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Fitch: CA Pension Case Highlights Legal Obstacles to Reform.

Fitch Ratings-New York-21 August 2015: A recent legal settlement in San Jose, CA underscores our view that reducing pension liabilities will be challenging for most governments and ultimately dependent on state-by-state judicial review, Fitch Ratings says. The city's agreement with police and firefighter unions would restrict most pension reforms to new hires, leaving benefits for existing employees and retirees largely untouched. San Jose voters authorized broad changes to public pensions under Measure B in 2012, but reforms have been stalled by legal challenges from the outset.

Many observers had expected the litigation to provide an opportunity for legal clarification of the so-called California Rule, which provides that pension benefits are a vested contractual right and cannot be impaired for existing public employees and retirees. Lower courts had generally supported this position in earlier Measure B litigation, but such cases had yet to come before the Supreme Court of California.

Local government pension reform in California could see increased attention under a voter initiative targeting the November 2016 general election. Signature gathering recently began for the Voter Empowerment Act of 2016, which would amend the state's constitution to permit local voter initiatives to address public employee compensation and retirement benefits. The measure was sponsored by San Jose's former mayor, among other proponents, and appears designed to overturn the California Rule.

The likelihood of approval for the new initiative is uncertain, particularly given anticipated strong opposition from public employee unions. However, ongoing legal battles over pension reform can be expected regardless of the initiative's outcome and will continue to challenge efforts to reduce pension liabilities in California and other states.

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