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MUNICIPAL LAW

BY JEFFREY D. FRIEDLANDER

A Brief Introduction To New York City Pension Law

In our present economic circumstances, stories repeatedly appear in the press decrying alleged pension abuses and the cost of pension benefits provided to New York City retirees. At the same time, public employees argue against any changes to the system designed to provide taxpayers with some relief from what may be an unsustainable burden.

While public pension law must surely be one of the most recondite of legal topics, it is useful at this time to examine the structure of the city's pension system, some of the issues that are being litigated, the role played by the New York City Law Department in the defense and administration of the system and, very importantly, the efforts to recover losses to the pension funds due to corporate fraud.

First, there is no single New York City pension fund; there are five: the New York City Employees' Retirement System (NYCERS), which is the largest of the group, the New York City Police Department Pension Fund, the New York City Fire Department Pension Fund, the New York City Teachers' Retirement System, and the New York City Board of Education Retirement System.¹ These funds are each administered by a different board of trustees, with authority shared by public and union representatives. With close to 600,000 active and retired members and assets exceeding \$83 billion, the city funds are cumulatively one of the largest public pension systems in the country.²

The second salient feature of the system is that all five pension funds are defined benefit plans. That is, retirees who have made their required member contributions receive a specified amount at retirement, generally based on years of service and salary, as opposed to defined contribution plans, in which benefits generally are based on amounts contributed and the investment earnings on those contributions.

Defined benefit plans have become rare in the private sector, where defined contribution plans are now the norm. In times of fiscal austerity and poor market conditions, a member of a defined benefit pension plan holds a very valuable asset.

The final initial point is that city pension benefits are contractual rights that are protected by the New York state constitution from any diminishment or impairment.³ This means that budget cuts or other cost saving measures can never target existing pension benefits, and the Legislature is barred from amending the pension laws to diminish in any way the benefits of existing members or retirees.

Once a benefit is conferred, it cannot be taken away. Therefore, any consideration of pension reform aimed at



reducing pension costs must be directed solely at the benefits of prospective new members of the system.

The Pensions Division of the Law Department, consisting of eight attorneys, represents the city's five pension funds in litigation challenging individual and class-wide benefit determinations, provides legal counseling and advice to the pension funds and city agencies, drafts and provides comments on proposed legislation relating to pensions, assists in the implementation of new laws, and, in conjunction

with nine securities litigation firms retained by the Law Department, investigates and represents the city funds in securities fraud cases.

As statutory counsel to the funds, it is the duty and objective of the Law Department to provide advice and counsel to each of the city's pension systems. Pension Division attorneys face the challenge of representing and providing counsel to each of the five different funds, each, as noted, administered by a board of trustees composed of different officials and divided between city and employee representatives.

For example, the Board of Trustees of one of those systems, NYCERS, consists of a representative of the Mayor, the Public Advocate, the Comptroller, each of the borough presidents, and the chief executive officer of three employee labor organizations. Administrative Code §13-103.

In the course of their proceedings, city and employee representatives on the boards may differ on a number of issues, most frequently on the application and interpretation of provisions of the pension laws to individual applications for disability retirement. See *Uniformed Firefighters Assn. v. Beekman*, 52 N.Y.2d 463 (1981). In this situation, it is the role of the Pensions Division attorneys to provide reasoned and balanced legal advice based on case law, as well as information on the experiences of the pension funds in similar circumstances.

Disability Benefit Litigation

The majority of litigation against the city retirement systems involves challenges brought pursuant to Article 78 of the Civil Practice Law and Rules by individual pension members who have been denied accident disability retirement benefits. For uniformed members, such as police and firefighters, these benefits are very valuable, equaling 75 percent of their salaries, and, but for a small portion, are tax free.

BY JEFFREY D. FRIEDLANDER

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The definition of “accident” in this context is one that has been defined through litigation. The Court of Appeals has defined the term, as used in the pension accident disability statutes, to be a “sudden, fortuitous mischance, unexpected, out of the ordinary, and injurious in impact.” *Lichtenstein v. Board of Trustees of the Police Pension Fund of the Police Department of the City of New York*, Article II, 57 N.Y.2d 1010, 1012 (1982).

In stating that “not every line of duty injury will result in an award of accident disability,” the Court of Appeals contrasted “injuries sustained while performing routine duties but not resulting from unexpected events,” which are not accidents, with injuries sustained by “precipitating accidental event[s] . . . which [are] not a risk of the work performed,” which are accidents. *McCambridge v. McGuire*, 62 N.Y.2d 563, 567-68 (1984). More recently, the Court has stated that accident disability is properly denied if it is found that the member “was injured while performing his usual duties.” *Kehoe v. City of New York*, 81 N.Y.2d 815 (1993), aff’g 186 A.D.2d 376 (1st Dept. 1992).

Last month, the New York Supreme Court upheld the New York City Fire Department Pension Fund’s determination denying accident disability retirement benefits to a firefighter who was injured in a personal altercation with another firefighter.

The incident occurred on New Year’s Eve 2003 at a Staten Island firehouse. The petitioner, who along with other firefighters was drinking alcohol while on duty, had an argument with a fellow firefighter that escalated into a physical altercation, culminating in the petitioner being hit over the head with a metal chair. The fact that as a result of the incident, petitioner suffered brain damage and was found to be disabled from performing the duties of a firefighter, did not entitle him to an accident disability pension. The Board of Trustees determined that petitioner was injured by the intentional act of his co-worker, which did not constitute an “accident” supporting the granting of the pension. *Walsh v. Scoppetta*, Index No. 23889/08 (Sup. Ct. Kings County, Feb. 25, 2009).

While the great majority of accident disability retirees collect their disability retirement benefits for life, that is not always the case. Pursuant to Safeguards on Disability Retirement laws,⁴ accident disability retirees may be called back to service if a determination is made that the person is no longer disabled from performing his or her job duties.

Recently, attorneys of the Pensions Division prevailed in a lawsuit brought by a former police officer whose accident disability retirement benefits were revoked after he was observed performing roofing work for his own company, and thereafter found by the Medical Board of the New York City Police Pension Fund to be no longer disabled from performing the duties of a police officer. The former officer then failed a pre-screening drug test and was consequently found unqualified for reappointment to the position of police officer

or any other city position. *Seiferheld v. Kelly*, Index. No. 114351/07 (Sup. Ct. N.Y. County, Oct. 23, 2008).

Other Litigated Matters

Although disability benefit litigation constitutes the bulk of pension litigation, other benefit issues are also litigated, including a contest, yet to be finally resolved, by the parents of a firefighter killed at the World Trade Center who are challenging the determination of the City of New York Fire Department Pension Fund to grant their son’s fiancée a portion of the death benefits payable by the pension fund, rather than granting the benefits in their entirety to the parents.⁵

After several interim orders and proceedings before the King’s County Supreme Court and the Board of Trustees of the Fire Department Pension Fund, as well as the submission of additional evidence, the court ultimately found in 2008 that questions of fact existed, necessitating a hearing. See *Prior v. Board of Trustees of the City of New York Fire Department Pension Fund*, Index No. 11979/2006 (Sup. Ct. Kings County, Feb. 27, 2008). The hearing began on April 17, 2008, resumed in May, and after numerous unsuccessful attempts at settlement, was completed on Dec. 10, 2008.

Benefit Class Actions

In addition to litigating claims brought by individual pension members, Pensions Division attorneys defend class actions challenging the method of calculating benefits for entire groups of pension members. Two active state court cases illustrate the complexity of this type of litigation and magnitude of exposure.

In *Nager v. The New York City Teachers’ Retirement System*, Index No. 119294/02 (Sup. Ct. N.Y. County), commenced in August 2002, the plaintiffs allege that the New York City Teachers’ Retirement System improperly failed to include “per session” compensation in determining pension benefits for certain retired TRS members. Per session work is work, such as coaching, that is performed in addition to regular teaching responsibilities, and for which teachers receive additional compensation.

Following the certification of a class, the parties agreed to calculate pension adjustments, if any, based on an algorithm, for the class of over 50,000 retirees. While the substance of the agreement is for the most part resolved and expected to be implemented later this year, class counsel continue to seek attorneys’ fees (approximately \$30 million) based on a percentage of the total amount of pension adjustments expected to be made pursuant to the terms of the settlement. That request was rejected by the trial court and the Appellate Division. See *Nager v. The New York City Teachers’ Retirement System*, 57 A.D.3d 389 (1st Dep’t 2008).

In March of 2005, the president of the United Federation of Teachers and three retired teachers filed an Article 78 proceeding and an action seeking an order requiring that the New York City Teachers’ Retirement System Board of

BY JEFFREY D. FRIEDLANDER

A Brief Introduction To New York City Pension Law

Trustees correct an alleged miscalculation of the benefit formula applicable to members who retire under the 20 Year Pension Plan. *Randi Weingarten v. Board of Trustees of the New York City Teachers' Retirement System*, Index No. 103818-05 (Sup. Ct. N.Y. County) and *Randi Weingarten v. Board of Trustees of the New York City Teachers' Retirement System*, Index No. 103819-05 (Sup. Ct. N.Y. County).

The 20 Year Plan, codified in 1970, provides that members retiring after 20 years of service are entitled to a basic retirement allowance equal to 50 percent of their salary. Administrative Code §13-547. A settlement was reached in 2007, providing for payment of \$160 million over a 10-year period, and could affect 30,000 retirees as well as 5,000 active members.

Legislation

The Law Department regularly drafts pension legislation, an activity that calls on the skills and expertise of the Pensions Division.

Pensions Division attorneys are now actively involved in analyzing and drafting pension legislation proposals that would amend certain pension laws prospectively to make pensions less costly to the government over the long term.

For example, legislation that is currently under consideration would increase the length of time it would take employees to vest rights to their pensions, increase employee contributions, and would eliminate overtime in the salary figures used in calculating pensions for certain employees. It is estimated that enactment of these proposals would save the City hundreds of millions of dollars.

Recouping Financial Losses

Particularly timely are the efforts of Pensions Division attorneys, working with outside counsel, to recover losses of the city's pension funds due to corporate fraud.⁶ In the past two years, the Division has recovered almost \$20 million for the funds in connection with securities fraud settlements.

The Private Securities Litigation Reform Act of 1995 requires a court to adopt the rebuttable presumption that "the most adequate plaintiff . . . is the person or group of persons that . . . has the largest financial interest in the relief sought by the class." 15 U.S.C. §78u-4(a)(3)(B)(iii). Accordingly, as one of the largest public pension systems in the country, the combined New York City pension systems frequently have been awarded lead plaintiff status in federal securities fraud class actions.

Most recently, the city's pension funds were awarded lead plaintiff status in two class actions arising out of the sub-prime mortgage debacle. On Nov. 28, 2007, the city's pension funds and the New York State Common Retirement System were appointed lead plaintiffs in litigation against Countrywide Financial Corporation, one of the nation's largest mortgage lenders. The city and state pension systems are both represented by outside counsel Labaton Sucharow.

The lawsuit alleges, among other things, that the defendants made materially false and misleading statements regarding the nature of its lending standards and the quality of its loans; that Countrywide distorted the definitions of the terms "prime" and "sub prime" to mislead investors and the financial community with respect to the nature of its business; and that certain of Countrywide's financial statements were materially misleading in violation of generally accepted accounting principles.

The action further alleges that top management of the company reaped hundreds of millions of dollars in proceeds upon their sale of personally held Countrywide stock while in the possession of material nonpublic information. After disclosure of Countrywide's problems, the company's common stock dropped billions of dollars.

Late last year, the U.S. District Court for the Central District of California issued a favorable decision that largely rejected Countrywide's requests to dismiss the claims, thus allowing the lawsuit to proceed. *In re Countrywide Financial Corporation Securities Litigation*, Lead Case No. 07-CV-5295 MRP (MANx) (C.D. Cal.).

On Oct. 14, 2008, the city's pension funds were appointed lead plaintiffs in the class action securities litigation commenced against Wachovia Corporation. In this litigation, the city funds are represented by outside counsel Kirby & McInerney.

The complaint alleges that during the class period of May 8, 2006, through Sept. 29, 2008, Wachovia, one of the nation's largest financial service providers, serving retail, brokerage and corporate customers, issued materially false and misleading statements regarding its business and financial results, and that as a result, the company's stock traded at artificially inflated prices. Class losses are estimated to be in the tens of billions of dollars.

Specifically, the amended complaint alleges that the company concealed the nature and magnitude of its exposure to sub prime mortgages and debt related to sub prime mortgages; misrepresented that the company maintained very conservative underwriting standards and had very conservative risk management policies and procedures; hid losses from certain risky mortgage products by disclosing them only after the properties had been foreclosed and sold at a loss; failed to disclose its exposure to subprime mortgage-backed securities such as collateralized debt obligations; and overstated its financial results in violation of generally accepted accounting principles by failing to timely write-down sub prime assets and failing to maintain adequate reserves for risky loans. *In re Wachovia Equity Securities Litigation*, Dkt. No. 08-6171 (RJS) (S.D.N.Y.).

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MUNICIPAL LAW

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A Brief Introduction To New York City Pension Law

1. See NYC Admin. Code §§13-101, 13-201, 13-301, and 13-501; and BERS Rules and Regulations, adopted pursuant to NY Education Law §2575.

2. See “The Largest Plan Sponsors,” *Pensions & Investments*, Jan. 26, 2009, at 16 (city combined funds ranked as seventh largest retirement plan in the country in terms of assets).

3. Specifically, the Constitution states that “membership in any pension or retirement system of the state or a civil division thereof shall be a contractual relationship, the benefits of which shall not be diminished or impaired.” Art. 4 §7.

4. Administrative Code §13-254 (police officers); §13-171 (NYCERS); §13-356 and §13-357 (Fire); §13-553 (TRS); and §19 of the BERS Rules and Regulations.

5. See Chapter 468 of the Laws of 2002, as amended by Chapter 162 of the Laws of 2003.

6. Counsel are chosen from a panel of nine law firms that were selected by the Law Department pursuant to a competitive procurement process.