



OFFICE OF THE COUNTY ATTORNEY

Isiah Leggett
County Executive

Leon Rodriguez
County Attorney

MEMORANDUM

TO: Michael J. Knapp, President
County Council

FROM: Edward B. Lattner *EBL*
Chief, Division of Human Resources & Appeals

DATE: May 13, 2008

RE: **Proposed Response to May 9, 2008, IAFF Local 1664 Letter Regarding Retiree Health Care Premiums**

You requested that this office respond to the enclosed May 9, 2008, letter from IAFF Local 1664 President John J. Sparks regarding retiree health care premiums.

The IAFF asserts that, if the County Council increases the health insurance premiums currently paid by retired County firefighters, that will amount to a “breach of contract” and a violation of the U.S. Constitution’s Contract Clause because § 33-34 of the County’s retirement law prohibits the County from reducing the overall value of retirement benefits unless necessary to maintain the fiscal integrity of the retirement system. The IAFF has misinterpreted the County law. The “benefits” referred to in § 33-34 are retirement benefits, not health benefits. Therefore, § 33-34 does not constitute a contractual obligation owed to retirees regarding retiree health benefits.

As an initial matter, § 33-34 is a self-described “declaration of policy” and, as such, is not binding on the Council. A “declaration of policy” section that is included in the codification of a statute is considered a “preamble” to the statute; the “declaration of policy” is not part of the operative, binding provisions of the statute. *Dillon v. State*, 277 Md. 571, 573-74, 582-83 (1976); *Battle v. State*, 65 Md. App. 38, 47 (1985), *cert. denied*, 305 Md. 243 (1986). The same principle applies to the construction of county ordinances. *Clarke v. County Commissioners*, 270 Md. 343, 345, 349 (1973). Statements of legislative purpose included in a county law are not considered part of the “operative portions” of the law. *Lone v. Montgomery County*, 85 Md. App. 477, 502-03 (1991).

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Even if § 33-34's "declaration of policy" could be construed to be a substantive provision of law, the "benefits" it refers to are income-related pension benefits, not health benefits. Section 33-34 provides:

It is the policy of the county to maintain a system of retirement pay and benefits for its employees which is adequately funded and insures employees sufficient income to enjoy during their retirement years. Any modifications to such retirement system shall not reduce the overall value of benefits which existed for members immediately prior to such modifications except that benefits may be reduced if necessary to maintain the fiscal integrity of the system after a finding by the county council that such change is necessary.

Before all liabilities with respect to the members and their beneficiaries are satisfied, no person may use or divert any part of the corpus or income of the retirement system to purposes other than the exclusive benefit of the members and beneficiaries.

Section 33-34 serves as the introduction to Article III of Chapter 33, entitled "Employees' Retirement System." Article III does not address, in any way, health benefits, either for active employees or retirees. To be sure, other provisions in Article III do address "benefits," but those are income-related pension benefits such as disability retirement benefits, death benefits, and even deferred retirement option plan (DROP) benefits.

Section 33-34 specifically addresses income-related pension benefits, not health benefits. This section expresses the County's policy of maintaining a system of retirement pay and benefits "which is adequately funded [to ensure] employees sufficient income to enjoy during their retirement years." Thus, the "benefits" referred to in § 33-34 are the benefits of a retirement system with sufficient funds to provide income for employees to enjoy during their retirement.

This section also expresses the County's policy precluding the diversion of any part of the corpus or income of the retirement system to purposes other than the exclusive benefit of the members of the retirement system. The corpus or income of the Employee Retirement System is the ERS Trust Fund overseen by the Board of Investment Trustees. Health benefits have never been a part of the ERS Trust Fund.

To the extent § 33-34 can be interpreted as a contract, its terms do not encompass health care benefits. The cases cited by the IAFF are inapposite because, unlike the situation here, each dealt with a public employee's attempt to obtain benefits under a statute after the public employer unilaterally modified the terms of that statute. The courts in those cases concluded that those statutes amounted to legislatively created "contracts," limiting the public employer's ability to modify their terms.

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Section 33-34 does not offer employees the promise or inducement of health benefits, either for active employees or retirees. Accordingly, § 33-34 does not constrain the Council's authority in funding retiree health benefits.

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Enclosure

cc: Joseph Adler, Director, OHR (w/ enclosure)
Sarah Miller, Labor Relations Manager, OHR (w/ enclosure)
Leon Rodriguez, County Attorney (w/ enclosure)
Marc P. Hansen, Deputy County Attorney (w/ enclosure)
Michael E. Faden, Senior Legislative Attorney (w/ enclosure)

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LOCAL 1664

Montgomery County Career Fire Fighters Ass'n., Inc.

May 9, 2008

Duchy Trachtenberg, Chair
Management and Fiscal Policy Committee
Montgomery County Council
100 Maryland Avenue
Rockville, MD 20850

Dear Ms. Trachtenberg,

This letter responds to the County Executive's proposal to increase the amount that Montgomery County retirees must pay for their health care benefits. The County Executive's proposal not only breaches the contract between retirees and the County, but violates Article I, Section § 10, C1, I of the United States Constitution. Therefore, the Union requests that the County Council not adopt the proposed changes.

The Montgomery County Code provides in relevant part:

It is the policy of the county to maintain a system of retirement pay and benefits for its employees which is adequately funded and insures employees sufficient income to enjoy during their retirement years. Any modifications to such retirement system shall not reduce the overall value of benefits which existed for members immediately prior to such modifications except that benefits may be reduced if necessary to maintain the fiscal integrity of the system after a finding by the county council that such change is necessary.

Before all liabilities with respect to the members and their beneficiaries are satisfied, no person may use or divert any part of the corpus or income of the retirement system to purposes other than exclusive benefit of the members and beneficiaries.

Montgomery County Code § 33-34. This language created a contract between employees and the County that, when they retired, employees would enjoy certain benefits, including health care benefits as they were offered when they retired. See, e.g., *United States Trust Company of New York v. New Jersey*, 431 U.S. 1 (1977); *Frederick v. Quinn*, 35 Md. App. 626, 629 (1977) (“[W]e agree that a pension is more contractual than gratuitous. ... It is reasonable to assume ... that appellees were induced, at least in part, to their employment by the pension benefits held out at the time, just as they were induced by the salary then offered.”); *Davis v. Mayor & Alderman of the city of Annapolis*, 98 Md. App. 707 (1994) (“Maryland has clearly placed itself in the

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majority view – pension benefits are contractual [.]”). Because the employees impacted that contract cannot be modified except under limited circumstances.

The County agreed not to reduce benefits absent a showing that the reduction is “necessary to maintain the fiscal integrity of the system.” § 33-34. Such a finding cannot be made here. Presumably, the proposed increase is tied to changes to governmental accounting standards, which require the County to disclose its entire liability for retiree benefits, rather than its annual liability for retirement benefits. According to media reports, this increased liability has threatened the County’s AAA bond rating. The changed reporting requirements, however, do *not* change the County’s actual liability for retirement benefits. As a result, the reduced benefits (through increased premium shares paid by retirees) are not necessary to maintain the retirement system’s fiscal integrity.

Further, the change violates the Contract Clause of the United States Constitution. It is well-settled law that, although the Contract Clause does not work an absolute prohibition on the rights of States to impair contractual limitations, a governmental entity’s right to do so is limited to *proper* exercises of its police powers. *Andrews v. Anne Arundel County*, 931 F.Supp. 1255, 1259-60 (D.MD. 1996), *aff’d*, 114F.2d 1175 (4th Cir. 1997), *cert. denied*, 522 U.S. 1015 (1997). In cases, as here, where a contract exists, the courts will find a Contract Clause violation if the change was substantial and the legislation adjusting the contractual rights was not based upon reasonable conditions and necessary. *Id.* At 1260.

The proposed change is substantial. Retirees rely on the stability of their health insurance premiums. In *Andrews*, the court noted: “The diminution of pension benefits is more likely than not an even more substantial impairment than a diminution of annual salary because the individual receiving pension benefits is typically already living on a reduced income as compared to her pre-retirement savings. Thus, a decrease in benefits would potentially have a greater impact.” *Id.* At 1265. The court’s rationale is equally applicable here, where the County Executive proposes to charge retirees more for health care benefits, thus reducing the value of their retirement pay and benefits.

Likewise, the proposed adjustments are not based on reasonable conditions, nor are they necessary. Typically, courts require a government to demonstrate that the means it has adopted to address its “problem” are the least drastic available. *Andrews*, 931 F.Supp. at 1266 (*citing* *U.S. Trust Co.*, 431 U.S. at 31). The County has offered no explanation as to how increasing retiree health care benefit costs would address the “problem” created by changed government accounting standards, and certainly made no showing that increasing retiree health care benefit costs is the only way to address those alleged problems.

Further, Maryland courts generally require a government that *does* unilaterally modify pension benefits to show that the changes either do not adversely alter the benefits, or that adversely altered benefits have been replaced with comparable benefits. *Davis*, 98 Md. App. at 715. No such showing has been made here, nor can one be made. The County Executive’s proposal

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simply reduces the value of the retirees' retirement benefits by charging them more for health care benefits.

The County Executive's proposal both breaches the terms of the contract between the County and retirees, and violates the United States Constitution. Further, it is unfair to retirees who faithfully served the County and retired with the expectation that their health insurance benefits would be funded in a specific manner. These changes may result in a substantial increase in health care benefit costs to certain retirees, for which they could not plan and which will result in a substantial *decrease* in the value of their retirement pay and benefits.

The Union respectfully requests that the County Council not act upon the proposal, and leave retirees' health care benefits and costs unchanged.

Best regards,



John J. Sparks
President

cc: Valerie Ervin, MFP Committee
Phil Andrews, MFP Committee
Megan K. Mechak, Woodley & McGillivray
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