

**RETIREE HEALTH BENEFITS**  
**FOR MOST MEA-REPRESENTED ACTIVE EMPLOYEES**  
**ARE UNDER ATTACK**

by MEA's Labor Counsel Ann M. Smith

**1. Your Current Eligibility For A City-Paid Retiree Health Benefit Depends On Your Date Of Hire**

- If you were hired **on or after July 25, 2009**, you are covered by a new pension plan which includes a defined contribution Retiree Medical Trust to which you contribute .25% of your salary and the City makes a matching contribution in the same amount.

- If you were hired **on or after February 17, 2007, and before July 25, 2009**, you still have the 2.5% at age 55 pension formula (based on highest one year of final compensation) but you have no City-paid retiree health benefit and you do not participate in any defined contribution Retiree Medical Trust.

- If you were hired **between June 30, 2005, and February 17, 2007**, there is a pending class action lawsuit which will determine whether you have the same retiree health benefit as those hired before July 1, 2005, *or no benefit at all*. The City's position in this lawsuit is that you are not entitled to any retiree health benefit.

- If you were hired **before July 1, 2005**, you currently have a City-paid retiree health benefit but it is under attack. The current benefit is:

- ▶ For a retiree *only*, not his or her dependents.

- ▶ For the plan year 2008-2009 (coverage effective August 1, 2009), if you are **not** Medicare-eligible, the City pays up to a maximum annual benefit of \$8,883.24 (or \$740.27 per month) for the health insurance plan you select from those the City sponsors, or the City will reimburse you up this maximum amount if you procure your own private coverage or have coverage from another source. If you are eligible for Medicare, this annual amount is reduced to \$8,365.92 (or \$697.16 per month) and the City reimburses you for the cost of Medicare Part B.

- The following non-Medicare premiums are in effect for retirees effective August 1, 2009: Health Net HMO: \$635.69/month; Health Net PPO: \$1,067.40/month; Kaiser HMO: \$657.11/month. The following Medicare premiums are in effect for retirees effective August 1, 2009: Health Net Seniority Plus: \$264.40/month; Health Net Flex Med: \$592.15/month; Kaiser Senior Advantage: \$285.01/month.

- ▶ Unless you are awarded a disability retirement, you must have 20 years of Creditable Service to be eligible for 100% of the maximum allowance; you are eligible for 50%

of the maximum allowance with 10 years of Creditable Service; and with more than 10 but fewer than 20 years of Creditable Service, you are eligible for an additional 5% per year – for example, a 75% benefit with 15 years of Creditable Service.

▶ Until July 1, 2009, this maximum allowance was subject to an adjustment, not to exceed 10% per plan year, based on the projected increase in National Health Expenditures by the Centers for Medicare and Medicaid Services, Office of the Actuary. For the two-year period of MEA's MOU, this inflation-based escalator has been "suspended," such that MEA-represented active employees who retire between June 30, 2009, and July 1, 2011, will receive the 2009 maximum annual benefit of \$8,883.24 or \$8,365.92 (or the Member's actual premium, whichever is less).

**2. Whether The Attack On Your Retiree Health Benefit Will End In An Agreement Or In Litigation Depends On The Outcome Of The Process Described In Article 22 Of MEA's Current MOU**

● Article 22 of MEA's current MOU explains what MEA and the City are doing to end the attack on your City-paid retiree health benefits (1) by participating in a Joint Study Committee with a written report due to be issued on or near May 1, 2010, and (2) by reopening negotiations on Retiree Health Benefits no later than July 1, 2010. [See Article 22, subsection 3B, pages 34-37.]

● What happens to your City-paid retiree health benefit after June 30, 2011, will only be known when the meet and confer process concludes in the spring of 2011.

▶ The City and MEA will either reach an agreement on a new MOU, including an agreement on your retiree health benefits or be at an "impasse" and unable to reach agreement by April 1, 2011.

▶ If the parties are at impasse, an "impasse hearing" will take place before the City Council and, with the requisite number of votes, the Mayor's "last, best and final offer" ("LBFO") – including any terms related to retiree health benefits – may be unilaterally imposed on MEA-represented employees over MEA's objections.

☛ If the City has otherwise engaged in good faith bargaining before any impasse occurs, the imposition of such a LBFO will be lawful under the MMBA.

☛ If MEA believes that the City violated its obligations to bargain in good faith before implementing a LBFO, MEA has the option to file an unfair labor practice charge with the Public Employment Relations Board (PERB).

● If MEA believes that any LBFO imposed on MEA-represented employees related to City-paid retiree health benefits constitutes an unconstitutional impairment of individually

vested pension benefits, MEA's Board of Directors will decide whether to authorize litigation challenging the City's LBFO in an effort to undo it and restore the level of retiree health benefits in effect before July 1, 2009 (when the temporary suspension of the inflation escalator took effect), and to seek damages for any retiring employees who were harmed by the unconstitutional impairment in the interim.

**3. Before 1997, There Were Differences In The Retiree Health Benefit Available To Employees Hired Before And After 9/3/82**

Employees Hired Before 9/3/82

- In December 1981, the City asked employees to support a vote out of the Social Security System for "cost avoidance" reasons because the City predicted rising payroll costs associated with participation in Social Security. Among other promises, the City assured worried employees that, if they voted out of Social Security, they would have lifetime City-paid retiree hospital and medical insurance **when they retired** as a form of **supplemental pension benefit under the City Employees' Retirement System** ("CERS"). To implement this promise, Section 24.0907.2 entitled "City-Sponsored Group Health Insurance For Eligible Retirees," was added to the San Diego Municipal Code ("SDMC"), Chapter II, Article 4, "City Employees' Retirement System."

- Both decisions – to ask City employees to support a withdrawal from Social Security and to promise lifetime City-paid retiree medical benefits in exchange – were made under the leadership of former Mayor Pete Wilson.

- ▶ **Funding:** When establishing the "City-Sponsored Group Health Insurance For Eligible Retirees" as a retirement system benefit in 1982, the City also amended another provision of the City's pension plan related to "Surplus Undistributed Earnings," to provide that the annual cost of the retiree premiums "shall be paid by the City" from the portion of the Surplus Undistributed Earnings which would otherwise have been credited to the Employer Contribution Reserve to reduce the unfunded liability of the pension plan.

- This City-paid retiree health benefit was initially available to (1) all employees eligible for general membership in CERS; (2) legislative officers; and (3) those CERS safety members who had been covered by Social Security as of December 31, 1981.

- ▶ Effective July 1, 1985, police officers and firefighters who were on the City's active payroll on or after June 30, 1985, were added to the list of eligible employees.

- ▶ Effective July 1, 1986, a settlement in the class action *Andrews* case expanded the list of retirees eligible for a lifetime City-paid retiree health benefit to include all General Member retirees who retired between October 6, 1980, and January 8, 1982; and all Safety Member retirees who retired between October 6, 1980, and June 30, 1985.

### Employees Hired On And After 9/3/82

- Those employees who were hired **on or after September 3, 1982**, however, took their jobs with the City under a new and inferior “tier II” pension plan called “the 1981 plan.” Under the 1981 plan – in contrast to the original CERS Plan – there was no City-paid retiree health benefit as a supplemental benefit.

- In 1989, MEA succeeded in closing the inferior 1981 pension plan and bringing all MEA-represented employees under the original CERS plan but with an express proviso in the pension plan that they were still not eligible for the City-paid retiree health benefit which had been established during Mayor Wilson’s tenure for those hired before 9/3/82 (and extended to police officers and firefighters effective July 1, 1985).

- In 1992, the first City-paid retiree health benefit was established **under the Retirement System** for employees hired on or after 9/3/82 – though the benefit was inferior to the existing City-paid retiree health benefit for other employees.

- ▶ This new City-paid retiree health benefit involved a “sliding scale” vesting schedule of 5% per year, with 20 years of service needed for the maximum City-paid benefit of *\$2,000 per year* regardless of the actual annual cost of a retiree’s health insurance premium.

- ▶ SDCERS conducted a vote under Charter section 143.1 before the City’s Ordinance amending the retirement system became effective to add this new City-paid retiree health benefit for employees hired on or after 9/3/82.

- ☛ **Funding:** From 1982 through 1992, the City paid the promised retiree health benefits from Surplus Undistributed Earnings in the Retirement System; however, after 1992, the City paid the cost of retiree health benefits directly from its operating funds by using the budget savings generated by the conversion of the SDCERS funding method from “Entry Age Normal” to “Projected Unit Credit,” which had the effect of reducing the City’s annual pension contribution.

#### **4. In 1997, A Single New Category Of “Health Eligible Retirees” Was Established Under The Retirement System With A Uniform Benefit Based On HMO Rates And Restrictions On Plan Design Changes**

- On the recommendation of SDCERS’ fiduciary and tax counsel, the City put a proposed amendment to City Charter section 141 on the ballot in November 1996 as Proposition D to get voter approval for the City Council to provide retiree health benefits through the Retirement System rather than to pay these benefits to retired City employees directly from the City’s operating funds. The measure passed and the Charter was amended accordingly.

▶ Apparently, the City's use of SDCERS trust fund assets to pay for retiree health benefits from 1982 through 1992 had been done without Charter authorization.

● With the passage of Proposition D, the City established a new category of "Health Eligible Retirees" with a uniform "Post Retirement Health Benefit." All active employees, regardless of their date of hire, and all retirees who had been on the City's active payroll on or after October 5, 1980, and who retired on or after October 6, 1980, were covered by the same uniform City-paid lifetime retiree health benefit except as noted below.

▶ For those Health Eligible Retirees who enrolled in any health insurance plan, the City agreed to pay or to reimburse the applicable Medicare-eligible or non-Medicare eligible retiree-only premium up to, but no more than, the cost of the retiree-only premium for the highest cost HMO plan which was also a City-sponsored health insurance plan made available to Health Eligible Retirees.

▶ Exception: For those Health Eligible Retirees who on January 1, 1997, were enrolled in and remained continuously enrolled in any PPO plan, the City agreed to pay or to reimburse the applicable Medicare-eligible or non-Medicare eligible retiree-only premium up to, but no more than, the cost of the retiree-only premium for the highest cost PPO plan which was also a City-sponsored health insurance plan made available to Health Eligible Retirees.

▶ The City established the single new category of "Health Eligible Retiree" and the uniform HMO- based retiree health benefit after meeting and conferring and reaching agreement with its four labor organizations.

▶ Certain bargained-for guarantees accompanied the City's establishment of the single category of "Health Eligible Retiree" and the uniform "Post Retirement Health Benefit" to assure that the City could not lawfully diminish the value of the HMO-based Post Retirement Health Benefit. By a unanimous vote of the Mayor and City Council, Ordinance O-18392 was adopted on March 31, 1997, with the following terms:

☛ "WHEREAS, it is the intent of the agreement reached between the four labor organizations and the City Management Team that the level of health benefits to be provided by the Retirement System not be diminished by any change in HMO health care providers by the City, or any new or amended contract with an HMO health care provider or by conversion to a blended premium for active employees and retirees without mutual agreement with the exclusive bargaining representatives; and,

☛ WHEREAS, the four labor organizations and the City Management Team have agreed that any change will not be approved by the City Council until after the proposed changes has been reviewed by a qualified independent consultant, who is mutually selected and jointly compensated by the City and the recognized labor organizations, who concludes that the proposed changes will not affect the benefit in any manner which triggers the

voting rights of active employees (under City Charter section 143.1), unless this process is waived by mutual consent; . . .”

► Funding: Having procured voter approval for the Council to arrange for payment of Retiree Health Benefits from the pension fund, the City expressly represented by a unanimous vote of Mayor and City Council on March 31, 1997:

☛ that it “wishes to ensure that retirees are provided with appropriate health benefits;”

☛ that “the best way to provide these benefits is through the Retirement System using the undistributed earnings of the System,” by means of a 401(h) trust and a “bifurcated rate program” permitted by the IRS; and,

☛ that “the City and the (SDCERS) Board have agreed that the bifurcated rate arrangement is to be used for a ‘pay as you go’ health program and that this program will not be fully actuarially funded.”

**5. In 2002, After Disputes Had Erupted Over HMO Plan Design Changes, The City Agreed to Establish A Fixed PPO-Based Benefit With An Escalator And Cap**

● Having agreed in 1997 that the HMO-based retiree health benefit for all Health Eligible Retirees would not be diminished in value by unilateral changes in plan design, the City began implementing plan design changes in the City-sponsored HMO plans being offered to retirees. Since the dollar value of the Retiree Health Benefit for most retirees was tied to the highest cost City-sponsored HMO plan, the City was motivated to keep the cost down by increasing deductibles and co-pays and making other plan design changes which reduced the economic value of the benefit when compared with the quality of the HMO coverage available for plan year 1997. The City’s labor organizations repeatedly challenged these changes.

● In 2002, the City and the same coalition of labor organizations which had negotiated the establishment of a uniform HMO-based Retiree Health Benefit in 1997, agreed on a means to eliminate these recurring disputes over HMO plan design changes.

● This agreement replaced the uniform HMO-based Retiree Health Benefit with a fixed dollar benefit based on the cost of the City-sponsored **PPO plan** being offered to retirees for the 2003 plan year, with an automatic annual increase in this amount, not to exceed 10% per year, based on an independent, objective source which is the Centers for Medicare and Medicaid Services, Office of the Actuary, which tracks projected increases in National Health Expenditures. By converting the Retiree Health Benefit to a fixed dollar value with an independent basis for making annual adjustments, disputes over plan design changes ended.

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- For the 2003 plan year, the monthly PPO-based rates were \$489.16 for Non-Medicare eligible retirees, and \$460.67 for Medicare eligible retirees.

- By application of the annual escalator with the 10% cap, these monthly amounts had grown, respectively, to \$740.27 and \$697.16 per month for plan year 2009.

**6. The Obligation To Pay For Retiree Health Benefits Has Always Been The City's From 1982 To The Present**

- From 1982, when a City-paid lifetime retiree health benefit was first established for City employees under Mayor Wilson's leadership, through the present, the obligation to pay for the Retiree Health Benefit as a supplemental pension benefit has always been the City's and the City's alone – whether the benefit was paid from Surplus Undistributed Earnings in the pension system or directly from the City's operating funds.

- Every ordinance amending the retirement system related to the establishment of retiree health benefits since 1982 has confirmed that the City is the ultimate obligor on this debt.

- When the balance in the SDCERS 401(h) health care trust account was exhausted in mid-January 2005, the City decided to support the recommendation of the Pension Reform Committee that retiree health care costs no longer be funded in a manner that reduces assets of the retirement fund.

- ▶ Consistent with its decades-old obligation to pay for this benefit “from any source of funds available to The City of San Diego,” the City has paid this obligation from General Fund and Non-General Fund revenues since the middle of the 2005 fiscal year and continuing to the present.

**7. Retiree Health Benefits Are A Supplemental, Vested Pension Benefit Not An Employment Benefit**

- Since 1982 when a City-paid lifetime retiree health benefit was established in exchange for employees' favorable vote out of the Social Security system, this benefit has always been a supplemental pension benefit under the retirement system.

- After 1982, as more employees became eligible for a Retiree Health Benefit, the essential character of this benefit remained the same in assuring an employee that he or she was earning the right to have City-paid health insurance upon retirement at the same time as he or she was earning a pension allowance. This supplemental pension benefit only becomes available when *an employee achieves the status of a retiree receiving a pension allowance from SDCERS*.

- Since 1982, any bargained-for improvements in this benefit have not been confined to MOUs with a set term and expiration date; instead, each improvement has been

codified in Chapter II, Article 4, “City Employees Retirement System” of the San Diego Municipal Code along with all other vested pension benefits.

- Because the City agreed that the Retiree Health Benefit *is* a Retirement System Benefit and *not* an employment benefit, the City amended Article 4, “City Employees Retirement System” of the San Diego Municipal Code on January 17, 2007 (following passage of the Proposition B ballot measure) to add Division 19 entitled “Voter Approval of Retirement System Benefit Increases.” Section 24.1902 defines an “increase” in Retirement System Benefits to include **“a change in retiree health benefits.”**

- Because of the nature of the Retiree Health Benefit as a supplemental pension benefit under the retirement system, whenever the City Council has adopted an Ordinance amending the retirement system to affect the Retiree Health Benefit, SDCERS conducted a vote as required by City Charter section 143.1 to get the approval of plan participants before the amendment became law.

### **What’s The Difference?**

- The essential difference between an “employment benefit” and a “vested pension benefit” is that employment benefits remain in effect during the term of an MOU or similar labor agreement, expire when the MOU ends, and become subject to re-negotiation.

- Examples of “employment benefits” include wages and the flexible benefits plan dollar value. These are subject to re-negotiation whenever an MOU expires; there are no guarantees that, upon re-negotiation, wages or the flexible benefits plan dollar value will improve – or even that these “employment benefits” will remain the same.

- However, although MEA has succeeded in improving pension benefits over the years through the collective bargaining process, these benefits are not merely another term of an MOU subject to change when the MOU expires.

- ▶ Once a pension benefit – including a supplemental pension benefit like the Retiree Health Benefit – is initially established or improved during your employment, it has a protected legal life which does not begin and end with each MOU because its legal character as a vested pension benefit becomes separately established.

- ☛ Pension benefits become part of the City’s statutory law by means of ordinances amending the retirement system which take effect if approved by plan participants under Charter section 143.1.

- ☛ Once enacted, these benefits are individually vested and protected by the State and Federal Constitutions as a form of deferred compensation for an employee’s services. The concept of “deferred compensation” essentially means that each payday the City



gives an employee (1) a paycheck for the services rendered during that pay period, and (2) an “IOU” for the pension benefits *being earned* for those services but not yet payable until the eligibility requirements are satisfied and the employee retires. As a supplemental pension benefit, the Retiree Health Benefit is in this category.

☛ Once “vested,” these benefits cannot be bargained away or changed unilaterally by the City even when the MOU expires.

- *Before retirement*, “vested” pension benefits *can* lawfully be changed under limited circumstances. An employee’s vested contractual pension rights may be modified prior to retirement for the purpose of keeping the pension system flexible to permit adjustments in accord with changing conditions and at the same time to maintain the integrity of the system.

- ▶ Any modification must be reasonable based upon the facts of each case.

- ▶ To be sustained as “reasonable” by California’s courts, alterations in employees’ pension rights must bear some material relation to the theory of the pension system and its successful operation, and changes in a pension plan which result in disadvantage to employees should be accompanied by comparable new advantages, whether in the form of additional benefits or greater funding security.

- ▶ Charter section 143.1 also protects an employee’s right to vote on proposed amendments to the retirement system which affect his or her benefits under the system – including the Retiree Health Benefit. The right to vote is itself a vested benefit.

- *After retirement*, pension benefits are *absolutely* vested and may not be changed or diminished. The Retiree Health Benefit for *retirees* may not lawfully be eliminated or detrimentally modified.

- In addition to the constitutional protections which “vested” pension benefits enjoy, employees who were on the City’s payroll when the vote to withdraw from Social Security occurred in December 1981, have an enforceable promise against the City for lifetime City-paid retiree health benefits.

## **8. The City Attorney Has Advised The City That The Retiree Health Benefit For Active Employees Is An Employment Benefit**

- Without waiting for the Joint Study Committee to complete its work and issue a report as described in Article 22 of MEA’s MOU – which will include a comprehensive history and legal analysis – the City Attorney unilaterally published his opinion in the matter on January 21, 2010.

- The City Attorney concedes that a court would find the Retiree Health Benefit

**vested for retirees** on the terms in effect when they retired.

- ▶ This concession is appropriate because the Retiree Health Benefit for retirees is *absolutely vested* as noted above.

- But, as to active employees, the City Attorney has concluded that the *same* Retiree Health benefit is an employment benefit which is not vested and which may be modified through the collective bargaining process.

- ▶ *Translation:* The Mayor and City Council can impose a change that reduces or eliminates the Retiree Health Benefit if MEA and the City do not reach agreement during the collective bargaining process.

- ▶ In attempting to distinguish retirees from active employees, the City Attorney makes an illogical comparison: *retirees* relied on “representations and promises made by the City,” he says, *but active employees allegedly did not*.

- The City Attorney “reasons” that, because modifications to the Retiree Health Benefit have been achieved through the collective bargaining process, this benefit is “more properly characterized as an employment benefit that may be modified through negotiations.”

- ▶ This argument is irrational because *all* pension benefit improvements for represented City employees have been achieved through the collective bargaining process and this fact does not transform them, once established in the City’s statutory law, from “vested pension benefits” into “employment benefits.”

- The City Attorney has also concluded that, in contrast to each other occasion over the decades, any change or reduction in the Retiree Health Benefit would *not* be subject to a vote of employees under Charter section 143.1 “because the benefit is not presently under the retirement system,” since the City Council adopted an Ordinance in April 2008, deleting the 401(h) retiree health benefit trust from the pension plan, and providing that the City would pay for the benefit directly from any source available to it.

- ▶ This argument is nonsensical because the Retiree Health Benefit has been codified as a retirement system benefit since 1982 and it remains codified in Division 12 of Article 4, “City Employees’ Retirement System.” It is – and has always been – a supplemental pension benefit for an eligible *retiree* under SDCERS.

- ▶ Since 1982, the City has always borne the ultimate obligation to fund Retiree Health Benefits, and the City paid directly for the cost of Retiree Health Benefits – without using retirement system assets – for the period 1992 through 1997, and has done so continuously since January 2005.

► When the City has changed the method of funding the Retiree Health Benefits, employees have not voted under Charter section 143.1 because the funding mechanism has never changed the character of the benefit as a vested supplemental pension benefit.

In short, I believe that the City Attorney's opinion that the Retiree Health Benefit is an "employment benefit" rather than a vested supplemental pension benefit is wrong.

As will be more fully developed in the Joint Study Committee's Report when issued in early May, the City Attorney's legal analysis is unsupportable because it is built on a heavily flawed foundation. His review of the history of the Retiree Health Benefit is incomplete, omits critical facts, and/or misinterprets events due to a lack of personal knowledge or participation by any member of the City Attorney's Office producing the "opinion. His opinion quotes from legislative enactments or other documents on a selective and "misleading" basis.

Thus, the battle lines are taking shape.

## **9. What Do You Need To Do?**

- Stay informed by paying attention to communications from MEA on this important issue.
- Participate when you are called upon by your elected leadership.
- Keep your Union strong so that you have an effective advocate in this fight.
- As always, continue to do your best work for the residents of San Diego despite declining resources and continued attacks on your promised benefits.