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March 12, 1980

Honorable Ralph M. Lovell
Maine Senate
State House
Augusta, Maine 04333

Honorable Merle Nelson
House of Representatives
State House
Augusta, Maine 04333

Dear Senator Lovell and Representative Nelson:

You have asked for an opinion from this office regarding certain aspects of L.D. 1787, whose purpose is to permit the Bingham Water District (hereinafter "District") to withdraw as a participating local district in the Maine State Retirement System (hereinafter "System"). Your questions deal with a troublesome provision of L.D. 1787 which essentially provides that employees of the District must withdraw their contributions within one year of the effective date of the District's withdrawal from the System or lose that money. After one year, L.D. 1787 provides that all monies then on deposit with the System resulting from contributions by the District will be returned to the District. It appears that, after this period, L.D. 1787 effectively terminates the District's pension plan as to all present members and retirees.

Your questions essentially ask whether the Legislature can properly act to allow a participating local district of the System to withdraw from the System and cut off its retirement plan in toto by divesting the employees and retirees of the District of their interest in the System by refunding to them their contributions, as provided for in L.D. 1787. While this question has not been addressed in Maine and is therefore not free from doubt, we conclude that the answer is in the negative. The Legislature should be aware, however, of the narrow conclusion reached in this opinion. We do not reach, and therefore take no

position regarding, the power of the Legislature to make changes in the benefit structure of the State Retirement System as it relates to state employees or employees of local districts. The conclusions reached herein apply only to the issue of whether a participating local district in the Maine State Retirement System may withdraw from the System by wholly eliminating its pension plan both as to present retirees and as to current employees.

We deem your first two questions to address the issue of the existence of a right in current retirees and employees in pension benefits or the expectation of such benefits. Clearly, if there is no such right in either group, or if such a right is merely statutory in nature, then the Legislature may enact legislation allowing local districts to withdraw from the System without protecting these groups. If, on the other hand, such rights are of constitutional stature, the Legislature may not authorize withdrawal under circumstances in which these rights are violated.

We believe that both current employees and retirees of a given local district of the Retirement System have rights of constitutional stature in the pension plan of which they are members. While we do not here determine the extent of these rights, we find their source in the contractual nature of the Retirement System arrangement, and in view of pensions as deferred compensation. See generally ANNOT., "Vested Rights of Pensioners to Pension," 5 A.L.R.2d 437 (1957).

Historically, pensions have been viewed as gratuities granted by the employer as a recognition of the long-term service of its employees. E.g., Pennie v. Reis, 122 U.S. 464 (1889); see generally 90 Harv. L. Rev. 992 (1977). Under such a view, there was no "right" to a pension, and it could therefore be granted or withdrawn at an employer's whim. Id. Gradually, however, the courts have replaced the "gratuity" view with the theory that pensions constituted deferred compensation for services rendered. See, e.g., Betts v. Board of Administration, Public Employees' Retirement System, 582 P.2d 614 (Cal. 1978); Kern v. City of Long Beach, 179 P.2d 799 (Cal. 1947); see generally discussion in City of Frederick v. Quinn, 371 A.2d 724, 725-27 (Md. Ct. of Spec. App. 1977). Such compensation has therefore been viewed as contractually based and has been held, in a number of jurisdictions, to be protected by the clause in the state constitution barring impairment of the obligation of contract. E.g., Campbell v. Michigan Judges Retirement Board, 143 N.W.2d 755 (Mich. 1966); see also Yeazell v. Copins, 402 P.2f 41 (Ariz. 1965) (pension right based on constitutional provision barring gifts of public funds); see Me. Const., art. I, § 11. While many jurisdictions still retain the "gratuity" view, see, e.g. City of Greenwood v.

Smith, 361 N.E.2d 168 (Ind. App. 1977), it is clear that the trend is towards the "contract" theory.[1/] See City of Frederick v. Quinn, supra at 726; see generally ANNOT, supra at 441.

The legislative history of the Maine State Retirement System supports the conclusion that the Legislature considered pension rights under that System to be contractual in nature and rejected the idea that pensions were merely a moral obligation. See Opinion of the Attorney General, September 26, 1979. Thus,

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1/ In a few jurisdictions, the courts have reached something of a middle ground between the seemingly inflexible end points of "gratuity" and "contract." In an effort to avoid locking in the State or municipalities to a specific level of pension benefits or a set benefit structure, these courts, while generally recognizing a "right" in a pension expectancy, have discarded the strict contract theory in favor of the view that such a right exists, and is, in general, a property right, but that a further characterization of the right is of little legal significance. See, e.g., City of Frederick v. Quinn, supra at 827 ("pension is more contractual than gratuitous" but pension plan subject to reasonable modification); Opinion of the Justices, 303 N.E.2d 320, 328 (Mass. 1973) (contract based on expectations of employees and subject to reasonable changes which do not interfere with "core expectations"); see also Stuart v. Flynn, 380 F. Supp. 424 (W.D. Pa. 1974) (property right). Perhaps the most cogently reasoned of these "middle ground" cases is Spina v. Consolidated Police and Fireman's Pension Fund, 197 A.2d 169 (N.J. 1964), which takes the position that to characterize a public employee's right to a pension proves too much.

> In these circumstances, it seems idle to sum up either the public's or the employee's contribution in one crisp word. We have no doubt that pension benefits are not a gratuity. . . [citation omitted]. And we think the employee has a property interest in an existing fund which the State could not simply confiscate. [Emphasis added.]
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> 197 A.2d at 175.

Finally, some jurisdictions recognizing a contract right nevertheless attempt to secure some flexibility for pension plans by barring changes disadvantageous to employees without offsetting new advantages, see Betts, supra, or providing for changes which relate to the fiscal integrity of the System in the long run. Quinn, supra. The impact of these cases upon the reasoning in this opinion is, however, minimal, since we deal with the very narrow situation in which a pension plan is entirely cut off both as to current members and retirees. The recognition of a constitutional right in such a system, whatever the characterization of that right, would seem, in our view, to bar the complete elimination of the plan.

although the Supreme Judicial Court has not ruled on the issue, we think it likely that that Court would embrace some theory under which retirees and members would have constitutionally cognizable rights in their pension system. Again, however, we hesitate to speculate as to the exact nature and extent of such rights which might be recognized by the Court.

Under the "contract" theory, the question arises as to the time at which a right of constitutional stature attaches. A number of answers has been proposed by the various courts which have addressed the issue. See generally ANNO, supra, § 2[c]. A right to a pension vests under the Retirement System statute after 10 years of service. See 5 M.R.S.A. § 1121(1)(A)(4).2/ We do not, however, see this as the time which would be viewed by a court as establishing a recognizable right in a pension plan or system. While views have varied, as noted above, it seems clear that the expectational interest upon which a constitutional right is founded, see Opinion of the Justices, supra, and the nature of pensions under this theory as deferred compensation, see Yeazell, supra, indicate that it should attach at the time of employment. E.g., Betts, supra; Quinn, supra. Thus, it would be our view that all present employees of the District who are members of the Retirement System have a constitutionally cognizable right to a pension system. Since the right here found arises at the time of employment, it must a fortiori attach to those already retired. See also Newman v. City of Oakland Retirement Bd., 145 Cal. Rptr. 628 (Cal. App. 1978). Thus, we also conclude that present retirees have constitutionally protected rights in the existence of a retirement system.

We must conclude, therefore, that to the extent L.D. 1787 attempts to withdraw the Bingham Water District from the Maine State Retirement System without protecting its present members and retirees, it is unconstitutional. Thus, the answer to questions 1 and 2 in your opinion request is that employees and retirees of participating local districts of the Maine State Retirement System do have a right in their existing retirement plan beyond the refund of their contributions. We need not determine the extent of such right except to state that the Legislature may not entirely eliminate the present system without protecting the rights of current members and retirees. We do not address or consider the much more complex question of whether, and to what extent, the Legislature might change the level of present and future benefits.

2/ While participating local districts have some flexibility in adopting the specifics of the Retirement System statute, see 5 M.R.S.A. § 1092(2)-(3-A), they have no discretion to vary the 10-year vesting provision.

Your third question is directed to the issue of waiver. It is settled law that constitutional rights may be waived if all the requirements of waiver, such as knowledge and capacity, are met. See generally State v. Boilard, 359 A.2d 65 (Me. 1976). Thus, a current member or retiree of the District may waive the rights which have been heretofore discussed, provided he has sufficient knowledge, capacity and does it freely.

The final question you ask is what action the Legislature may take to withdraw the District from the Retirement System without violating the rights which we have found to exist and "without affecting the potential legal challenge to the claims or rights of the current employees and retirees." We cannot, within the scope of this opinion, address all of the possible alternatives which may be open to the Legislature in handling such a case, and we would not, in any event, presume to advise the Legislature in matters of policy where a number of legal alternatives is available. It is our understanding that, in the past, the withdrawal of a local district from participation in the Maine State Retirement System has been accomplished by permitting current members and retirees to continue in that status if they so desire, but ceasing the operation of the plan for employees hired subsequent to the date of withdrawal. Such a method would, in this instance, protect those persons so entitled but would allow for the eventual disengagement of the District from the System.

The second part of your question is somewhat more troublesome. As we understand it, there is some question of the legal propriety of the District's original entry into the System because the trustees who voted to enter may not have been empowered to take that action under the District's charter. While we would, of course, take no position on the merits of this question, which might well result in litigation between the voters of the District and its former trustees, we think that the Legislature could amend L.D. 1787 in such a way as to protect those current members and retirees who might be entitled to continuing rights and benefits in the System, regardless of the disposition of the question of the legality of the original entry, while making clear that the bill should in no way be read to authorize payment or the granting of rights to those who might later be found, in such litigation, not to be entitled to such

rights or benefits as a result of their improper actions. We would not propose such clarifying language here, but we would be happy to offer our aid in arriving at a solution to this problem.

If you have further questions, please feel free to contact this office.

Sincerely,

RICHARD S. COHEN
Attorney General

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