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December 18, 1991

Honorable Charles P. Pray
President of the Senate
State House Station #3
Augusta, Maine 04333

Dear Senator Pray:

You have inquired whether Sections NN-1 of Legislative Document 1985, prohibiting the award of merit pay increases to certain employees, would, if enacted, violate the contract Clauses of the United States and Maine Constitutions. For the reasons which follow, it is the opinion of this Department that the sections would likely be found unconstitutional with regard to those employees entitled to merit increases during the period from January to June 30, 1992 under the currently valid collective bargaining agruments.

Section NN-1 of L. D. 1985 provides as follows:

> **Sec. NN-1. Merit Increase.** Notwithstanding the Maine Revised Statutes, Title 26, section 979-D, and any other provisions of law, any merit increase scheduled to be awarded between January 1, 1992 and December 31, 1992 to any person employed by the State, including probationary employees,

> employees of the Legislature, Judicial Department and independent agencies and employees of the University of Maine System, the Maine Technical College System and Maine Maritime Academy may not be awarded, authorized or implemented. Any savings realized by the University of Maine System, the Maine Technical College System and Maine Maritime Academy must be used to offset any proposed or implemented tuition increases.

At the outset, we see no potential problem with this provision except to the extent that it is inconsistent with express contractual provisions contained in current collective bargaining contracts. As to those employees who are not covered by such contracts or whose contracts do not contain any inconsistent provisions with respect to merit increases, therefore, the enactment of Section NN-1 of L.D 1985 would be entirely permissible.

Given the shortness of time, we have not attempted to review all the applicable collective bargaining contracts. However, we did review certain of the current MSEA contracts and the current AFSCME contract. These contracts, which cover the period from July 1, 1989 to June 30, 1992, provide that employees will be eligible to receive step increases based upon annual performance evaluations and that, if job performance is found to be satisfactory, the step increases will be effective on or about the employee's anniversary date -- the date that the employee originally entered state employment. As a result, certain employees will be entitled under the collective bargaining agreements to step increases during the period from January 1, 1992 to June 30, 1992 if their job performance is found to be satisfactory and if their anniversary date falls during that period.

As to those employees, the issue is whether Section NN-1 of L.D 1985, if enacted, would violate those provisions in the United States and Maine constitutions which prohibit the State from passing any law "impairing the obligation of contracts." U. S. Const., Art. 1, § 10; Me. Const. Art. I, § 11. Since the language in these two constitutional provisions is identical and has been similarly interpreted, see N. A. Burkitt, Inc. v. J. I. Case Co., 597 F.Supp. 1986, 1089-90 (D. Me. 1984) no distinction need be drawn between them for purposes of analysis.

Before it can be determined whether there has been any contractual impairment, it much first be determined whether the subject of merit pay increases is "prescribed or controlled" by

state law. Specifically, 26 M.R.S.A. § 979-D(1)(E)(1) provides that all matters concerning the relationship between a public employer and its employees "shall be the subject of collective bargaining, except those matters which are prescribed and controlled by public law." (emphasis added). Under this provision, matters prescribed or controlled by state law are not appropriate subjects for collective bargaining and even if there is contractual language on those subjects, the relevant statutes rather than the collective bargaining agreement are controlling. Since the Legislature is always free to alter or modify existing law and since parties to a contract have no legitimate expectation that the law will not be changed, it is far less likely that any successful claim of an unconstitutional impairment of contract could be brought if the Legislature makes changes with respect to matters that were, when the contract was entered into, prescribed or controlled by State law.

In our view, however, the subject of merit pay increases is not prescribed or controlled by State law except with respect to probationary employees. Title 5 M.R.S.A. § 7065(3) provides that step increases shall not be automatic but are dependent upon performance. It also provides that no such advancements in salary shall be made until the employee has completed the probationary period. As to non-probationary employees, however, § 7065(3) does not control or prescribe when merit increases may be given and does not remove this subject from collective bargaining.

As a result, we conclude that § NN-1 of L.D. 1985, as currently proposed, would effect an impairment of contractual obligations. To determine whether this is an unconstitutional impairment, however, requires analysis of the factors set forth by the U. S. Supreme Court in Energy Reserves Group v. Kansas Power and Light Co., 459 U.S. 400 (1983). In that case, the Court noted that "although the language of the contract clause is facially absolute, its prohibition must be accommodated to the inherent police power of the State 'to safeguard the vital interests of its people'". 459 U.S. at 411, quoting Home Building and Loan Assn. v. Blaisdell, 290 U.S. 398, 434 (1934). Under Energy Reserves, the three factors that must be considered are (1) whether the State law has operated as a "substantial" impairment; (2) whether the State is acting to further a significant and legitimate public purpose; and (3) whether the specific impairment in question is reasonable and necessary to serve the State's interest. 459 U.S. at 412-413.

A particular problem exists in this case because § NN-1 involves an impairment of the State's own financial obligations. In U. S. Trust Co. v. New Jersey, 431 U.S. 1, 25-26 (1977), the U. S. Supreme Court noted that such an impairment requires heightened scrutiny:

> The Contract Clause is not an absolute bar to subsequent modification of a State's own financial obligations. As with laws impairing the obligations of private contracts, an impairment may be constitutional if it is reasonable and necessary to serve an important public purpose. In applying this standard, however, complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State's self-interest is at stake. A governmental entity can always find a use for extra money, especially when taxes do not have to be raised. If a State could reduce its financial obligations whenever it wanted to spend the money for what it regarded as an important public purpose, the Contract Clause would provide no protection at all.

(Footnote Omitted). In Energy Reserves, the Supreme Court also commented that "[w]hen a State itself enters into a contract, it cannot simply walk away from its financial obligations. In almost every case, the Court has held a governmental unit to its contractual obligations when it enters financial or other markets." 459 U.S. at 413 n. 14.

Moreover, we are aware of several court decisions from other states whose Legislatures have attempted to rescind pay increases that were expressly called for in collective bargaining agreements. See Carlstrom v. State of Washington, 694 P.2d 1 (Wash. 1985); Public Employees v. County of Sonoma, 591 P.2d 1 (Cal. 1979); Matter of Subway Surface Supervisors Assn., 404 N.Y. Supp. 2d 323 (N.Y. 1978). In both the Washington and California cases, state legislation rescinding pay increases was invalidated. In both these cases the courts found that legislative prohibition of contractual pay increases was a substantial impairment under the first part of the Energy Reserves test. Moreover, they also found that such an impairment was not justified by the specific fiscal situation faced by the state at that time. These cases found that a

shortfall in revenues was not a sufficiently significant and legitimate purpose under the second part of the Energy Reserves test to justify the proposed impairment of contractual obligations.

This does not mean that a fiscal emergency can never justify legislation rescinding contractual wage increases. This is demonstrated by the New York case, where such legislation was upheld in circumstances where the City of New York was virtually bankrupt and was faced with a potential inability to meet its obligations to its bondholders and a potential inability to provide essential services to its inhabitants. See Matter of Subway - Surface Supervisors Assn., 404 N.Y. Supp. 2d at 328 n.3.

In this case, the State is faced with a $100 plus million shortfall but would only save $1 million by restricting merit increases. Moreover, it would be different to argue that the State has no other alternatives to achieve savings other than by eliminating merit increases. Under these circumstances, § NN-1 of L.D. 1985 presents a situation far more similar to that faced by the Washington and California courts in Carlstrom and Sonoma County than the situation faced by the New York court in Subway - Surface Supervisors. For this reason, we believe that it is doubtful that a court would uphold § NN-1 if faced with a challenge brought by an employee who would otherwise be entitled to a merit increase during the period from January 1, 1992 to June 30, 1992.

This does not mean that § NN-1 would be invalid in its entirety with respect to employees under collective bargaining agreements. Section NN-1, as drafted, applies not just to merit increases scheduled during the current contract but also to merit increases scheduled during the period from July 1 and December 31, 1992. Since the current collective bargaining agreements expire at the end of June, the prospective application of § NN- 1 to any future collective bargaining agreement beginning after June 30, 1992 would present no constitutional problem. A contract cannot be impaired by a statute enacted before the contract was entered into. Ogden v. Saunders, 25 U.S. (12 Wheat) 213 (1827).

The opinion should also not be read to suggest that where contractual financial obligations are expressly made subject to legislative action, as in the State's collective bargaining agreements, the Legislature would not be entitled to reject unfunded pay increases for future years of the contract.

I hope the foregoing answers your questions. If not, please feel free to reinquire.

Sincerely,

MICHAEL E. CARPENTER
Attorney General

MEC/rar

cc: Honorable John R. McKernan, Jr.
Honorable John L. Martin