d 587, 582-589 (holding right to petition completely precludes government entity from suing unsuccessful litigant).) As stated in *CTA*, "[t]he imposition of a cost or risk upon the exercise of the right to a hearing is impermissible if it has no other purpose or effect than to chill the assertion of constitutional rights by penalizing those who choose to exercise them." (*CTA*, 20 Cal.4th at 338 (emphasis added).) Broadly stated, any government action designed to keep a citizen from initiating legal remedies infringes upon the right to petition. (*In re Workers Comp. Refund Cases* (8th Cir. 1995) 46 F.3d 813 (*citing Harrison v. Springdale Water* (8th Cir.1986) 780 F.2d 1422).) This principle is broadly construed and applied: the right of access to courts may not be directly or indirectly impaired. (*Harrison,* at 1428 (emphasis added).) Because an "indirect impairment" of the right to petition may include "retaliatory action taken against an individual designed either to punish him for having exercised his constitutional right to seek judicial relief or to intimidate or chill his exercise of that right in the future," courts routinely find laws that contain "litigation penalties" to be unconstitutional. (*CTA*, *supra*, 20 Cal.4th at 331, 338.)

In the instant case, Measure B imposes a significant penalty on employees who successfully seek judicial review. Measure B subjects employees to a drastic reduction in pay, potentially greater than the reduction Measure B imposes. Section 1514-A provides that in the event an employee successfully challenges section 1506-A(b), which would force current employees to make additional retirement contributions up to a maximum of 16% of their pensionable pay, the employee will immediately face a reduction in pay of up to 16%. Accordingly, on its face, Measure B unconstitutionally chills the right to seek judicial review by imposing a penalty for a successful challenge. According to the City, a sixteen percent reduction in pay is less desirable than an increase in retirement contributions because the former results in lower levels of pension benefits based upon lower pensionable pay. In other words, the maximum penalty imposed by section 1514-A is greater than the maximum detrimental effect of section 1506-A(b).

In addition to violating current employees' right to petition, Measure B also imposes an impermissible litigation penalty on the petitioner labor unions, because, if they are successful in challenging section 1506-A(b), section 1514-A imposes a wage reduction on current employees, a topic which is a mandatory subject of collective bargaining under the Meyers-Milias-Brown Act.

Defendants may argue, as a general matter, that section 1514-A is merely intended to serve as an alternative means to achieve the objectives of section 1506-A(b) if the latter is found to be unconstitutional or illegal, and, thus, the pay reduction threatened by section 1514-A is not properly termed a "litigation penalty." This argument fails on two primary grounds. First, as discussed above, the harm imposed by section 1514-A is more severe than the detrimental effect of section 1506-A(b).

Second, while the "additional retirement contributions" required by section 1506-A(b) necessarily address the City's unfunded pension liabilities (and, indeed, are explicitly linked to the City's unfunded liabilities as they are limited to "no more than 50% of the costs to amortize any pension unfunded liabilities . . ."), there is no requirement in section 1514-A that any "savings" achieved by the pay reductions threatened by that section be used to address the City's unfunded liabilities. This further suggests that 1514-A is not intended as an alternative method of achieving the purported objectives of section 1506-A(b), rather, it is intended as a penalty to discourage challenges to section 1506-A(b).

Thirdly, section 1514-A threatens to impose pay reductions without any bargaining with the petitioner unions. Thus, Section 1514-A serves as a litigation penalty for petitioner unions representing current employees. While the City has incorrectly argued that "there is no question that the City has the right to impose a straight wage reduction," (City's Consolidated Reply in Support of Motion for Summary Adjudication, 23:18-19), this argument underlines the impropriety of 1514-A: If the City were right that it could impose the pay reductions without voter approval and without collective bargaining, then what reason was there for the City to include that section in Measure B other than to present a clear penalty designed to discourage legal challenges to section 1506-A(b)?

F. Promissory and Equitable Estoppel

The California Supreme Court has expressly recognized the "unique importance of pension rights to an employee's well-being" and affirmed the application of estoppel against government retirement agencies to protect those rights, particularly in cases where "employees were induced to accept and maintain employment on the basis of expectations fostered by widespread, long-continuing misrepresentations." (*Longshore v. County of Ventura* (1979) 25 Cal.3d 14, 28.) The doctrine of estoppel may be applied against a public entity where justice and right require it as long as its application is not harmful to a specific public interest or policy, or an expansion of the authority of a public official. (*Fleice v. Chualar Union Elem. Sch. Dist.* (1988) 206 Cal.App.3d 886; *City of Long Beach v. Mansell* (1970) 3 Cal.3d 462 ("*Mansell*").) The remedy of equitable estoppel is available where the plaintiff is injured upon reliance on defendant's misrepresentation or concealment of material facts.

1. Equitable Estoppel

Equitable estoppel may be invoked in situations where a party makes a false representation or conceals material facts. Equitable estoppel poses a factual question. (*Walsh, supra,* 4 Cal.App.4th at 709.) The requisite elements for equitable estoppel are: (1) the party to be estopped was apprised of the facts (knew or ought to have known the facts), (2) the party to be estopped intended by conduct to

induce reliance by the other party, or acted so as to cause the other party reasonably to believe reliance was intended, (3) the party asserting estoppel was ignorant of the facts, and (4) the party asserting estoppel suffered injury in reliance on the conduct. (*Mansell*, *supra,* 3 Cal.3d at 489.)

a. Knowledge

While actual knowledge is normally required for the first prong, knowledge is imputed where the defendant ought to have known or where the party actively made affirmative misrepresentations, as opposed to remaining silent or acquiescing. (*Feduniak v. Cal. Coastal Com'n.* (2007) 148 Cal.App.4th 1346; *Kieffer v. Spencer* (1984) 153 Cal.App.3d 954.) Here, the City conveyed a promise that upon fulfillment of a given condition, employees would be provided certain pension benefits. It further informed that employees' were vested in their benefits and that the City would pay their retiree health costs. According to the City now, it never made such promises and it has the right to alter the benefits previously promised to employees.

b. Inducement of Reliance

The second prong requires that the defendant have acted in a manner so as to cause the other party to reasonably believe that reliance was intended. In *Baillargeon v. Dep't of Water and Power,* a booklet distributed by the employer promised supplemental benefit payments to employees injured on the job despite the fact that the disability plan did not actually include such payments. A former employee relied upon that promise set forth in the booklet she received early in her career. She was thereafter injured due to that reliance. The Court of Appeal reversed the lower court's dismissal of plaintiff's equitable estoppel cause of action noting that "it would not be beneficial to anyone for public employees to be misled--intentionally or otherwise--by an informational booklet issued to them." (*Baillargeon v. Dep't of Water and Power* (1977) 69 Cal.App.3d 670, 680.)

It is well understood that pension information is provided in booklets and orientations "to attract and retain good employees." (*Christensen v. Minneapolis Mun. Employees* (Minn. 1983) 331 N.W.2d 740, 747.) Here, the benefits materials provided to employees were widely-publicized and distributed, and cited as a reason for remaining in public service despite higher paying private sector options. As such, new employees and active employees reasonably believed that reliance was intended when they received pension benefit information in booklets and at orientation.

c. Ignorance

The third prong requires that the plaintiffs were ignorant of the facts when they relied on the misrepresentation. Here, the employees were ignorant of the fact that the benefits they were promised were not vested, but, in accordance with the City's current position, subject to change. Further, the employees were ignorant of the fact that the pension system could be changed

unilaterally and that they could be required to make additional contributions. The inquiry of whether the Plaintiff was ignorant hinges on the moment at which the Plaintiff was injured as she relied to her detriment. An employee alleging that she refused a higher-paying private sector job in ignorant reliance on the City's representation was actually unaware of the facts. Similarly, an employee alleging that she accepted employment with the City in ignorant reliance on the City's representation was also unaware of the facts at the time she relied upon the misrepresentation.

d. Injury

The final prong of the equitable estoppel analysis requires that the party asserting estoppel have suffered injury in reliance on defendant's representations. Here, the employees suffered actual and prospective monetary injury in reliance on the City's representation. The employees suffered immediate harm upon the lost opportunity to contribute to the Social Security system. The employees forewent the opportunity to pay into the Social Security system for retirement benefits in reliance on the City's retirement system. Additionally, the employees currently suffer injury from the lost opportunity to budget their mortgages and retirement plans with the knowledge that they would be liable for contributions and unfunded liability. Finally, the employees relinquished other employment prospects with higher salaries in reliance on the City's representation that their guaranteed, future retirement benefits would offset that difference. As such, equitable estoppel is available to AFSCME's members, and the City should be estopped from denying the benefits Measure B affects.

2. Promissory Estoppel

Promissory estoppel operates to render a promise enforceable in the absence of consideration when injustice can only be avoided by enforcement of the promise. Promissory estoppel may be invoked when a party has made a clear and definite promise upon which the other party reasonably and foreseeably relies to her detriment. The elements for promissory estoppel are: (1) a promise clear and unambiguous in its terms; (2) actual reliance by the promisee; (3) reliance by the promisee is both reasonable and foreseeable; (4) promisee is injured by her reliance. (*Van Hook v. S. Cal. Waiters Alliance, Local 17* (1958) 158 Cal. App. 2d 556.)

a. Promise

The first element of promissory estoppel is a clear and definite promise made by the promisor to the promisee. In *Requa v. Regents of the Univ. of Cal.*, the lower court dismissed a promissory estoppel cause of action because the plaintiff failed to allege a "clear and unambiguous promise to lifetime retiree medical benefits." The court relied primarily on the Regents' interpretation of conditional booklet statements that health benefits "may continue" or "can be continued." The Court

of Appeal reversed the trial court's decision noting that the booklet also contained language of commitment such as "coverage can be continued *as long as monthly income received from retirement is large enough to cover employee contribution,*" and "your University group medical and dental plans may be continued when you retire, *provided that you are enrolled at the time of retirement*." (*Requa v. Regents of the Univ. of Cal* (2012) 213 Cal.App.4th 213.) Permissive language is clearly relevant but not decisive post-*Requa*.

In *Hunter v. Sparling*, the court found that plaintiff's reliance on oral promises of a retirement allowance sufficed to establish an enforceable promise. The court found that even though the Plaintiff had never read the benefit plan written in Japanese, the plan constituted an implied contract between the employer and employee. The court added that the promise to pay pension was also enforceable under promissory estoppel, because "[t]he undisputed and found facts show that after plaintiff knew of the promise, he received several offers of employment by other banks and turned them down because, if accepted, he would lose his retirement allowance. The promise was one that was designed to accomplish just that result. Under such circumstances the doctrine of promissory estoppel is applicable." (*Hunter v. Sparling* (1948) 87 Cal. App. 2d 711, 725.)

Here, the City's retirement booklets, which will be introduced at trial, contain representations sufficient to induce reliance, and the City's regular retirement orientations represented that when the stated condition was fulfilled, employees would receive the listed pension benefits. The fact that a promise is conditional does not render it unenforceable or ambiguous. (*Garcia v. World Sav., FSB* (2010) 183 Cal. App. 4th 1031, 1045.)

b. Actual Reliance

The second prong of promissory estoppel is actual reliance by the promisee on the promisor's promise. In *Van Hook*, the court found reliance where a former employee had refused other jobs and remained in his position after the employer passed a resolution to offer retirement benefits to him to "assure him financial security so that he will not find it necessary to find other employment." (158 Cal. App. 2d at 556.) Where, as here, employees opting into city employ forego social security coverage, they necessarily place additional reliance on the city's representations of the benefits they can expect to receive in lieu of social security.

Reliance is also demonstrated by the fact that the employees remained in public service and refused higher-paying private sector jobs in reliance on future post-retirement benefits. The employees believed these benefits to be "deferred compensation" and they calculated their budgets and retirement plans around the information they were provided. They believed this information was accurate and that this information would remain applicable to them when they retired in the future.

c. Reasonable and Foreseeable Reliance

The third prong mandates that the reliance by the promisee be both foreseeable and reasonable. The court in *Norman v. Hous. & Redevelopment Auth. of Chisholm*, found that a retiree's reliance on the company promise in the CBA to continue paying her premiums was not unreasonable as a matter of law, and the employer was estopped from denying payment of her premiums. (*Norman v. Hous. & Redevelopment Auth. of Chisholm* (Minn. Ct. App. 2004) 681 N.W.2d 376, 379, *aff'd on other grounds,* (Minn. 2005) 696 N.W.2d 329.)

Here, the employees' reliance on the City's booklets and representations at employee orientations was likely foreseeable and reasonable. The booklets do not contain reservation of rights language as in *Maurer* and the orientation leaders did not inform employees that the benefits could or would change. As such, it was foreseeable that employees would rely on the information presented by the City and reasonable that they would believe these promises to remain in effect at the time of their retirement.

d. Injury

The final prong is the requirement that the Plaintiff suffered injury due to her reliance. In *SD Firefighters,* the California Supreme Court stated that estoppel will not be applied if there is "no proof that anyone had actually been hurt by the handbook's statement--that any employee had accepted employment or remained on the job in reliance on the misleading answer." (34 Cal.3d. at 306 (Kaus, J., concurring).)

Here, as stated above, the employees suffered actual and prospective monetary injury in reliance on the City's representation. The employees suffered immediate harm upon the lost opportunity to contribute to the Social Security system. The employees forewent the opportunity to pay into the Social Security system for retirement benefits in reliance on the City's retirement system. Additionally, the employees currently suffer injury from the lost opportunity to budget their mortgages and retirement plans with the knowledge that they would be liable for contributions and unfunded liability. And finally, the employees relinquished other employment prospects with higher salaries in reliance on the City's representation that their guaranteed, future retirement benefits would offset that difference. As such, promissory estoppel is applicable here. As such, the City should be estopped from denying the benefits Measure B affects.

3. Estoppel Does Not Contravene Public Interest

The City may argue that estoppel cannot apply here to active members because estoppel would contravene the public "interest in an actuarially sound pension and benefit system for their

employees." But in *Baillargeon*, the court dismissed this argument stating that the Plaintiff's recovery would not jeopardize the entire system and that it was in the interest of everyone that public employees not be misled by informational booklets provided to them by the public employer. (69 Cal.App.3d at 670.)

VI. REMEDIES SOUGHT

A. Declaratory Relief

AFSCME seeks a declaration finding Measure B as a whole, and its separate provisions, unconstitutional pursuant to the laws discussed within this brief as well as under the federal Constitution.

B. Injunctive Relief

AFSCME seeks a permanent injunction prohibiting the City from enforcing Measure B or adopting any ordinances implemented its parts.

C. Writ of Mandate

AFSCME seeks a writ mandating Defendant Debra Figone to eliminate the City's ordinance eliminating the SRBR and to repeal any other ordinances enacting Measure B or its parts.

Dated: July 8, 2013

BEESON, TAYER & BODINE, APC

By:
TEAGUE P. PATERSON
VISHTASP M. SOROUSHIAN
Attorneys for Plaintiff AFSCME LOCAL 101

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PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF ALAMEDA

I declare that I am employed in the County of Alameda, State of California. I am over the age of eighteen (18) years and not a party to the within cause. My business address is Beeson, Tayer & Bodine, Ross House, Suite 200, 483 Ninth Street, Oakland, California, 94607-4051. On this day, I served the foregoing Document(s):

PLAINTIFF/PETITIONER AFSCME LOCAL 101'S PRE-TRIAL BRIEF

☒ **By Mail** to the parties in said action, as addressed below, in accordance with Code of Civil Procedure §1013(a), by placing a true copy thereof enclosed in a sealed envelope in a designated area for outgoing mail, addressed as set forth below. I am readily familiar with this business's practice for collecting and processing correspondence for mailing. On the same day that correspondence is placed for collection and mailing, it is deposited in the ordinary course of business with the United States Postal Service in a sealed envelope with postage fully prepaid.

☐ **By Personally Delivering** a true copy thereof, to the parties in said action, as addressed below in accordance with Code of Civil Procedure §1011.

☐ **By Messenger Service** to the parties in said action, as addressed below, in accordance with Code of Civil Procedure § 1011, by placing a true and correct copy thereof in an envelope or package addressed to the persons at the addresses listed below and providing them to a professional messenger service.

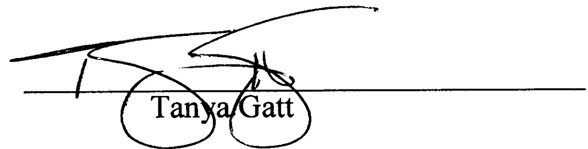
☐ **By UPS Overnight Delivery** to the parties in said action, as addressed below, in accordance with Code of Civil Procedure §1013(c), by placing a true and correct copy thereof enclosed in a sealed envelope, with delivery fees prepaid or provided for, in a designated outgoing overnight mail. Mail placed in that designated area is picked up that same day, in the ordinary course of business for delivery the following day via United Parcel Service Overnight Delivery.

☐ **By Facsimile Transmission** to the parties in said action, as addressed below, in accordance with Code of Civil Procedure §1013(e).

☐ **By Electronic Service.** Based on a court order or an agreement of the parties to accept service by electronic transmission, I caused the documents to be sent to the persons at the electronic notification addresses listed below. I did not receive, within a reasonable time after the transmission, any electronic message or other indication that the transmission was unsuccessful.

SEE ATTACHED SERVICE LIST

I declare under penalty of perjury that the foregoing is true and correct. Executed in Oakland, California, on this date, July 8, 2013.



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SERVICE LIST

Greg McLean Adam, Esq. Jonathan Yank, Esq. Gonzalo C. Martinez, Esq. Amber L. West, Esq. CARROLL, BURDICK & McDONOUGH LLP 44 Montgomery Street, Suite 400 San Francisco, CA 94104 *Attorneys for Plaintiff, SAN JOSE POLICE OFFICERS' ASSOCIATION (Santa Clara Superior Court Case No. 112CV225926)*	Arthur A. Hartinger, Esq. Jennifer L. Nock, Esq. Linda M. Ross, Esq. Michael C. Hughes MEYERS, NAVE, RIBACK, SILVER & WILSON 555 12th Street, Suite 1500 Oakland, CA 94607 *Attorneys for Defendants, THE CITY OF SAN JOSE AND DEBRA FIGONE*
John McBride, Esq. Christopher E. Platten, Esq. Mark S. Renner, Esq. WYLIE, McBRIDE, PLATTEN & RENNER 2125 Canoas Garden Avenue, Suite 120 San Jose, CA 95125 *Attorneys for Plaintiffs/Petitioners, ROBERT SAPIEN, MARY McCARTHY, THANH HO, RANDY SEKANY AND KEN HEREDIA (Santa Clara Superior Court Case No. 112-CV-225928)* *AND* *Plaintiffs/Petitioners, JOHN MUKHAR, DALE DAPP, JAMES ATKINS, WILLIAM BUFFINGTON AND KIRK PENNINGTON (Santa Clara Superior Court Case No. 112-CV-226574)* *AND* *Plaintiffs/Petitioners, TERESA HARRIS, JON REGER, MOSES SERRANO (Santa Clara Superior Court Case No. 112-CV-226570)*	Harvey L. Leiderman, Esq. REED SMITH, LLP 101 Second Street, Suite 1800 San Francisco, CA 94105 *Attorneys for Defendant, CITY OF SAN JOSE, BOARD OF ADMINISTRATION FOR POLICE AND FIRE DEPARTMENT RETIREMENT PLAN OF CITY OF SAN JOSE (Santa Clara Superior Court Case No. 112CV225926)* *AND* *Necessary Party in Interest, THE BOARD OF ADMINISTRATION FOR THE 1961 SAN JOSE POLICE AND FIRE DEPARTMENT RETIREMENT PLAN (Santa Clara Superior Court Case No. 112CV225928)* *AND* *Necessary Party in Interest, THE BOARD OF ADMINISTRATION FOR THE 1975 FEDERATED CITY EMPLOYEES' RETIREMENT PLAN (Santa Clara Superior Court Case Nos. 112CV226570 and 112CV22574)* *AND* *Necessary Party in Interest, THE BOARD OF ADMINISTRATION FOR THE FEDERATED CITY EMPLOYEES RETIREMENT PLAN (Santa Clara Superior Court Case No. 112CV227864)*

Stephen H. Silver, Esq.
Richard A. Levine, Esq.
Jacob A. Kalinski, Esq.
SILVER, HADDEN, SILVER, WEXLER & LEVINE
1428 Second Street, Suite 200
Santa Monica, CA 90401-2367

Attorneys for Plaintiffs, SAN JOSE RETIRED EMPLOYEES ASSOCIATION, HOWARD E. FLEMING, DONALD S. MACRAE, FRANCES J. OLSON, GARY J. RICHERT and ROSALINDA NAVARRO (Santa Clara Superior Court Case No. 112CV233660)