

Modifying Post-Retirement Health Benefits of Current Public Sector Employees:

A Primer on Employers' Legal Rights and Responsibilities

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Introduction

Over the past few years, California's public employers have been battered by the effects of the lingering state and federal economic crises. At the same time, the cost of health benefits packages, negotiated by those employers during headier economic days, has literally skyrocketed. According to the Kaiser Family Federation's most recent update, health insurance premiums for California workers increased by an average 15.8% in 2003; during the same time period, CalPERS plan premiums had a 22.9% average increase.¹ This financial storm has devastated budgets and directly contributed to hiring freezes, furloughs and layoffs in the majority of California's public agencies, creating a very real risk of bankruptcy in a growing number of cases.

Thus, many public employers -- in the interest of their very survival -- are now seeking to terminate or repeal the richer aspects of the health and welfare benefits they currently offer their employees. In particular, many employers are re-evaluating earlier commitments to pay lifetime post-retirement health benefits.

There is no serious dispute that such benefits may appropriately be renegotiated for "new hires."² Conversely, the benefits of those already retired should be analyzed as a simple matter of contract law.³ However, the status of future benefits for current employees has been the subject of some confusion. Some employees -- and their representative employee organizations and unions -- have asserted that such benefits become individually vested as soon as they are offered, in a manner similar to pensions, and thus may not subsequently be waived or modified without individual consent.

This article addresses the potential legal basis for vesting of retiree medical benefits, and concludes that the better reasoned precedent supports treating future post-retirement health benefits as a non-vested term and condition of employment that is subject to the meet and confer processes under California's various public sector collective bargaining statutes.

The Central Tension: Balancing Employment By Statute With Individual Rights To Salary Earned

The debate over post-retirement health benefits' vesting arises from the tension between two basic principles of California public sector labor law.

On the one hand, it is well established under California law that the terms and conditions of public employment are controlled by statute or ordinance rather than by contract.⁴ Accordingly, public employees have no vested right to any particular measure of such compensation or benefits, and compensation or benefits may be modified or reduced pursuant to proper statutory authority.⁵ For health benefits purposes, "[p]ursuant to proper statutory authority" means, most importantly, consistent with bargaining obligations under California's collective bargaining statutes. Where an agreement is reached with the employees' exclusive representative, or where the employer implements new terms and conditions of employment, individual consent is not necessary to bind all members of the relevant bargaining unit -- even for those who decline membership in the exclusive representative.⁶

On the other hand, public employees do have an individual right to a limited number of obligations "protected by the contract clause of the constitution, including the right to the payment of salary that has been earned."⁷ The quintessential example of such a protected benefit is a pension, which is considered a form of "deferred compensation."⁸ Accordingly, on the very first day of employment, each employee gains a vested right to receive a pension substantially identical to that promised, subject to fulfillment of specified conditions.⁹ Generally, the pension terms may not subsequently be amended without individual consent.¹⁰

Accordingly, the central question is whether post-retirement health benefits, once promised and extended, should be treated as equivalent to, and analyzed the same as, pension benefits.

Appellate Split: Palos Verdes Library District and City of Fontana

The answer to this key question is complicated by the fact that appellate courts have split over the appropriate standard for determining which non-pension benefits are protected by the constitutional contract clauses.

On the one hand, those who argue in favor of individualized vesting typically cite the 1978 case of *California League of City Employee Associations v. Palos Verdes Library District* ("*Palos Verdes Library District*").¹¹ In that case, the Second Appellate District¹² stated that any benefit that acts as an inducement for continued employment is "fundamental" and therefore vested in the same manner as a pension, because of "the effect of [such benefits] in human terms and the importance of [such benefits] to the individual in the life situation."¹³ As can readily be seen, this standard is very broad.

In 1998, however, the Fourth Appellate District¹⁴ specifically disavowed *Palos Verdes Library District* in *San Bernardino Public Employees Association v. City of Fontana* ("*City of Fontana*").¹⁵ The *City of Fontana* court held that the constitutional contract clauses are implicated *only* when the circumstances and language of the statute in question "evinces a legislative intent to create private rights of a contractual nature enforceable against the state."¹⁶ Taking into account the purpose and structure of the Meyers-Milias Brown Act ("*MMBA*"), the *City of Fontana* court concluded that inclusion of such benefits as vacation leave and longevity pay in a collective bargaining agreement of fixed duration creates no legitimate expectation that the benefits will indefinitely continue in future agreements.¹⁷

"Upon expiration of an MOU, an employee who elects to continue employment with a public entity has impliedly agreed to be bound by the salary and benefit package provided in the new MOU."¹⁸

City of Fontana does not overrule *Palos Verdes Library District* (except within the Fourth Appellate District), and final determination of the correct standard must await a future decision of the Supreme Court. However, we note with interest that in the more than five years since the publication of *City of Fontana*, *Palos Verdes Library District* has not been cited in a single published court decision.¹⁹ Such silence suggests that courts have been hesitant to extend the *Palos Verdes Library District* analysis without further guidance. Moreover, the simple fact is that *Palos Verdes Library District* fails to directly address the relevance and overall purpose of the collective bargaining system imposed on California public sector employers. Thus, we believe that the strong weight of evidence supports concluding that *City of Fontana* is the better reasoned precedent, and is likely to be followed by other courts of appeal or by the Supreme Court in the appropriate case.

What About *Thorning v. Hollister School District*?

Moreover, despite some claims to the contrary, no published case has ever directly addressed how *collectively bargained* future post-retirement health benefits of *current employees* should be treated.

Many vesting proponents cite to the 1992 Sixth Appellate District case of *Thorning v. Hollister School District*²⁰ for the broad proposition that post-retirement health benefits always individually vest once offered.²¹ Even commentators sympathetic to the arguments for non-vesting pursuant to *City of Fontana* have described *Thorning* as "the only case holding that retirement health benefits were vested rights."²² However, the holding of *Thorning* is, in reality, much narrower. First, the decision is entirely dependant on the analysis set forth in *Palos Verdes Library District*, as specifically disavowed in *City of Fontana*. If the *Palos Verdes Library District* standard is incorrect, *Thorning* must also be rejected. Second, *Thorning* did not involve collectively bargained benefits or modifications - rather, it involved legislatively enacted benefits of elected school board members serving set terms of office. Third, the plaintiffs in *Thorning* were *already retired, and their benefits had been terminated after their retirement occurred*.²³ Although full discussion of the rules applicable to the benefits of those already retired is beyond the scope of this article, this fact alone renders *Thorning* inapposite to any discussion involving renegotiation of current employees' future post-retirement benefits.


The *City of Fontana* court was asked to rule on collectively bargained modifications to post-retirement health benefits, but declined to do so because the issue was not yet ripe under the specific facts of the case.²⁴ However, under the *City of Fontana* standard, there are very strong arguments that such benefits do not become individually vested until retirement actually occurs and that such benefits may be renegotiated at any time prior to retirement, absent explicit language to the contrary.


Conclusions


In light of the current appellate split, the standard applicable to the issue of post-retirement health benefits vesting remains uncertain. However, we believe that the *Palos Verdes Library*


District standard is clearly overbroad and incompatible with the intent of collective bargaining, and that it is more likely than not that the better reasoned *City of Fontana* standard would be adopted in any litigation before other courts. Further, strong arguments support concluding that under that standard, future post-retirement benefits of current employees may be renegotiated consistent with collective bargaining obligations under the applicable collective bargaining statute. Where such bargaining obligations are met, and modified benefits are agreed to by the relevant employee organization, that agreement will bind all individual unit members without the necessity of individual consent. Moreover, where a good faith effort is made at mediation, and impasse procedures are exhausted, in some cases such changes may be unilaterally implemented. The appropriate strategy will, in each case, be extremely fact-specific.


Footnotes:

 Footnote *. *Charles Sakai is a founding partner of Renne Sloan Holtzman & Sakai. He regularly represents public entities in the areas of employment litigation, including harassment, discrimination and wrongful discharge, and traditional labor law, including unit determinations, PERB and NLRB unfair practice proceedings, interest and rights arbitration, and negotiations.*

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 Footnote 1. *California Health Insurance Premiums Jumped 15.8% in 2003, Higher Than National Increase, New Survey Finds, Kaiser Family Foundation Health Research and Educational Trust (Press Release, 3/16/04); Trends and Indicators in the Changing Healthcare Marketplace, 2004 Update, Kaiser Family Foundation Health Care Marketplace Project (April 2004), Exhibit 3.6 ("Annual Change in Health Insurance Premiums for Employers Overall, FEHBP, and CalPERS, 1993-2003"). Both documents available online at www.kff.org.*

 Footnote 2. Future benefits of current employees, including health benefits, are generally within the scope of mandatory bargaining under California's public sector collective bargaining statutes.

 Footnote 3. There is no clear and binding California precedent on this point. However, under federal private-sector precedent it is well settled that the vesting of retiree health benefits is a matter of contractual interpretation. Agreements that unambiguously terminate such benefits upon termination of the agreement will be enforced (see, e.g., [Murphy v. Keystone Steel and Wire Co.](#), 61 F.3d 560, 565 (7th Cir. 1995)), but so will clear and unambiguous promises of lifetime benefits (see [Keffer v. H.K. Porter Co.](#), 872 F.2d 60, 62-64 (4th Cir. 1989)). Accordingly, the exact extent to which the benefits of those already retired can be modified is generally controlled by the language of the collective bargaining agreement in place at the time the retiree actually retired. Extremely detailed and fact-specific analysis should occur before any attempt is made at such modification.

Footnote 4. [Miller v. State of California, 18 Cal. 3d 808, 813-814 \(1977\)](#); [Butterworth v. Boyd, 12 Cal. 2d 140, 150 \(1938\)](#); [Kim v. Regents of the University of California, 80 Cal. App. 4th 160, 164 \(2000\)](#).

Footnote 5. *Id.*

Footnote 6. [San Lorenzo Education Association v. Wilson, 32 Cal. 3d 841, 846 \(1982\)](#).

Footnote 7. [Kern v. City of Long Beach, 29 Cal. 2d 848, 852-853 \(1947\)](#) (city barred from eliminating pension payments by charter amendment as to fire department employee, 32 days before completion of required 20 years of service). The federal and state contract clauses (U.S. Const. Art.1, Sec.10 and Cal. Const. Art.1, Sec.9) bar the state from repudiating contractual obligations.

Footnote 8. [Kern, 29 Cal. 2d at 855](#); [Miller, 18 Cal. 3d at 814](#).

Footnote 9. *Id.*

Footnote 10. *Id.*; minor exceptions to this principle are allowed for modifications that (1) are necessary to protect the continued flexibility and viability of the pension system, (2) bear a material relation to the "theory of a pension system," and (3) result in no disadvantage to the employee that is not balanced by a comparable new advantage. [Allen v. City of Long Beach, 45 Cal. 3d 128, 131 \(1955\)](#).

Footnote 11. [California League of City Employee Associations v. Palos Verdes Library District, 87 Cal. App. 3d 135 \(1978\)](#) ("Palos Verdes Library District") (the specific benefits analyzed in *Palos Verdes Library District* included a variety of longevity-based benefits, including salary increases, one-time vacation bonuses, and one-time sabbaticals).

Footnote 12. The Second Appellate District is headquartered in Los Angeles and Ventura.

Footnote 13. [Palos Verdes Library District, 87 Cal. App. 3d at 139-140](#), citing [Bixby v. Pierno, 4 Cal. 3d 130, 144 \(1971\)](#).

Footnote 14. The Fourth Appellate District consists of three Divisions, headquartered in San Diego, Riverside, and Santa Ana.

Footnote 15. [67 Cal. App. 4th 1215 \(1998\)](#).

Footnote 16. [Id. at 1223](#); the *City of Fontana* court specifically disapproved of importing the standard set forth in *Bixby v. Pierno*, which it characterized as having "merely established a rule of judicial review applicable to adjudicatory orders or decisions of public agencies." *Id.*

Footnote 17. [Id. at 1223](#)

Footnote 18. [Id. at 1226](#), comparing [Olson v. Cory, 27 Cal. 3d 352 \(1980\)](#) (statute limiting cost-of-living increases for judges unconstitutional as to judges in office at time statute passed, but constitutional upon commencement of new terms; acceptance of new term considered waiver of any contractual right).

Footnote 19. Indeed, the most significant reference to *Palos Verdes Library District* since 1998 is in the unpublished case of [Barber v. East Bay Municipal Utility District, 2001 Cal. LEXIS 933](#) (Cal. App. 1 Dist. Nov 9, 2000), wherein the First Appellate District (San Francisco) characterized the case to the extent not limited to its facts, as "inconsistent with ... Supreme Court decisions."

Footnote 20. [11 Cal. App. 4th 1598 \(1992\)](#); the Sixth Appellate District is headquartered in San Jose.

Footnote 21. See Robert J. Bezemek, "A Short Primer on Retirees' Vested Health Benefits," 163 Cal. Pub. Emp. Rel. J. (December 2003) at page 15, and generally. However, in a public letter appearing in the February 2003 *Association of College Educators Update for West Valley-Mission Community College District*, available on the internet at www.wvmccd.cc.ca.us/wvmccd/ace/updates/u0203.pdf, Mr. Bezemek also stated that "[i]f an employee acquired her/his right to benefits through a collectively bargained plan, the assumption is that the plan is subject to change while the employee is still employed, through the bargaining process."

Footnote 22. Arthur A. Hartinger and Amy Lynne Lyman, "An Update of the Vested Benefits Doctrine and Its Effects on Collective Bargaining," CPER Journal No. 162 (October 2003) p.14.

Footnote 23. [Thorning, 11 Cal. App. 4th at 1601.](#)