



Agenda Item No. (10)(A)  
**Special Order of Business**

To: Board of Directors  
Meeting of January 28, 2022

From: Joseph M. Wire, Auditor-Controller  
Denis J. Mulligan, General Manager

Subject: **INFORMATIONAL REPORT ON 2020 CALIFORNIA SUPREME COURT  
RULING ON “VESTED RIGHTS” UNDER PENSION PLANS**

**Recommendation**

This report on the July 30, 2020 California Supreme Court’s ruling in the *ACERA* case regarding the “California vested rights rule” with respect to pension benefits is provided for informational purposes only and does not require any action.

**Summary**

This report provides follow-up information responding to discussion by the Board of Agenda Item No. (10)(D) Special Order of Business, at the Board Meeting of November 19, 2021, “Informational Report on Pension Plans Covering District Employees”<sup>1</sup> regarding the four pension plans covering District employees, and, in particular, the ATU pension plan (“ATU Plan”), as well as Agenda Item No. 10(A) Special Order of Business, at the Board Meeting of December 17, 2021, “Informational Report on Amalgamated Transit Union (“ATU”) Pension Plan’s Actuarially Determined Contribution Shortfall.”<sup>2</sup> As discussed in those prior agenda items, under *ACERA* certain benefit features in the ATU Plan that are not found in the District’s other pension plans, and thatacerbate the ATU Plan’s underfunding, could be changed by the ATU Plan’s Board of Trustees for current employees on the basis that such modifications “bear some material relation to the theory of a pension system and its successful operation.” (See *Alameda Cty. Deputy Sheriff’s Ass’n v. Alameda Cty. Employees’ Ret. Ass’n (“ACERA”)*, 9 Cal. 5th 1032 (2020).)

**ACERA Decision**

The *ACERA* case involved a challenge to the constitutionality of changes made by the Public Employee Pension Reform Act (“PEPRA”) as it applied to employees covered by a county retirement system under the County Employees’ Retirement Law (the “CERL”). (See *ACERA*, 9

<sup>1</sup> Available at: [2021-1119-boardmeeting-no10d-informationalrepregardpensplans.pdf \(goldengate.org\)](https://www.goldengate.org/assets/1/25/2021-1217-boardmeeting-no10a-infoatucdcshtfallfundrev.pdf?7601).

<sup>2</sup> Available at: <https://www.goldengate.org/assets/1/25/2021-1217-boardmeeting-no10a-infoatucdcshtfallfundrev.pdf?7601>

Cal. 5th 1032.) Under PEPRA, certain items of pay were no longer included in the definition of “compensation” used to determine county employees’ retirement benefits – both for employees hired before and after PEPRA’s effective date. (*Id.* at 1059-60.) The lawsuit challenged application of the new definition to employees hired prior to the effective date of PEPRA, who argued that they were entitled to pension benefits provided by the retirement system rules that were in effect when they were hired, under the “California vested rights” rule. (*Id.* at 1063.) The “vested rights” rule is based on the contract clause of the California state Constitution, which prohibits the legislative “impairment” of contracts, including employment contracts. (*Id.* at 1074-75.) Generally, the “vested rights” rule has been invoked in cases involving pension plan reductions for current employees who claim that a “comparable advantage” should be provided to offset any reduction. (*Id.* at 1077-81.)

The *ACERA* case clarified the legal landscape. The California Supreme Court articulated a three step framework for courts to analyze the constitutionality of pension changes. First, a court must assess whether the modification “impose[s] an economic disadvantage on affected employees,” relative to the preexisting pension plan and, if so, whether the disadvantage was “offset in some manner by comparable new advantages.” (*Id.* at 1082.) Next, assuming a disadvantage is found that was not offset, a court must determine whether the government’s articulated purpose for the change is “sufficient, for constitutional purposes, to justify any impairment.” (*Id.*) A change is constitutional where it “bear[s] some material relation to the theory of a pension system and its successful operation.” (*Id.*) Assuming the change was made for a permissible purpose, it will be upheld “if providing comparable advantages would undermine, or would otherwise be inconsistent with, the modification’s constitutionally permissible purpose.” (*Id.* at 1093.)

The Court in *ACERA* held that changes made under PEPRA to close loopholes and end abusive practices under the retirement system, including pension “spiking”, were for a permissible purpose, and that providing a comparable advantage would undermine that purpose. The Court also held that changes made under PEPRA that were intended to maintain the retirement system’s financial integrity and discourage manipulation in the management of pension benefits were made for a proper reason. Accordingly, the Court upheld the changes made by PEPRA to the definition of “compensation” used to determine retirement benefits under the CERL for employees hired prior to the effective date of PEPRA.

The *ACERA* decision provides some clarity with regard to the type of changes a pension plan might make to maintain its viability, which is most certainly a permissible purpose. For example, the recent adoption of new service credit rules applicable to current employees by the ATU Plan’s Board of Trustees is consistent with the vested rights rule, as applied by the Court in *ACERA*, as are other potential measures that have been discussed with this Board in November and December, 2021, such as increasing the early retirement age and reducing benefits to account for early retirement, and eliminating the subsidized spousal benefit. Thus, in summary, additional changes to the ATU Plan affecting benefits for current employees would be subject to the *ACERA* test, meaning benefit changes for a permissible purpose would not need to include a comparable advantage, if doing so would undermine, or be inconsistent with, the permissible purpose of the change.