

IN THE
Supreme Court
OF THE STATE OF CALIFORNIA

RETIRED EMPLOYEES ASSOCIATION OF ORANGE COUNTY
Petitioner,

v.

COUNTY OF ORANGE,
Respondent.

Case No. S184059

AFTER ORDER OF THIS COURT ACCEPTING CERTIFICATION OF QUESTION
FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT,
DOCKET NO. 09-56026

APPLICATION BY THE CALIFORNIA PUBLIC EMPLOYEES'
RETIREMENT SYSTEM TO FILE AMICUS CURIAE BRIEF AND
AMICUS CURIAE BRIEF IN SUPPORT OF PETITIONER

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APPLICATION TO FILE BRIEF AS AMICUS CURIAE

Pursuant to California Rules of Court, rule 8.520(f), the California Public Employees' Retirement System (hereinafter "CalPERS") applies for leave from the Court to file the attached *amicus curiae* brief in this case. The proposed *amicus* brief is filed in support of Petitioner, Retired Employees Association of Orange County (hereinafter "REAOC" or "Petitioner"). The proposed brief is authored in whole by the undersigned counsel for CalPERS. No other person or entity has made monetary contributions intended to fund the preparation or submission of the brief.

I. CalPERS' INTEREST IN THE CASE

This Court accepted certification of the following question: "Whether, as a matter of California law, a California County and its employees can form an implied contract that confers vested rights to health benefits on retired county employees." CalPERS members have a substantial interest in the resolution of this issue.

In 1945, CalPERS was created by the Legislature to provide retirement benefits to over a million active and retired public employees and their beneficiaries. CalPERS was established by the Public Employees' Retirement Law (Government Code §§ 20000 et seq.), and is the largest public pension system in the United States, holding approximately \$214.6 billion in assets. (CalPERS Facts At A Glance: Investments < www.calpers.ca.gov/eip-docs/about/facts/investments.pdf>

[as of December 2010].) As of June 30, 2010, CalPERS had 1,116,044 members and 513,623 retirees, survivors, and beneficiaries. (CalPERS Facts At A Glance: General <www.calpers.ca.gov/eip-docs/about/facts/general.pdf> [as of December 2010].) CalPERS is also responsible for providing health benefits to nearly 1.3 million active and retired California public employees and their families. (CalPERS Facts At A Glance: General <www.calpers.ca.gov/eip-docs/about/facts/general.pdf> [as of December 2010].)

Respondent argues that there is no presumption that health benefit rights are vested rights. CalPERS currently provides health benefits to over 360,000 retired public employees and their families. (CalPERS Health Program Enrollment Report <www.calpers.ca.gov/eip-docs/employer/program-services/health/health-enrollment-report.pdf> [as of December 2010].) If this Court jeopardizes their health benefit rights by failing to recognize that they are vested, it will give license to public employers to unilaterally reduce or eliminate the health benefits of these retirees and their families and for all those other public employees who have been promised retiree health benefits during their careers after retirement. This result would be devastating for all CalPERS members, both retired members and those seeking to retire in the future after having been promised retiree health benefits after retirement. Thus, CalPERS and its members have a direct and substantial interest in the issues presented in the case.

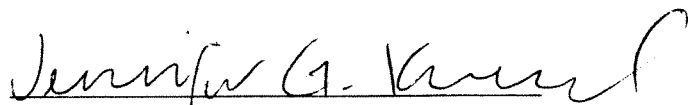
II. CalPERS' PARTICIPATION MAY ASSIST THE COURT

Amicus curiae can often provide a broader prospective on the issues presented than parties advocating their own interests in a particular case. (*State of California v. Superior Court (Lyon)* (1981) 29 Cal.3d 210, 216 (amicus identified broad scope of the court's possible decision); Simpson and Vasaly, *The Amicus Brief* (2d ed. 2004) ABA, p. 24 ("Where larger policy or social issues are implicated by a decision, the amicus has a role that the parties often cannot play.")) Here, CalPERS may assist the Court by explaining the implications of the Court's decision to public employees well beyond those that are parties to this proceeding. CalPERS also has extensive experience with administering retiree health benefits to public employees on a statewide basis. CalPERS' insights gained from this experience may be beneficial to the Court.

Accordingly, CalPERS respectfully requests that its application to participate as *amicus curiae* be granted.

Respectfully submitted,

Dated: December 28, 2010



JENNIFER G. KRENGEL
Attorneys for the California
Public Employees' Retirement System

AMICUS BRIEF

I. INTRODUCTION

In this proceeding, Respondent County of Orange (hereinafter the “County”) calls into question the vested nature of retiree health benefits, challenging a large body of well-settled California law. This is a radical departure in public retirement law that is inconsistent with California’s long history of treating retirement benefits as vested rights. CalPERS respectfully submits that if this Court adopts Respondent’s unprecedented claim that retiree health benefit rights are not vested rights, it will be an invitation to public employers to disregard otherwise valid promises on which hundreds of thousands of state and local public employees, retirees and their families rely. Accordingly, the adverse effect for these individuals could be astronomical. The right to retiree health benefits is a fundamental part of public retirees’ pension benefits which cannot be unilaterally reduced or eliminated by their prior employers without violating the retirees’ constitutional rights.

II. ARGUMENT

A. **California Law Does Not Preclude Implied-In-Fact Contracts That Confer Retiree Health Benefits**

It is well-settled that contracts which bind public employers and confer employment and retirement rights may be implied, absent a statutory prohibition to the contrary. (*Youngman v. Nevada Irrigation Dist.* (1969))

70 Cal.2d 240, 246.) In its opening brief, Petitioner argues that California law does not preclude implied-in-fact contracts in the context of public sector employment. (See Petitioner's Opening Brief on the Merits (September 17, 2010, S184059) at pp. 32-54.) CalPERS joins with Petitioner's arguments on this point and will not repeat those arguments here except to say that whether an implied contract exists depends on the conduct at issue in a specific case. (*Youngman v. Nevada Irrigation Dist.*, *supra*, 70 Cal.2d 240, 246.) Nothing about this Petition requires the Court to determine if an implied contract granting retiree health benefits actually existed between the parties to this case. Rather, the Court is only being asked to acknowledge that such implied-in-fact contracts are not precluded as a matter of law. (*Retired Employees Assn. of Orange County, Inc. v. County of Orange*, (9th Cir. 2010, No. 09-56026) certif. question June 29, 2010, S184059.) Insofar as the law does not preclude implied-in-fact contracts that confer a right to retiree health benefits, we turn to the critical issue regarding the vested nature of that right.

B. Public Sector Retiree Health Benefit Rights Are Necessarily Vested Rights

The vested nature of public retirees' health benefits is solidly established under California law. To appreciate the radical departure in public retirement law that the Respondent advocates in this case, it is helpful to review California's long history of treating retirement benefits as

vested rights.

1. Retirement benefits vest immediately upon hiring.

It is well-settled that upon entering public service, an employee obtains a *vested contractual right* to earn retirement benefits. (*Allen v. City of Long Beach* (1955) 45 Cal.2d 128; *Terry v. City of Berkeley* (1953) 41 Cal.2d 698; *Kern v. City of Long Beach* (1947) 29 Cal.2d 848; *Wisley v. City of San Diego* (1961) 188 Cal.App.2d 482; *Vielehr v. State of California* (1980) 104 Cal.App.3d 392, 395-396; *Carman v. Alvord* (1982) 31 Cal.3d 318, 325.) Pension rights are vested at the time employment is accepted because they are an integral part of the contract of employment and a form of deferred compensation. (*Terry v. City of Berkeley, supra*, 41 Cal.2d 698, 703; *Wallace v. Fresno* (1954) 42 Cal.2d 180, 184; *Kern v. City of Long Beach, supra*, 29 Cal.2d 848, 851-853.) As articulated by this Court: “Pensions are an obligation of great importance. They help induce faithful public service and provide agreed subsistence to retired public servants who have fulfilled their employment contracts.” (*Carman v. Alvord, supra*, 31 Cal.3d 318, 325, fn. 4.)

This Court has recognized on several occasions that the vested nature of pension rights stems from the fact that such rights are a form of deferred compensation that is earned at the time service is performed, even

though the benefits are not provided until retirement. For example, in *Kern v. City of Long Beach*, this Court stated:

[An employee] is not fully compensated upon receiving his salary payments because, in addition, he has then earned certain pension benefits, the payment of which is to be made at a future date...the mere fact that performance is in whole or in part dependent upon certain contingencies does not prevent a contract from arising, and the employing governmental body may not deny or impair the contingent liability any more than it can refuse to make the salary payments which are immediately due.
Kern v. City of Long Beach, supra, 29 Cal.2d at p. 855.

Similarly, in *Terry v. City of Berkeley*, this Court stated that “pension payments are in effect deferred compensation to which the pensioner becomes entitled upon the fulfillment of the terms of the contract which may not be changed to his detriment by subsequent amendment.” (*Terry v. City of Berkeley, supra*, 41 Cal.2d 698, 703.) In short, because pension rights are “a part of the compensation which the employee has at that time earned,” they are not subject to forfeiture. (*Kern v. City of Long Beach, supra*, 29 Cal.2d at p. 854.)

Both the California and U.S. Constitutions bar the State or its subdivisions from passing any law impairing these contractual obligations. (See e.g., Cal. Const. art. I, § 9; U.S. Const. art. I, § 10, cl. 1.) Unnecessary impairment of these vested contractual rights may give rise to a claim under the Contracts Clause and Takings Clause of the State and Federal Constitutions. (See *Kern v. City of Long Beach, supra*, 29 Cal.2d at p. 854)

(total elimination of employees' contractual rights to benefits impermissibly destroyed vested rights); *Allen v. City of Long Beach, supra*, 45 Cal.2d 128 (City's attempt to substitute fixed pension formula for fluctuating formula impermissibly reduced vested rights); *Abbott v. City of Los Angeles* (1958) 50 Cal.2d 438 (City could not modify pension plan to require current employees to contribute a percentage of their salaries to fund benefits).)

2. Retiree health benefits are a form of vested retirement benefits.

Retiree health benefits are among these constitutionally-protected retirement rights. Courts recognize that public employees have a vested right to the continuation of retiree health benefits. (*Thorning v. Hollister School Dist.* (1992) 11 Cal.App.4th 1598; *California League of City Employees Assn's. v. Palos Verdes Library Dist.* (1978) 87 Cal.App.3d 135.) In reaching this conclusion, both the *Thorning* and *California League* courts considered “the effect of [the benefit] in human terms and the importance of [the benefit] to the individual in the life situation.” (*Thorning v. Hollister School Dist., supra*, 11 Cal.App.4th at p. 1609; *California League of City Employees Assn's. v. Palos Verdes Library Dist., supra*, 87 Cal.App.3d at pp. 139-140.) They reasoned that, like pension benefits, the promise to provide retiree health benefits is a significant inducement to prospective employees and a strong incentive to remain employed. (*Ibid.*)

In short, retiree health benefits are simply another form of deferred compensation, often contingent upon many years of continued public service. (*Thorning v. Hollister School Dist.*, *supra*, 11 Cal.App.4th at p. 1607.) The cost of healthcare can be one of the largest expenses a former public servant bears during retirement. Therefore, retiree health benefits are clearly a critical component of the total retirement package. To that end, courts have treated them as part of the protected retirement package. (*Thorning v. Hollister School Dist.*, *supra*, 11 Cal.App.4th at p. 1609; *California League of City Employees Assn's. v. Palos Verdes Library Dist.*, *supra*, 87 Cal.App.3d at p. 140.)

If there is any doubt as to the importance of these benefits, consider the fact that state and local governments were not required to make Medicare contributions for public employees hired before April 1, 1986. (26 U.S.C. § 3121(b)(7)(E)(F).) For such employees, the promise of retiree health benefits substituted the Medicare system to provide medical insurance during retirement. Clearly these employees, when they accepted state service, gave up important Medicare benefits in exchange for the retiree health benefit promised by their employers. In turn, their employers enjoyed significant savings in lieu of making Medicare contributions. Therefore, it would be unreasonable to treat the promise of retiree health benefits as anything other than the kind of deferred compensation this Court has previously protected. (*Terry v. City of Berkeley*, *supra*, 41 Cal.2d

698, 703; *Wallace v. Fresno*, *supra*, 42 Cal.2d 180, 184; *Kern v. City of Long Beach*, *supra*, 29 Cal.2d 848, 851-853.)

3. Retiree health benefit rights must be vested once the employee retires or the right would be illusory.

Courts recognize that reasonable modifications to a vested contractual pension right are permitted prior to retirement in very limited circumstances. (See e.g. *Claypool v. Wilson* (1992) 4 Cal.App.4th 646; *Betts v. Board of Administration* (1978) 21 Cal.3d 859.)¹ However, even in the limited circumstances where reasonable modifications are permitted, they are only permitted for active employees and not for retirees. (See *Claypool v. Wilson*, *supra*, 4 Cal.App.4th 646, 664 (holding that retirees, unlike employees, are not subject to the reasonable modification doctrine), citing *Betts v. Board of Administration*, *supra*, 21 Cal.3d 859, 864 and *Terry v. City of Berkeley*, *supra*, 41 Cal.2d 698, 702).) Therefore, the vested quality of retirement rights is stronger after retirement since the rights cannot be diminished under any modification theory. This Court explained this concept, stating:

¹ In general, a modification will only be permissible if it is reasonable, meaning the modification bears some material relation to the theory of a pension system and the system's successful operation, and the modification is accompanied by comparable new advantages to employees (to the extent the modification results in disadvantages). *Betts v. Board of Administration*, *supra*, 21 Cal.3d 859, 864. In addition, permissible modifications must be for the purpose of keeping the pension system flexible to permit adjustments in accord with changing conditions and at the same time maintaining the integrity of the system. (*Ibid.*)

In the present case the plaintiff had been retired; he had rendered the called-for performance; he had done everything possible to entitle him to the payment of his pension and all conditions precedent to the obligation of the city were fulfilled upon the determination that he be retired as a result of his service-connected disability. The pension payments are in effect deferred compensation to which the pensioner becomes entitled upon the fulfillment of the terms of the contract which may not be changed to his detriment by subsequent amendment.

Terry v. City of Berkeley, supra, 41 Cal.2d 698, 703.

The notion that retirement benefits cannot be modified (even reasonably) after retirement is self-evident; if promised retiree health benefits could be reduced or forfeited after retirement, then the original promise to provide those benefits would be meaningless. Unlike an active employee, a retiree has fully performed his or her side of the employment contract. As a result, the retiree has fully earned all benefits promised under the contract, including retiree health benefits. (*Terry v. City of Berkeley, supra, 41 Cal.2d 698, 703.*) If an employer can simply change its mind and decide not to honor a promised benefit, then there was no promise in the first place. Earned benefits are not subject to an employer's unilateral contractual reduction. (*Kern v. City of Long Beach, supra, 29 Cal.2d at p. 854.*)

Even public sector jurisdictions which reject the concept that retiree health benefits vest upon acceptance of employment agree that they vest at the time of retirement. (See, e.g. *Roth v. City of Glendale (2000) 237*

Wis.2d 173, 185 (holding that the employer cannot offer a retirement system as an inducement to employment and, after an employee has accepted employment under such circumstances, withdraw or terminate the program after an employee has complied with all the conditions entitling him to retirement rights thereunder.)) Similarly, in the private sector where retiree health benefits are not subject to mandatory vesting as a matter of law, retiree health benefits are still understood to be a form of delayed compensation and accordingly some federal jurisdictions recognize a presumption in favor of vesting at retirement. (*Int'l Union et al. v. Yard-Man, Inc.* (1983) 716 F.2d 1476, 1482; see also *Alday v. Raytheon Co.* (2010) 620 F.3d 1219 (finding that employer's agreement to continue to pay premiums for retiree medical insurance survived termination of collective bargaining agreement and could not be unilaterally terminated); *Maurer v. Joy Technologies, Inc.* (2000) 212 F.3d 907, 915 (acknowledging an inference that the parties to a collective bargaining agreement intended for retiree benefits to vest).)

C. If The Court Finds As A Matter Of Law That An Implied Contract Cannot Confer Vested Retiree Health Benefit Rights, It Will Encourage Public Employers To Disregard Otherwise Valid Promises

Public employers face many economic challenges related to promised retiree health benefits. These challenges include the rising cost of

health care, financial accounting hurdles created by Governmental Accounting Standards Board requirements and the sheer number of employees approaching retirement, among others. (See Governmental Accounting Standards Board Statement No. 43, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, <www.gasb.org/st/summary/gstsm43.html> (June, 2004); Governmental Accounting Standards Board Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions <www.gasb.org/st/summary/gstsm45.html> (April, 2004); White House Fact Sheet: Early Benefits from the Affordable Care Act of 2010 Reinsurance Program for Early Retirees, <www.whitehouse.gov/sites/default/files/rss_viewer/reinsurance_early_retirees_fact_sheet.pdf> [as of May 04, 2010]; Legislative Analyst's Office, Retiree Health Care Frequently Asked Questions <www.lao.ca.gov/retireehealth/RetFAQ.aspx> [as of November 16, 2010].) While the economic challenges related to promised retiree health benefits require attention, it would be a mistake to allow employers to bury their heads in the sand and pretend that the promises were never made, particularly in light of the fact that promised retiree health benefits comprise a significant portion of the total value of many retirees' retirement packages. For example, the average monthly pension allowance for a CalPERS retiree is \$2,220.00 per month. (CalPERS Facts At A Glance: Retirement & Membership

<www.calpers.ca.gov/eip-docs/about/facts/retiremem.pdf> [as of December 2010].) The average monthly health premium amount for a CalPERS retiree and his or her dependents is approximately \$641.31 per month.² When compared to the relatively low average monthly pension allowance, the cost of retiree health coverage represents a large part of the value of the total retirement package.

If the Court finds as a matter of law that vested retiree health benefits cannot be conferred by implied-in-fact contracts, it will be license for public employers to disregard otherwise valid promises for reasons that have nothing to do with the implied nature of the promise. Public employers who have intentionally and consciously promised retiree health benefits will be incentivized to dispute the existence of those obligations, rather than deal with the economic realities of honoring those obligations, simply because non-substantive technicalities make a contract implied rather than express.

The result would be devastating for the many hundreds of thousands of retirees and beneficiaries who currently receive retiree health coverage through CalPERS. Currently, over 360,000 people (including retirees and

² CalPERS' generated this number based on premium amounts for retirees enrolled in CalPERS health benefits in December of 2010. (See Health Program Enrollment Report <www.calpers.ca.gov/eip-docs/employer/program-services/health/health-enrollment-report.pdf> [as of December 2010]; CalPERS Facts At A Glance: Health <www.calpers.ca.gov/eip-docs/about/facts/health.pdf> [as of December 2010].)

their beneficiaries) receive CalPERS health insurance coverage on account of a retiree health benefit right, and this number has steadily increased over the past several years. For example, in 2005 only 292,281 people received CalPERS retiree health insurance coverage, showing that the growth rate for retiree health insurance coverage has been approximately 22% in the past five years. (CalPERS Health Program Enrollment Statistics [generated in November 2010].) CalPERS expects the number of retiree health insurance participants to continue to increase as more people retire in the coming decade. Accordingly, this Court's decision could impact not only the retiree health benefit rights of the current 360,000 participants, but those of future retirees and their families as well.

Public employers should be required to honor their promises to retirees and should not be granted license to unilaterally reduce or eliminate previously promised retiree health benefits. Any other result would have severe ramifications across the state of California, creating distrust among employees and rendering the deferred components of their compensation packages meaningless. This Court has recognized that one of the primary objectives in providing pensions for government employees is to induce competent persons to enter and remain in public employment, and has further recognized that this purpose "would be thwarted if a public employee could be deprived of pension benefits, and the promise of a pension annuity would either become ineffective as an inducement to

public employees or it would become merely a snare and a delusion to the unwary.” (*Kern v. City of Long Beach, supra*, 29 Cal.2d 848, 856.)

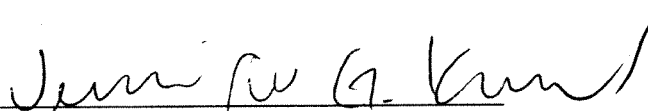
Similarly, if public sector employees have no reason to believe that their employers will honor their retirement promises, then those promises will have no value to employees, and this important aspect of public service compensation packages will be lost.

III. CONCLUSION

For the reasons described above, the Court should confirm that, as a matter of California law, a California County and its employees can form an implied contract that confers vested rights to health benefits on retired county employees.

Respectfully submitted,

Dated: December 28, 2010



JENNIFER G. KRENGEL
Attorneys for the California
Public Employees' Retirement System

IN THE SUPREME COURT OF CALIFORNIA

Case Name: Retired Employees Assn. of Orange Supreme Court Case No. S184059
County, Petitioner v. County of
Orange, Respondent

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Attorney For: California Public Employees Retirement System

CERTIFICATE OF INTERESTED PARTIES OR ENTITIES
(Cal. Rules of Court, rule 8.208)

(Check One) [X] INITIAL CERTIFICATE [] SUPPLEMENTAL CERTIFICATE

This certificate is being submitted on behalf of the following party:
Amicus Curiae of the California Public Employees' Retirement System in
Support of Petitioner, Retired Employees Assn. of Orange

Please check the applicable box:

[X] There are no interested entities or persons to list in this certificate per California
Rules of Court, rule 8.208(d).

[] Interested entities or persons are listed below:

Table with 2 columns: Full Name of Interested Entity or Party, Nature of Interest (Explain)

- (1)
(2)
(3)
(4)
(5)

The undersigned certifies that the above-listed persons or entities (corporations, partnerships, firms, or any other association, but not including government entities or their agencies) have either (1) an ownership interest of 10 percent or more in the party if it is an entity; or (2) a financial or other interest in the outcome of the proceeding that the justices should consider in determining whether to disqualify themselves, as defined in rule 8.208(e)(2).

Date: December 28, 2010

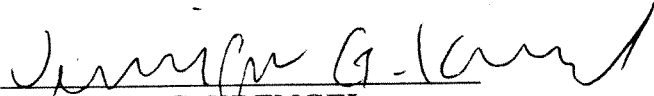
JENNIFER G. KRENGEL
(Type or Print Name)

[Handwritten Signature]
(Signature of Party or Attorney)

**CERTIFICATE OF COMPLIANCE
WITH CAL. RULES OF COURT, RULE 8.204(c)**

I hereby certify that the foregoing Application by the California Public Employees' Retirement System to File Amicus Curiae Brief in Support of Petitioner does not exceed 14,000 words, including footnotes. According to the word processing system used to prepare this brief (Microsoft Word 2007), the word count of the brief is 3470, not including the Table of Contents, Table of Authorities, Certificate of Service of this Certificate of Compliance.

Dated: December 28, 2010


JENNIFER G. KRENGEL
Attorneys for the California Public
Employees' Retirement System

PROOF OF SERVICE

I am employed in the County of Sacramento, State of California. I am over the age of 18 and not a party to the within action; my business address is: California Public Employees' Retirement System, Lincoln Plaza North, 400 "Q" Street, Sacramento, CA 95811 (P.O. Box 942707, Sacramento, CA 94229-2707).

On December 28, 2010, I served the foregoing document described as:

APPLICATION BY THE CALIFORNIA PUBLIC
EMPLOYEES' RETIREMENT SYSTEM TO FILE AMICUS
CURIAE BRIEF AND AMICUS CURIAE BRIEF
IN SUPPORT OF PETITIONER

on interested parties in this action by placing ___ the original XX a true copy thereof enclosed in sealed envelopes addressed as follows:

Michael P. Brown
MOSCONE EMBLIDGE & SATER,
LLP
220 Montgomery Street, Suite 2100
San Francisco, CA 94104
*Counsel for Petitioner Retired
Employees Association of Orange
County*

Jennifer Nock
MEYERS NAVE RIBACK
SLIVER & WILSON LLP
555 12th Street, Suite 1500
Oakland, CA 94607
*Counsel for Respondent County of
Orange*

Teri L. Maksoudian
Office of the County Counsel
333 W. Santa Ana Blvd., Suite 407
Santa Ana, CA 92702-1379
*Counsel for Respondent County of
Orange*

[] BY MAIL -- As follows: I am "readily familiar" with the firm's practice of collection and processing correspondence for mailing. Under that practice it would be deposited with the U.S. postal service on that same day with postage thereon fully prepaid at Sacramento, California, in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if postal cancellation date or postage meter date is more than one day after the date of deposit for mailing an affidavit.

[X]

BY OVERNIGHT DELIVERY: I caused such envelope(s) to be delivered to the above address(es) within 24 hours by overnight delivery service.

Executed on December 28, 2010, at Sacramento, California.

I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Roland Hyatt
NAME


SIGNATURE