

No. S239958

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

CAL FIRE LOCAL 2881 (formerly known as CDF Firefighters), *et al.*

Petitioners and Appellants,

v.

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM
(CalPERS)

Defendant and Respondent,

and

THE STATE OF CALIFORNIA,

Intervener and Respondent.

SUPREME COURT
FILED

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On Review From The Court Of Appeal For the First Appellate District,
Division Three, Civil No. A142793

After An Appeal From the Superior Court For The State of California,
County of Alameda, Case Number RG12661622, Hon. Evelio Grillo,
Presiding Judge

OPENING BRIEF ON THE MERITS

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I.

SUMMARY OF ARGUMENT

This case involves whether the Legislature may eliminate the right of existing state and local public employees to purchase additional service credits pursuant to former Government Code section 20909 (“section 20909”).¹ The Legislature enacted the benefit in 2004, in part to allow employees to take educational and child-rearing leaves of absence without foregoing their pension benefits. It abruptly modified the statute in 2012, to prevent any purchases of additional service credits after December 31, 2012, prompting this action.²

Petitioners contend that under this Court’s extensive and longstanding vested rights doctrine—dating back to *Allen v. City of Long Beach* (1955) 45 Cal.2d 128, and arguably to *O’Dea v. Cook* (1917) 176 Cal. 659—the repeal of a pension right without providing adversely affected employees with a comparable pension advantage violated the Contracts Clause in article 1, section 9 of the California Constitution. This follows because the right to purchase additional service credits at any point

¹ All statutory citations are to the Government Code unless expressly stated otherwise.

² Strictly speaking, the Legislature modified section 20909 by adding subsection 20909(g) in tandem with a new enactment, section 7522.46, which ended purchases after December 31, 2012; however, as the court of appeal recognized (Slip Op. at p. 6), this “effectively repeal[ed]” the pension right—so Petitioners use the term “repeal” or “repealed” herein to describe the elimination of the right to purchase additional service credit.

prior to retirement was one of a wide array of pension rights under the Public Employees' Retirement Law ("PERL"), section 20000 *et seq.* When existing employees performed service during periods in which section 20909 was offered as part of their employment terms with the state employer, vested contractual rights were created.

In this Opening Brief, Petitioners argue that under this Court's vested rights precedents (which have been widely and, until recently, invariably followed by the courts of appeal) section 20909 created a vested right. The repeal of section 20909 in 2012 therefore violated employees' vested rights in two distinct ways. First, the Legislature failed to establish that the elimination of the right to purchase additional service credits was necessary to preserve and maintain the pension system. Second, it failed to provide employees who were disadvantaged by repeal with offsetting comparable pension advantages.

This Court has routinely struck down modifications—whether statutory (*Olson v. Cory* (1980) 27 Cal.3d 532) or constitutional (*Legislature v. Eu* (1991) 54 Cal.3d 492)—to vested pension benefits. It should do so again here because no special circumstances warrant abandoning its longstanding precedent.

II.

ISSUE PRESENTED

1. Was the option to purchase additional service credits a vested pension right or benefit?
2. Was the repeal of section 20909 necessary to preserve and maintain PERL?
3. Did the repeal of section 20909, without providing disadvantaged employees with an offsetting pension advantage, violate the Contracts Clause?

III.

STANDARD OF REVIEW

The facts in this case are undisputed; accordingly, because the issues presented involve interpretation of statutes and our state Constitution, this Court exercises its independent judgment and reviews the matter *de novo*. (*Bd. of Administration of the Public Employees' Retirement System v. Wilson* (1997) 52 Cal.App.4th 1109, 1129 [“The ultimate questions of whether vested contractual rights exist and whether impairments are unconstitutional present questions of law subject to independent review”].)

IV.

FACTS AND PROCEDURAL HISTORY

Petitioners are a labor union and its state employee members whose pension benefits are administered by the California Public Employees'

Retirement System (“CalPERS”). They sued in early 2013, after the Legislature repealed section 20909, a pension statute, which had formerly allowed employees to purchase additional service credit. (Joint Appendix (“JA”) at p. 001 [Petition].) Petitioners alleged that the repeal of section 20909 violated the Contracts Clause of the California Constitution. (JA at p. 004.) The lawsuit did not contest the Legislature’s right to prevent application of the statute to future employees.

A. In 2004, The Legislature Created The Right Of Qualifying Employees To Purchase Additional Service Credit

CalPERS is a public pension system, established under PERL, which defines its pension rights exclusively by statute. (Slip Op. at p. 2.)

CalPERS administers benefits and discharges its duties solely in the interest of plan participants and their beneficiaries. (Cal. Const. art. XVI, § 17(b).)

CalPERS’ plans provide defined benefits to members based on age at retirement, service credit and final compensation. (See, e.g., § 21363.4 [state firefighters’ safety formula].) The more service credit the employee has, the higher will be his or her monthly pension.

The right to purchase service credit began when section 20909 was enacted in 2004, and remained available until December 31, 2012. It permitted a “member who has at least five years of credited state service” to make a one-time purchase of “not less than one year, nor more than five years, in one-year increments, of additional retirement service credit in the

retirement system ... at any time prior to retirement.” (§ 20909(a) and (b).)

This right to secure additional service credit is not unusual—PERL also allows employees to supplement their service credit with, for example: prior military service (§§ 21032, 21033; see §§ 21020, 21024); certain leaves converted into additional retirement service credit (§ 20898 [credit for holidays, sick leave, vacation, or leave of absence]); and, two years of additional service credit for certain retiring judicial branch state employees (§ 20902.5). In fact, from section 20890 to section 21054, PERL provides dozens of statutes governing the use, crediting and computation of service credit relating to service other than that provided directly to the state.

The opportunity to purchase additional service credits provided advantages to employees:

Being able to purchase [additional service credits] allows members of CalPERS to increase their retirement benefits at no cost to employers. Many members take breaks in employment to raise children, advance their educations, or work in the private sector for a time. For members who do not enter CalPERS covered employment until later in life or who have breaks in service, purchasing [additional service credits] may contribute to providing a livable retirement income.

(JA at pp. 260, 266, 271-272.) Thus, an employee might take three years off to improve her education, to care for a new child or a relative, or might plan to do so, and rely upon section 20909 to allow her to purchase additional service credit so as to allow her to retire without loss of time or

future income level. Because pension benefits are predominately based on length of service and compensation, without the statute employees who take leave either postpone retirement or suffer a reduced pension.

The entire cost of the benefit, if exercised, was designed to be borne by the employee, who was required to “contribute ‘an amount equal to the increase in employer liability, using the pay rate and other factors affecting liability on the date of the request for costing of the service credit.’” (Slip Op. at p. 2, citing § 20909, subs. (a), (b); § 21052; see also *Marzec v. California Public Employees Retirement System* (2015) 236 Cal.App.4th 889, 905 [“... section 21052 provides that if an employee elects to purchase [additional service credit] it is the employee, not the employer, who is required to contribute ‘an amount equal to the increase in employer liability’”].) The “increase in employer liability” was calculated as the “present value of the projected increase in liability to the CalPERS system.” (§ 21052; Assem. Bill No. 719, 2nd reading Aug. 18, 2003, Bill Analysis, p. 2.) This right nonetheless benefitted employees because it gave them the option of turning savings into defined pension benefits.

B. CalPERS Recognized And Publicized That The Right To Purchase Additional Service Credit Was A Vested Right

CalPERS’ role administering pensions gives it special expertise in interpreting pension laws. (*People ex. rel. Lungren v. Superior Court* (1996) 14 Cal.4th 294, 309 [“contemporaneous administrative construction

of [an] enactment by those charged with its enforcement ... is entitled to great weight”], quoting *Coca-Cola Co. v. State Bd. of Equalization* (1945) 25 Cal.2d 918, 921.) CalPERS agreed with Petitioners that section 20909 created vested rights. Its 2011 publication “Vested Rights of CalPERS Members: Protecting the Pension Promises Made to Public Employees” was widely-read and remained on its website, unaltered, until at least December 21, 2016.³ CalPERS recognized that the right to purchase additional service credits vests immediately when offered:

RULE 1:

**Employees Are Entitled To Benefits In Place
During Their Employment**

Public employees obtain a vested right to the provisions of the applicable retirement law that exist during the course of their public employment. Promised benefits may be increased during employment, but not decreased, absent the employees’ consent. *These rules apply to all active CalPERS members, whether or not they have yet performed the requirements necessary to qualify for certain benefits that are part of the applicable retirement law. For example, even if a member has not yet satisfied the five year minimum service prerequisite to receiving most service and disability benefits, the member’s right to qualify for those benefits upon*

³ The publication remained on CalPERS website until at least December 21, 2016 (the day before the court of appeal heard oral argument) at www.Calpers.ca.gov/docs/forms-publications/vested-rights-members-pdf. It was subsequently removed.

completion of five years of service vests as soon as the member starts work.

(JA at p. 229, emphasis added.) More specifically, CalPERS described the right to “Purchase service credit under the terms that existed in the law when they provided service, if the member satisfies all eligibility requirements” as one of eleven defined vested rights. (JA at p. 234.) Individual petitioners’ reliance on the future ability to purchase is set forth in the record. (JA at p. 160.)

C. The Legislature Repealed Section 20909 And Petitioners Filed Suit

On January 1, 2013, section 7522.46 became effective as part of the Public Employees’ Pension Reform Act of 2013 (“PEPRA”). PEPRA significantly changed public employee pensions for *future* employees, including reducing pension formulas. (See Legis. Counsel’s Dig., Assem. Bill No. 340 (2011-2012 Reg. Sess.)) But section 7522.46 added subsection 20909(g), which eliminated the right of *current and future* employees to purchase service credit.

It is uncontested that the Legislature offered no comparable pension advantages to existing employees who were disadvantaged by repeal. Moreover, in passing PEPRA the Legislature failed to make any specific finding that repeal of section 20909—or any other part of PEPRA—was necessary to preserve and maintain the integrity of the system.

D. The Trial Court Determined Section 20909 Created No Vested Rights

Petitioners sued in the Superior Court of Alameda County seeking to compel CalPERS to allow future purchases of service credits for qualifying employees employed as of December 31, 2012. (JA at p. 166.) Among the Petitioners is one firefighter who missed eligibility to purchase additional service credits by 16 days (JA at pp. 158, 164), and others who provided five years of service, and planned to purchase additional service credits, but were financially unable to do so before December 31, 2012. (JA at pp. 157-158.) CalPERS declined to defend the legislation, so Respondent State of California intervened, without opposition, to defend it.

The trial court held a hearing on the petition on February 24, 2014. Several months later, on May 12, 2014, the trial court issued a final order and on June 5, 2014 an amended final order, both denying the petition.

In its order the trial court made a number of erroneous determinations. It concluded that: even if section 20909 created a vested pension right, “the Legislature lawfully eliminated the benefit as a permissible modification to a pension plan” (JA at p. 390); the adoption of sections 7522.46 and 20909(g) “were materially related to the theory and successful operation of a pension system because they restricted the pension system to providing retirement benefits based on work performed” (JA at p. 391); the Legislature did not intend to create a vested right

because the phrase “at any time” in subsection 20909(b) meant only at any time the statute was in effect (JA at pp. 397-400); and no service was provided in exchange for the right to purchase additional service credit or for the additional service credit itself. (JA at p. 400.)

The trial court entered judgment against Petitioners on June 19, 2014. (JA at pp. 428-429.)

E. The Court Of Appeal Held That Pension Reductions Need Not Be Offset By Comparable Benefits So Long As Employees Retain A “Reasonable” Pension

On appeal, Petitioners relied on this Court’s longstanding vested rights jurisprudence. (AOB at pp. 11-12.) The State did not contest that body of law but argued that the right to purchase service credits was an “option,” not a pension benefit. (State’s Br. at p. 13.) It reasoned that if the employee bore the cost of the benefit, this right to purchase neither qualified as a deferred compensation nor a pension benefit, and consequently the Legislature could freely repeal the statute. (*Id.* at p. 15.) Oral argument occurred on December 21, 2016.

On December 30, 2016, the court of appeal issued its opinion rejecting Petitioners’ claims. First, it faulted section 20909 for failing to “unambiguously state[] an intent by the Legislature to create a vested pension right.” (Slip Op. at p. 9, citing *Retired Employees Ass’n of Orange County, Inc. v. County of Orange* (2011) 52 Cal.4th 1171, 1190.) Without such a statement, reasoned the lower court, the Legislature’s “continuing

government power” allowed it to eliminate the benefit. (Slip Op. at pp. 7-9.)

Second, accepting for the sake of argument that vested pension rights were created, the lower court held that “California law is quite clear that the Legislature may indeed modify or eliminate vested pension rights in certain cases.” (Slip Op. at p. 10.) The lower court cited older decisions of this Court for the proposition that the “government entity providing the pension may make reasonable modifications and changes in the pension system ... [t]o maintain the integrity of the system and carry out its beneficent purpose.” (Slip Op. at p. 10, quoting *Kern v. City of Long Beach* (1947) 29 Cal.2d 848, 854-855 and citing *Wallace v. City of Fresno* (1954) 42 Cal.2d 180 and *Packer v. Board of Retirement* (1950) 35 Cal.2d 212.) But when it confronted the critical additional component of pension law—that “changes in a pension plan which result in disadvantage to employees should be accompanied by comparable new advantages” (Slip Op. at p. 11, quoting *Betts v. Board of Administration* (1978) 21 Cal.3d 859, 864 [italics in the original])—the lower court fell back on *Marin Association of Public Employees, et al. v. Marin County Employees’ Retirement Association, et al.* (2016) 2 Cal.App.5th 674, 704-705 (review granted, California Supreme Court, Case No. S237460) and its view that so long as pension reductions do not destroy a public employee’s pension, the Legislature is not

foreclosed by the Contracts Clause from making modifications. (Slip Op. at p. 12, n. 5, and pp. 13-16.)

Third, it accepted the State's argument that any purchase of service credits under section 20909 was not deferred compensation and therefore was not a pension benefit. (Slip Op. at p 13; but see *Marzec, supra*, 236 Cal.App.4th at p. 905 [right to purchase service credit pursuant to section 20909 "is a benefit that was offered to some individuals who were already members of CalPERS"].) Despite the statute requiring that employees provide five years of service before being eligible to exercise their right to purchase service credit, the Court concluded that the benefit was "wholly unrelated" to service. (*Id.*)

V.

LONGSTANDING PRINCIPLES GOVERN PUBLIC EMPLOYEE PENSION RIGHTS

A. A Vested Contractual Right To Pension Benefits Accrues Upon A Public Employee's Acceptance Of Employment

Unlike other terms of public employment, which are wholly a matter of statute, pension rights are obligations protected by the Contracts Clause of the federal and state Constitutions. (U.S. Const., art. I, § 10, cl. 1; Cal. Const., art. I, § 9 ["a law impairing the obligation of contracts may not be passed"]; *United Firefighters of Los Angeles City v. City of Los Angeles* (1989) 210 Cal.App.3d 1095, 1102.) "A public employee's pension constitutes an element of compensation, and a vested contractual right to

pension benefits accrues upon acceptance of employment. Such a pension right may not be destroyed, once vested, without impairing a contractual obligation of the employing public entity.” (*Betts, supra*, 21 Cal.3d at p. 863; *Allen v. City of Long Beach* (1955) 45 Cal.2d 128, 131; *Kern, supra*, 29 Cal.2d at p. 855 [“employing governmental body may not deny or impair the contingent liability [of pensions] any more than it can refuse to make the salary payments which are immediately due”].) These rights vest in the sense that they cannot be destroyed by statutory repeal—even before the benefit has been accessed or the time for retirement has arrived. (*Kern, supra*, 29 Cal.2d at pp. 855-856; *Wallace, supra*, 42 Cal.2d at p. 183.)

This follows because, from the moment an employee begins service, the pension is part of the contemplated compensation and part of the contract of employment itself. (*Kern, supra*, 29 Cal.2d at pp. 855-856; *Wallace, supra*, 42 Cal.2d at p. 183; *O’Dea, supra*, 176 Cal. at pp. 661-662.) Moreover, public employees have the “right to earn future pension benefits through continued service, on terms substantially equivalent to those” existing at the time they began working, or added at any point during their service. (*Legislature v. Eu, supra*, 54 Cal.3d at p. 528; *Sweesy v. Los Angeles County Peace Officers’ Retirement Board* (1941) 17 Cal.2d 356, 361 [public employees entitled to subsequent benefit increases]; *Carman v. Alvord* (1982) 31 Cal.3d 318, 325 [“[b]y entering public service an

employee earns a vested contractual right to earn a pension on terms substantially equivalent to those then offered by the employer”].)

B. Modifications To Vested Pension Benefits Are Controlled By A Strict And Longstanding Rule

While the constitutional proscription against the destruction of vested contractual pension rights “does not absolutely prohibit their modification” (*Allen v. Board of Administration* (1983) 34 Cal.3d 114, 120), lawmakers’ power to modify pension rights, once vested, is “quite limited.” (*In re Retirement Cases* (2003) 110 Cal.App.4th 426, 447.) Over a series of cases from *Allen v. City of Long Beach, supra*, 45 Cal.2d 128 to *Legislature v. Eu, supra*, 54 Cal.3d 492, this Court developed what has become known as “the California Rule”:

With respect to active employees ... any modification of vested pension rights must be reasonable, must bear a material relation to the theory and successful operation of a pension system, and, when resulting in a disadvantage to employees, must be accompanied by comparable new advantages. [Citations.] As to retired employees, the scope of continuing governmental power may be more restricted, the retiree being entitled to the fulfillment without detrimental modification of the contract which he already has performed.

(*Allen v. Board of Administration, supra*, 34 Cal.3d at p. 120

[disadvantageous amendments to pension plan ruled unconstitutional]; see

also *Abbott v. City of Los Angeles* (1958) 50 Cal.2d 438 [amendment

substituting fixed pension for payments on a fluctuating basis invalid; increase in benefits for a narrow class of pensioners was not commensurate with detriment imposed], *Betts, supra*, 21 Cal.3d 859 [no comparable benefits were provided to offset the detriment to former State Treasurer of less generous, later-enacted method of calculating pension]; *Olson v. Cory* (1980) 27 Cal.3d 532, 541 [statute limiting cost-of-living increases for retired judges failed to provide any offsetting comparable advantages].) Importantly, “it is the advantage or disadvantage to the particular employees ... by which modifications to pension plans must be measured.” (*Abbott, supra*, 50 Cal.2d at p. 449.)

Thus, a modification of a vested pension benefit must pass two tests: (1) it “must bear a material relation to the theory and successful operation of a pension system;” and (2) “a disadvantage to employees, must be accompanied by comparable new advantages.” (*Allen v. Board of Administration, supra*, 34 Cal.3d at p. 120.)

As discussed below, petitioner contends that the repeal of section 20909 satisfied neither test.

VI.

THE REPEAL OF SECTION 20909 VIOLATED THE VESTED RIGHTS OF EXISTING EMPLOYEES

A. The Right To Purchase Additional Service Credits Under Section 20909 Was A Pension Right

Whether section 20909 is classed as a pension right or benefit, the Contracts Clause protected existing employees' rights under it. (*Board of Retirement v. Wilson, supra* 52 Cal.App.4th at p. 1145, quoting *Valdes v. Cory* (1983) 139 Cal. App. 3d 773, 784 ["controlling principle applies to modification of any 'vested contractual pension rights.'"]) The court of appeal committed reversible error when it held that section 20909 did not create vested contractual pension rights. It reasoned that because the employee "pays the present value cost of the additional service credit" (§ 21052), "this simply is not a case where the state provided a retirement benefit to its employees in exchange for their work performance." (Slip Op. at p. 16.) As explained below, this unnecessarily narrow view that "pension benefits are 'deferred compensation that has been earned through the performance of work' not ... an option to purchase nonqualifying service credit wholly unrelated to actual services provided or work performed" (Slip Op. at p. 13), caused the lower court to fail to apply California law.

Section 20909 was a component part of PERL, adopted on employees' behalf by the Legislature. And PERL's provisions "become a part of the contemplated compensation for those services and so in a sense a part of the contract of employment itself." (*O'Dea, supra*, 176 Cal. at pp. 661-662; *Int'l Ass'n of Firefighters v. City of San Diego* (1983) 34 Cal.3d 292, 302 [public pension plan part of employment "contract"].) If an employee exercised the right to purchase additional service credit, it increased the pension benefit—which the Legislature fully intended as a means to encourage employees to take leaves of absence from state service. (JA at pp. 260, 266, 271-272.) Importantly, the benefit was *directly* tied to state service: only a "member who has at least five years of credited state service" (§ 20909(b)) could exercise the option to buy additional service credit.

Courts sometimes frame pension benefits as deferred compensation. (*Kern, supra*, 29 Cal.2d at p. 853 ["a pension right is an 'integral portion of contemplated compensation'"], quoting *Dryden v. Bd. of Pension Commissioners* (1936) 6 Cal.2d 575, 579.) But the court of appeal read this too rigidly, embracing the trial court's reasoning that the law distinguished between service credit that was earned through labor and that which was purchased. (Slip Op. at p. 13.)