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OPINION NUMBER 2015-3

DATE: October 26, 2015

SUBJECT: Legal Status of Annual Supplemental Benefit (13th Check)

TO: Honorable Mayor and Councilmembers

PREPARED BY: City Attorney

INTRODUCTION

In August 2015, the City of San Jose in Northern California (San Jose) announced a proposed settlement of its dispute with the employee organizations representing its police officers and firefighters over a pension reform measure, known as Measure B, approved by San Jose voters in June 2012. The settlement involves invalidation of Measure B through litigation of a quo warranto writ, and then replacement of Measure B with agreed-upon alternative reforms. The agreed-upon reforms include elimination of so-called "bonus checks" for retirees.[1]

Earlier this year, a superior court judge upheld the elimination of special reserve funds for so-called "bonus checks" in Measure B, but San Jose's retired employees and others are appealing that decision. The settlement that San Jose is pursuing is global in nature and requires the retired employees to join, and San Jose has proposed a modified benefit for retired employees to replace the benefits they received from the special reserve funds.

The elimination of the reserve funds, which allowed for supplemental benefits, has prompted questions about the ability of the City of San Diego (City) to eliminate its retirement benefit known as the Annual Supplemental Benefit or "13th Check." The 13th Check is paid to eligible retirees when the San Diego City Employees' Retirement System (SDCERS) trust fund earnings for a given year, subtracted by an amount sufficient to credit interest to SDCERS members and the City and an amount to cover administrative costs and expenses, is $100,000 or more. San Diego Municipal Code (Municipal Code or SDMC) §§ 24.1502, 24.1503. When

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[1] *See* City of San Jose Memorandum, July 24, 2015, http://www.sanJose ca.gov/DocumentCenter/View/45253. *See also* San Jose MercuryNews, "San Jose, Unions Reach Pension Settlement," August 14, 2015, http://www.mercurynews.com/bay-area-news/ci_28490334/san-jose-unions-reach-pension-settlement; San Jose MercuryNews, "San Jose Council Approves Measure B Settlement," August 25, 2015, http://www.mercurynews.com/bay-area-news/ci_28700793/measure-b-settlement-at-top-san-jose-council

initially implemented, the 13th Check was paid from "Surplus Earnings," which were commonly referred to as the "Waterfall." San Diego Ordinance O-19781 (Sept. 11, 2008). The use of the "Waterfall" was eliminated by ordinance in 2008. *Id.* And the 13th Check is now a benefit that is reflected in the actuarial calculation of the City's Annual Required Contribution. SDMC § 24.1501.

In 2010, this Office issued Legal Opinion 2010-1, entitled "Pension Benefits and Other Post-Employment Benefits." 2010 Op. City Att'y 2 (2010-1; Jan. 21, 2010) (2010 Legal Opinion). In that Legal Opinion, this Office concluded that the City's 13th Check may not be eliminated for any active or retired employees, who were hired or assumed office prior to July 1, 2005, without providing a comparable benefit under the general legal principles in California related to vested pension benefits. The 13th Check was prospectively eliminated for employees hired on or after July 1, 2005. SDMC § 24.1503.1.

In this supplemental opinion, we re-examine the City's 13th Check in light of recent events in San Jose and a recent court of appeal case involving the City and County of San Francisco.

QUESTION PRESENTED

Can the City rely on the proposed settlement in San Jose to seek elimination of the City's 13th Check?

SHORT ANSWER

No. The City's 13th Check was implemented as part of the settlement of class action litigation. Further, its terms are different from the San Jose benefit. To determine whether a retirement benefit is vested, a court will look to the specific terms and conditions of the benefit. Here, a court would likely find the 13th Check vested, meaning it may only be modified under narrow and specific circumstances and accompanied by a comparable advantage for employees entitled to the benefit.

DISCUSSION

I. CALIFORNIA COURTS HAVE HELD THAT THE REDUCTION OF A COST OF LIVING ALLOWANCE, WITHOUT A COMPARABLE NEW ADVANTAGE IMPAIRS THE PENSION CONTRACT.

It is well established in California that "[a] public employee's pension constitutes an element of compensation, and vested contractual right to pension benefits accrues upon acceptance of employment." *Protect Our Benefits v. City & County of San Francisco*, 235 Cal. App. 4th 619, 628 (2015) (citing *Betts v. Board of Administration*, 21 Cal. 3d 859, 863 (1978)). Pension rights are obligations protected by the contract clause of the federal and state Constitutions. *Id.* (citing U.S. Const., art. I, § 10; Cal. Const., art. I, § 9). "Upon accepting public employment, one acquires a vested right to a pension based on the system then in effect, and to additional pension benefits conferred during his or her subsequent employment." *Id.*

Employees have a contractual right to pension benefits because they earn them in exchange for the services they provide to their employer. *Claypool v. Wilson*, 4 Cal. App. 4th 646, 662 (1992). Pension benefits are a form of deferred compensation. *Miller v. State of California*, 18 Cal. 3d 808, 814 (1977). The contractual right to a pension benefit is "defined by the benefits and law in place when an employee is rendering services, not by changes that occur after retirement." *In re Retirement Cases*, 110 Cal. App. 4th 426, 447 (2003).

Vested, constitutionally protected pension benefits may be modified only under limited circumstances and if accompanied by a comparable new advantage. The California Supreme Court has explained:

> 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 disadvantage to employees, must be accompanied by comparable new advantages. 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, 34 Cal. 3d 114, 120 (1983) (internal citations omitted).

A modification to a vested benefit must not "frustrate the reasonable expectations of the parties to the contract of employment." *Frank v. Board of Administration*, 56 Cal. App. 3d 236, 244 (1976).

Protected rights may be created in an express contract, or may be implied from an ordinance or resolution, "when the language or circumstances accompanying its passage clearly evince a legislative intent to create private rights of a contractual nature enforceable against the [governmental body]." *Retired Employees Ass'n v. County of Orange*, 52 Cal. 4th 1171, 1177 (2011).

Vested rights may be created by charters and municipal code provisions. *See International Ass'n of Firefighters v. City of San Diego*, 34 Cal. 3d 292, 302 (1983). A legislative intent to grant contractual rights can be implied from a legislative enactment, like an ordinance or resolution, "if it contains an unambiguous element of exchange of consideration by a private party for consideration offered by the state." *California Teachers Ass'n v. Cory*, 155 Cal. App. 3d 494, 505 (1984).

In a number of cases, California courts have held that the reduction of a cost of living allowance (COLA), without a comparable new advantage, impairs a pension contract. *See, e.g.*, *Protect Our Benefits*, 235 Cal. App. 4th at 629. Earlier this year, the Court of Appeal, First District, Division 5 reaffirmed this long-standing rule, when it held that a 2011 voter approved initiative measure, which amended the charter of the City and County of San Francisco to, among other things, condition payment of a supplemental COLA for retired employees, was

unconstitutional. *Id.* A political action committee representing the interests of retired employees filed a writ of mandate, challenging the initiative, known as Proposition C, on the grounds that it impaired a vested contractual pension right under the control classes of the federal and state Constitutions. *Id.*

Prior to voter approval of Proposition C, retired employees were eligible to receive a supplemental COLA as part of their pension benefits when the retirement fund's actual earnings from the previous year exceeded projected earnings. *Id.* at 622. Proposition C modified the supplemental COLA to condition payment on the retirement fund being "fully funded" based on the market value of the assets for the previous year. *Id.* The political action committee argued that Proposition C impaired vested contractual rights of San Francisco workers and pensioners because the full funding requirement reduced the supplemental COLA pension benefit. *Id.* at 627. The court of appeal agreed. *Id.* at 630.

The court of appeal concluded that the modification was unconstitutional, as applied to existing employees and employees who retired after the supplemental COLA took effect in 1996. *Id.* at 622. The court explained that voters had made the supplemental COLA permanent by a charter amendment in 2002. *Id.* at 625. And, in 2008, voters raised the maximum annual amount of the supplemental COLA. *Id.* The court found that Proposition C reduced the supplemental COLA benefit, by modifying the conditions upon which it would be paid, without providing a comparable advantage to impacted employees and retirees. The court wrote:

> Because there might be some years in which the Fund will earn more than projected, but will not be fully funded under a market value measurement, the full funding requirement results in a detriment to pensioners who would otherwise be entitled to receive the supplemental COLA. This diminution in the supplemental COLA cannot be sustained as reasonable because no comparable advantage was offered to pensioners or employees in return.

Id. at 630.

The court concluded that the 2011 charter amendment could not apply to current employees or those who retired after the effective date of the 1996 initiative, which established the supplemental COLA. *Id.* at 627. However, the modification to the supplemental COLA "may be constitutionally applied to employees who retired before the effective date of the 1996 initiative establishing the supplemental COLA." *Id.* at 628. In an earlier case, the court of appeal explained why employees who retire before a supplemental COLA or other benefit is created have no vested contractual right to it:

> The contractual basis of a pension right is the exchange of an employee's services for the pension right offered by statute. A member whose employment terminated before enactment of a statute offering additional benefits does not exchange services for the right to benefits.

Claypool, 4 Cal. App. 4th at 662 (citations omitted) (cited in *Protect Our Benefits*, 235 Cal. App. 4th at 638).

The court in the *Protect Our Benefits* case relied on prior appellate court decisions, which also found modifications to COLA allowances unconstitutional. In *United Firefighters of Los Angeles City v. City of Los Angeles*, 210 Cal. App. 3d 1095 (1989), voters had approved cost of living adjustments for retired city employees in 1966. The adjustments were tied to the Consumer Price Index and were initially capped at two percent. But a 1971 amendment eliminated the cap and allowed the adjustments to fully reflect the amount of inflation each year. *Id.* at 1101. In 1982, voters passed a charter amendment imposing a three percent cap on the cost of living adjustment, and the court of appeal concluded that the 1982 amendment impaired a vested contractual right because it burdened employees with a disadvantage while offering no comparable advantage. *Id.* at 1102-04. The court concluded that once the cap was lifted in 1971, employees had "a reasonable expectation that pension benefits earned thereafter would be fully adjusted for inflation and their post-retirement standards of living thus would be protected from any further diminution." *Id.* at 1108.

Similarly, in *Pasadena Police Officers Association v. City of Pasadena*, 147 Cal. App. 3d 695 (1983) (*Pasadena Police*), the city charter was amended in 1969 to provide for a cost of living adjustment in addition to the basic pension, at a rate equal to the annual percentage change in the Consumer Price Index. *Id.* at 699. In 1981, voters amended the city charter to cap the annual cost of living increase at two percent for certain members, and the appellate court held that the cap impaired a vested right. *Id.* at 701-08.

The court in the *Protect Our Benefits* case adopted the reasoning of the earlier cases, when it explained:

> With respect to current employees, the court [in *Pasadena Police*] found the amendment impaired a vested contractual right that was not offset by a comparable benefit. With respect to employees who had retired before any cost of living allowance went into effect, there was no vested right based on the contract in effect during their employment.

Protect Our Benefits, 235 Cal. App. 4th at 639.

Therefore, the court concluded, Proposition C is an unconstitutional infringement on the vested rights of current employees and employees who retired after the supplemental COLA went into effect. *Id.* at 622. But, the court also concluded, Proposition C may be applied to City employees who retired before the supplemental COLA went into effect in 1996, without violating vested contractual rights because those employees did not provide any consideration, such as performing services, in exchange for receipt of the supplemental COLA. *Id.* at 640.

II. WHILE SAN JOSE'S MEASURE B ELIMINATED THE RESERVE FOR SUPPLEMENTAL BENEFITS, RETIREES ARE BEING ASKED TO SETTLE THEIR LITIGATION BY AGREEING TO A COMPARABLE BENEFIT.

In June 2012, San Jose voters approved Measure B, a charter amendment to modify retirement benefits of city employees and retirees.[2] San Jose's charter provides for two separate retirement systems or plans, administered by two different retirement boards: the 1961 Police and Fire Department Plan, covering sworn employees in the police and fire departments, and the 1975 Federated City Employees Retirement Plan, covering miscellaneous or civilian employees in the San Jose's workforce.

Among other things, Measure B provided authorization for the San Jose City Council to temporarily suspend COLA adjustments for up to five years with a declaration of a fiscal and service level emergency and capped COLA adjustments. Measure B also discontinued San Jose Supplemental Retiree Benefit Reserve (Reserve), and directed that the assets be returned to the appropriate retirement fund. Measure B also prohibited the funding of supplemental payments to retirees from plan assets.

Measure B resulted in multiple lawsuits filed against San Jose, by active and retired employees and three recognized employee organizations, representing police officers, firefighters, and the miscellaneous employees, alleging, among other things, that San Jose violated its meet and confer obligations under the Meyers-Milias-Brown Act in placing Measure B on the ballot and that Measure B infringed upon vested rights. On February20, 2014, a Santa Clara County Superior Court judge issued her Statement of Decision in a consolidated case on the vested rights issues. *See San Jose Police Officers' Ass'n v. City of San Jose*, Superior Court, County of Santa Clara, Case No. 1-12-CV-225926 (*City of San Jose*).

The judge found the provision in Measure B, which authorized the San Jose City Council to suspend and cap COLA adjustments, unlawful and invalid because the evidence at trial established that the COLA is a vested right.

The judge then reviewed the provision which discontinued the Reserve and returned its assets to the appropriate retirement fund. The judge reviewed the legislative history of the two Reserve funds. The Reserve fund for each retirement plan was established as a separate fund for "excess earnings" from superior investment performance. The purpose of the Reserve funds, as established in the San Jose Municipal Code, was to provide a source of funding for supplemental benefits.

The judge found that the terms of the Federated Reserve gave discretion to the San Jose City Council to determine whether distributions should be made at all. From 1986 to 1999, the San Jose City Council did not authorize any distributions, but instead used the Federated Reserve funds to pay for other retirement benefits. From 2000 until 2009, the San Jose City Council authorized distributions, and established a separate Reserve for the Police and Fire plan, which contemplated that there would be circumstances in which distributions would not be made. In 2010, the Reserve distributions ceased and did not resume.

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[2] Information about Measure B can be found on the San Jose website at http://www.sanjoseca.gov/index.aspx?nid=543

The employees and employee organizations challenging elimination of the Reserve funds by Measure B acknowledged that the San Jose City Council had discretion to make no distributions from the Federated Reserve, but the employees and employee organizations argued that there was a vested right to the existence of a segregated reserve, which is not required to be distributed. The trial court judge disagreed because she could find no statutory language supporting this argument. The judge concluded that existence of the Reserve fund was not a vested right for employees or retirees under that plan.

As to the Police and Fire Plan Reserve, the judge recognized that the statutory language was materially different. She found that the Reserve was intended to apply when there was "superior investment performance" by the system and not to a fund with billions in unfunded liabilities. Therefore, the judge found that there was no constitutional impediment to the Measure B provision, which discontinued the Reserve and returned its assets to the appropriate retirement system. It is important to note that Measure B did not prohibit supplemental payments to retirees, it only prohibited payment from plan assets. Impacted employees and retirees have filed a notice of appeal.[3]

The ruling in the *City of San Jose* case is called into question by the recent *Protect Our Benefits* case, discussed above. In that case, the charter amendment in question, which changed the requirements for payment of the supplemental COLA, stated that this was "to clarify the intent of the voters" when they originally enacted the section. This is similar to the trial court's reasoning in the San Jose cases that the benefit was never intended to be paid by an underfunded pension fund. The court in the San Francisco case rejected this reasoning, and held that the charter amendment impaired a vested pension right to the supplemental COLA.

While the appeal is pending, San Jose has reached a tentative agreement with its police and fire unions to resolve the litigation by pursuing an alternative retirement plan. The parties are jointly pursuing a quo warranto writ,[4] which the police union filed and the City is not opposing, to have the Measure B provisions removed from the San Jose Charter and in its place the alternative, negotiated agreement will be implemented. However, this plan will require all parties to be in agreement. This Office understands that the San Jose intends to provide its retired employees impacted by the elimination of the Reserve with a modified benefit, consistent with the holding in *Allen v. Board of Administration*, 34 Cal. 3d 114, 119 (1983).

III. THIS CITY'S 13TH CHECK IS DISTINGUISHABLE FROM THE SUPPLEMENTAL BENEFITS PAID OUT OF THE SAN JOSE RESERVE FUNDS.

Prior to adoption of Measure B, in San Jose, the retirement system boards were to transfer excess earnings to the Reserve funds, when the plans earned more than the assumed rate of return in any given year. It was then up to the San Jose City Council to determine the distribution, if any, from the Reserve funds. The San Jose City Council did not authorize payments from the non-safety, Federated Reserve on a regular basis. From 1986 to 1999, the council didn't authorize any distributions to retirees from the non-safety reserve. From 2000 to

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[3] *See* http://www.sanjoseca.gov/index.aspx?nid=3182.

[4] A quo warranto writ is the means to test the regularly of proceedings by which municipal charter provisions have been adopted. *International Ass'n of Firefighters, Local 55 v. City of Oakland*, 174 Cal. App. 3d 687, 693 (1985).

2009, the council authorized distributions to non-safety retirees, but exercised its discretion to determine the formula for distribution. No retiree had an expectation of receiving any particular amount or any benefit at all.

The benefit for retired safety members was different. The San Jose City Council reserved discretion to approve the methodology for paying the supplemental benefit. However, once the council approved the methodology, the board was required to make distributions in accordance with that methodology. In 2002, the council approved a methodology, and stated that the methodologywould remain in effect until the council approved a subsequent methodology. The council later amended the plan to provide "there shall be no distribution during calendar years 2010, 2011, 2012, or 2013."

In contrast, this City's 13th Check must be paid whenever there are sufficient investment earnings, as determined by an express formula set out in the Municipal Code. Section 24.1503 defines which retirees qualify to receive the benefit, establishes the method for determining when the benefit must be paid, and sets a formula to determine the amount payable to each qualified retiree. The benefit must be paid in any year in which the "investment earnings received" subtracted by the expenses listed in Municipal Code section 24.1502, equal $100,000 or more. In years in which the benefit is paid, it is allocated to eligible retirees according to a mathematical formula. SDMC § 24.1503(b). Neither the SDCERS Board of Administration (Board) nor the San Diego City Council (Council) has any discretion in determining whether the benefit will be paid or the amount of the benefits.

The Council originally established the 13th Check benefit in 1980, by San Diego Ordinance O-15353 (Oct. 6, 1980). The Council requested that SDCERS study the problem faced by retired employees under extreme inflationary factors. San Diego Resolution R-252479 (Aug. 12, 1980). The Council approved a proposal to have SDCERS distribute fifty percent of excess undistributed earnings to retirees under specific conditions. San Diego Ordinance O-15353 (Oct. 6, 1980). The Council characterized the proposal as a change in pension benefits, requiring an amendment to the San Diego Municipal Code and approval of the SDCERS membership pursuant to San Diego Charter section 143.1. *Id.* Under the adopted ordinance, the Board determined the "Surplus Undistributed Earnings," also known as the "Waterfall," and provided for their distribution, with fifty percent being credited to an account to provide funds to pay the annual supplemental benefit or 13th Check to qualified retirees. *Id.* The Council identified the criteria to be applied to determine who was a qualified retiree and the formula to be applied to determine the benefit amount. *Id.* The Council authorized the Board to promulgate rules to effectuate the provisions and intent of the 13th Check ordinance. *Id.*

In October 1981, the Council expanded the 13th Check benefit, by granting it to a previously excluded class of retirees in a special class of safety members. San Diego Ordinance O-15593 (Oct. 5, 1981).

In May 1983, the Board enacted a Board Rule that imposed a cap on the amount of the 13th Check, limiting the payment to $30.00 for each year of creditable service. The Board also created a two percent reserve fund, which further limited the amount that would have otherwise been available for distribution in the 13th Check.

In 1984, a group of retired employees filed a lawsuit, *Darrell J. Andrews et al. v. City of San Diego et al.*, San Diego Superior Court Case No. 515699 (*Andrews*), alleging that the effect of the cap and the reserve was to reduce the amount available for distribution to eligible retirees, and this reduction deprived all similarly situated retirees, who retired on or after October 6, 1980, of vested retirement benefits. The superior court judge certified the lawsuit as a class action. After a trial on the merits, the judge entered judgment for the retired employees and ordered the Board to vacate the cap and the reserve and to pay to the members of the class the amounts by which their supplemental benefits were reduced on account of the implementation of the cap and the reserve, with interest. The court ordered approximately $11.3 million in damages, plus attorney's fees. In lieu of pursuing an appeal, the City settled the litigation with the retired employees, by paying the retired employees $9.7 million plus interest, and fees and costs. The trial court ordered the Board to vacate its Board Rule creating the cap and the reserve fund. *Andrews*, supra, San Diego Superior Court Case No. 515699 (May 8, 1986).

The 13th Check has continued to be paid consistently, following the *Andrews* settlement. However, prior to the *Andrews* settlement, by ordinance in June 1985, the Council adopted a cap on the benefit of $30 per year for each year of creditable service. San Diego Ordinance O-16449 (Jun. 24, 1985). This limitation was implemented following meet and confer negotiations and a vote of the SDCERS members pursuant to San Diego Charter section 143.1, which allows for modifications of future benefits with the approval of a majority of the active members of the SDCERS, who are active employees and not yet retired. *Id.* The cap was associated with additional language providing rules on how the 13th Check funds would be carried over and paid later, in the event the "Surplus Earnings" did not reach a specified amount in a given year.[5] *Id.*

The Council adopted further modifications to the 13th Check benefit following the *Andrews* settlement, and in accordance with it. In June 1986, the Council explained its legislative purpose in the recitals to its ordinance:

> WHEREAS, as part of the settlement of a lawsuit brought against the City and the Retirement Board by retired City employees, and with the recent approval by a vote of the active members of the San Diego City Employees' Retirement System, certain retirees have been awarded increased benefits; and

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[5] Former San Diego Municipal Code section 24.0907.1, provided, in part:

> (a) Surplus Undistributed Earnings shall be comprised of investment earnings received for the previous fiscal year, as defined below, less:
> (5) an amount sufficient to provide necessary funds to pay an annual supplemental benefit to Qualified Retirees, pursuant to the provisions and conditions set forth in section 24.0404. If, at the time of the annual determination, the amount provided for the supplemental benefits is less than $100,000, no supplemental benefits will be paid in that fiscal year and the monies will be placed in a special reserve and be carried forward to ensuing years until such time as the amount to be provided for this benefit from ensuing Surplus Undistributed Earnings and the special reserve is $100,000 or more.

San Diego Ordinance O-16449 (Jun. 24, 1985).

> WHEREAS, the City Council was previously advised of the matter and changes in connection therewith and gave its approval for the settlement; and
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> WHEREAS, the changes were endorsed by the employee organizations; and
>
> WHEREAS, the matter was submitted to a vote of the active members of the Systemand approved by a vote of 2,630-Yes as opposed to 213-No;

San Diego Ordinance O-16679 (Jun. 30, 1986).

The 1986 ordinance lifted the 13th Check cap for General Members who retired between January 8, 1982 and June 30, 1985, to an annual value of not more than $45.00 per year of service. *Id.*

In December 1996, the 13th Check benefit was again increased for certain retirees. The increase was part of a comprehensive proposal to make changes to retiree health benefits, employer contribution rates, retirement plan benefits, and retirement plan reserves. San Diego Ordinance O-18364 (Dec. 2, 1996). Implementation of the proposal was contingent upon passage of a San Diego Charter amendment to authorize the SDCERS Board to administer retiree health benefits, which occurred with voter approval of Proposition D in November 1996. *Id. See also* San Diego Ordinance O-18383 (Feb. 25, 1997).

The Council increased the cap on the annual 13th Check benefit to $60 per year of service for employees who retired on or before October 6, 1980, and $75.00 per year of service who retired on or before December 31, 1971. San Diego Ordinance O-18364 (Dec. 2, 1996). The Council explained that its intent in making the improvements for certainretirees was recognition that the benefit for older retirees had been "severely eroded by years of inflation." *Id.* In its ordinance recitals, the Council explained its intent:

> WHEREAS, it is recommended that for Fiscal Year 1997 only employees who retired on or before October 6, 1980, shall have their Annual Supplemental Benefits (13th Checks) increased from thirtydollars ($30) per year of service to sixtydollars ($60) per year of service; and employees who retired on or before December 31, 1971, shall have their Annual Supplemental Benefits (13th Checks) increased fromthirtydollars ($30) per year of service to seventy-five dollars ($75) per year of service; and
>
> WHEREAS, it is recommended that this benefit improvement to the Annual Supplemental Benefit (13th Check) be increased on a permanent basis if the contingencies are met to implement the total retirement proposal.

Id.

The contingencies referenced in the ordinance recitals were met in November 1996 when voters approved Proposition D, which amended San Diego Charter section 141 to allow SDCERS to provide for health insurance for eligible retirees. *See* General Election Ballot Pamphlet (Nov. 5, 1996). [6]

The 13th Check is presently being paid in accordance with the 1996 modifications to the benefit. However, in 2008, by ordinance, the Council eliminated "the concept of Surplus Earnings" because it was not consistent with sound actuarial principles and because it was being used for certain payments, which were not consistent with federal tax law or state law requirements to assure the competency of the assets of SDCERS. SDMC § 24.1501. *See also* San Diego Ordinance O-19781 (Sept. 11, 2008). In doing so, the Council stated its intent "to ensure that the benefits referenced in the San Diego Municipal Code section 24.1502 be actuarially accounted for as a retirement system liabilityand accordingly be calculated in the City's Annual Required Contribution." *Id.* The Council eliminated the concept of "Surplus Earnings," but affirmed payment of the 13th Check on established conditions. *Id. See also* SDMC §§ 24.1501, 24.1502, 24.1503.

Since September 11, 2008, the 13th Check has been reflected in SDCERS's liabilities and included in the City's annual required contribution. SDMC § 24.1501. In the 35 years since its inception, the 13th Check has been paid in all but three years, when there were insufficient earnings to award the checks under the established formula. SDMC §§ 24.1502, 24.1503. The 13th Check was not paid in 2003, 2009, and 2012.[7] The benefit has been eliminated for employees hired after June 30, 2005. SDMC § 24.1503.1.

Based on this history, as well as recent court decisions, this Office continues to assert, as we did in our 2010 Legal Opinion, that the 13th Check may not be eliminated for active employees or retired employees who were hired or assumed office from October 1980, when the benefit was created, until June 30, 2005, after which the benefit was prospectively eliminated. If the City were to seek to elimination of the 13th Check benefit, it would constitute a breach of the settlement agreement in the *Andrews* case. It would also impair vested contractual rights of employees, who earned the benefit for services provided.

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[6] http://www.sandiego.gov/city-clerk/pdf/pamphlet961105.pdf

[7] *See* https://www.sdcers.org/News.aspx?tagname=13th+Check+and+Corbett&groupid=9

CONCLUSION

It remains this Office's opinion that the 13th Check benefit is vested for employees who were hired or assumed office fromOctober 1980 until June 30, 2005, when the benefit was prospectively eliminated for new hires after that date. This opinion is consistent with recent California appellate court decisions. And, as noted above, it appears that San Josehopes to settle its litigation with its retired employees on elimination of its Reserve by offering them a comparable benefit in exchange, but that will not be paid throughthe Reserve.

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