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March 15, 1984

The Honorable Jim Green  
Arizona State Representative  
House Wing, State Capitol  
1700 West Washington  
Phoenix, Arizona 85007

Re: I84- 039 (R84-034)

Dear Representative Green:

This letter is in response to your inquiry concerning the effect of enactment of recent amendments to Arizona's Retirement Act ("the Retirement Act") and, specifically, to A.R.S. § 38-781.01 which changed the definition of "compensation" and specifically excluded "lump sum payments, on termination of employment, for accumulated vacation or annual leave, sick leave, compensatory time or any other form of termination pay." You have asked whether this change in the definition of "compensation" applies to persons who become members of the State Retirement System before the effective date of the aforementioned amendments which is December 31, 1983. For the reasons set forth below, we conclude that changes in retirement benefits may be made only prospectively and that retirement benefits must be calculated to reflect the existing statutory formula at the time the benefits were earned.

Our conclusion is based upon the case of Yeazell v. Copins, 98 Ariz. 109, 402 P.2d 541 (1965). In that case the plaintiff, a retired policeman, was hired by the City of Tucson in 1942 when the 1937 Police Pension Act provided for a pension equal to half the average monthly salary during one year immediately prior to retirement. The 1937 Act was amended in 1952, changing the pension amount to half the average monthly salary for five years prior to retirement. The effect of this change would be to provide the plaintiff with \$7.21 a month less than under the 1937 Act. The Arizona Supreme Court held that,

under the terms of plaintiff's contract of employment, an entitlement to retirement benefits was fixed the day he started his job which could not be changed retroactively or unilaterally without the plaintiff's assent or the existence of circumstances evidencing that the plaintiff had waived his rights to benefits under the law in effect when he became employed.<sup>1/</sup>

Subsequently, the Yeazell holding has been analyzed and by courts in both Arizona and other jurisdictions. In City of Phoenix v. Boerger, 5 Ariz. App. 445, 427 P.2d 937 (1967), the Arizona Court of Appeals summarized the Yeazell holding and concluded that an employee's compliance with statutory changes does not constitute a waiver by the employee of his right to insist that retirement provisions in effect when he was hired be enforced for his benefit. The court stated:

Yeazell holds that a pensioner's entitlement to benefits may not be reduced below those which are provided by law at the time of the commencement of employment. We hold that the employees cannot be deemed to have elected to come under the provisions of later enactments by virtue of the fact that first 3-1/2% and later 5% of their salaries were contributed to the reserve fund. By their compliance with the statute requiring such contribution, they augmented the fund but did not thereby waive their rights under the 1928 Act. They did not thereby elect to come under any later act.

5 Ariz. App. at 453-454.

While Yeazell and Boerger hold that benefits may not be reduced below those which are provided by law at the time of the commencement of employment, both cases imply that, if the employee accepts an increase in benefits conferred by a later amendment, then he has elected to also accept all changes conferred by that amendment. The difficulty with the Yeazell and Boerger holdings is that, because the Retirement Act is amended on a regular basis, an employee theoretically could have the right to choose which of the amendments enacted during the

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1. The court left unanswered in Yeazell what particular circumstances constitute waiver or estoppel to assert rights under the Act in effect when employment began.

entire term of his employment would be most beneficial to him upon retirement, creating a myriad of accounting and actuarial problems.

Yeazell was also analyzed in Bennett, Ex Rel Arizona State Personnel Commission v. Beard, 27 Ariz. App. 534, 556 P.2d 1137 (1976). In that case the court held that employment rights not yet vested, such as the rate of annual leave accrual, can be changed prospectively. However, the court cautioned that the employee's leave benefits accrued prior to the change in benefits cannot be modified. The court distinguished a change in the rate of annual leave accrual from the situation addressed in Yeazell stating:

We do not have the situation touched upon in Yeazell that continued employment after the 1952 amendment to the Pension Act should not be construed as a waiver of his right to retirement benefits under the 1937 Act. As previously pointed out, Yeazell dealt with the attempted retroactive change of previously vested contractual rights. Here we are dealing with future benefits as yet unvested.

27 Ariz.App. at

The vested nature of benefits was discussed in Abbott v. City of Tempe, 129 Ariz. 273, 630 P.2d 569 (App. 1981) in which the Arizona Court of Appeals while referring to the Bennett and Yeazell cases stated:

In both these cases the Court recognized that a vested contractual right to benefits existed only when an employee had already performed services and earned benefits, the payment of which was to be made at a future date. The same rationale did not apply where the city has merely adopted an ordinance which provides for the payment of certain benefits, and an employee has yet to perform services entitling him to the benefits.

129 Ariz. at

Thus, the Arizona courts have recognized that an employee has a vested contractual right to benefits existing

when an employee has already performed services and earned the benefits, the payment of which is to be made at a future date. Those employees who became members of the State Retirement System before the effective date of the pertinent amendments have a vested contractual right to benefits under the preexisting definition of "compensation" which did not exclude "lump sum payments, on termination of employment, for accumulated vacation or annual leave, sick leave, compensatory time or any other form of termination pay."

In reaching our conclusion, we are nonetheless mindful that the analysis adopted in Yeazell has been strongly criticized by courts in many other states as being too restrictive. Brazelton v. Kansas Public Emp. Retirement, 227 Kan. 443, 607 P.2d 510 (1980); Betts v. Board of Administration, 21 Cal. 859, 148 Cal. Rptr. 158, 582 P.2d 614 (1978). As the court stated in Brazelton:

We decline to adopt that hard and fast rule [referring to the Yeazell holding]. There may be times when changes are necessary to protect the financial integrity of the system or for some other compelling reason which would mandate and justify some unilateral changes.

607 P.2d at 517.

The necessity for allowing changes in benefits conferred by a particular retirement system based upon the vicissitudes of the economy was recognized in Betts v. Board of Administration in which the court stated:

An employee's vested contractual pension rights may be modified prior to retirement for the purpose of keeping a pension system flexible to permit adjustments in accord with changing conditions and at the same time maintain the integrity of the system. [citations omitted] Such modifications must be reasonable, and it is for the courts to determine upon the facts of each case what constitutes a permissible change. To be sustained as reasonable, alterations of an employees' pension rights must bear some material relation to the theory of a pension system and its successful operation, and

changes in pension plan which result in disadvantage to employees should be accompanied by comparable new advantages. [emphasis added by court, citations omitted]

582 P.2d at 617.

See also Nash v. Boise City Fire Department, 104 Idaho 803, 663 P.2d 1105, (1983) in which the court criticized the contract analysis adopted by the court in Yeazell and quoting Dullea v. Massachusetts Bay Transportation Authority, 421 N.E. 2d 1232 (Mass. App. 1981) stated,

[b]y freezing the provisions of the plan without any adjustments, serious harm can occur to the governmental entity that created it. Changes in policies, commitments and financial conditions can make plans drafted under favorable conditions unrealistic and burdensome on the government employer.

663 P.2d at 1107

Although we perceive manifest flaws in the analysis adopted in Yeazell which is contrary to the approach now taken by most courts in the country, we are constrained to follow Yeazell because it is the law in Arizona.

Finally, we note that A.R.S. § 38-781.33 which gives the legislature "the right to modify, amend or repeal this article, or provisions thereof" does not alter our conclusions. Discussing a similar provision, the Arizona Supreme Court has stated:

The right of a subsequent legislature to amend or repeal it entirely was no more or more less than with any ordinary law . . . in so far as [subsequent legislation] attempted either to limit or enlarge the general powers of a subsequent legislature in any respect, was void.

Hammons v. Watkins, 33 Ariz. 76, 262 P.2d 616 (1927).

While the Legislature has the inherent authority to amend or repeal any existing statute, it is nonetheless is barred from enacting legislation which would impair the

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obligation of a contract. Ariz.Const., Art. II, § 25.<sup>2</sup>  
Under the Yeazell analysis, the 1970 passage of A.R.S.  
§ 38-781.33 still would not become part of the contract with the  
retirement system members employed after the effective date of  
the statute because it would destroy the mutuality of the  
contract allowing the legislature to modify benefits without the  
consent of the employee.

Sincerely,



BOB CORBIN  
Attorney General

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2. Of course, if the contract analysis adopted by Yeazell is  
rejected, the constitutional bar against impairment of contracts  
would not apply.