CHAPTER 7

INTEREST ARBITRATION: CAN THE PUBLIC SECTOR AFFORD IT? DEVELOPING LIMITATIONS ON THE PROCESS

I. AN OVERVIEW

WAYNE MINAMI*

Compulsory arbitration has been adopted in many states as an alternative to public employee strikes. As of August 1980, 20 states had such legislation on their books.

Growing just as fast are statutes or constitutional provisions that attempt to limit government spending. At the present time, Hawaii, Nevada, New Jersey, Oregon, and Washington have both a "cap" law and compulsory interest arbitration. How do these "cap" laws affect interest arbitration in the public sector? Today's panel will address the pros and cons of such legislation. My role is to give an overview of the subject.

What are "cap" laws and how prevalent are they? New Jersey was the first state to adopt the process. In 1976 the New Jersey legislature adopted a state spending limit that restricted increases in state spending to increases in personal income. With regard to school districts, counties, and municipalities, the legislature set a 5-percent maximum per year on increases in spending. Colorado's legislature in 1977 approved a measure that limits increases in state spending to a 7-percent increase over the previous year's expenditures.

Probably the most publicized of these spending limitations is Proposition 13 which was approved by California voters in June 1978. By drastically reducing the amount of tax revenues generated from property taxes, Proposition 13 had an immediate impact on the amount of money available to fund negotiated or arbitrated salary increases. The passage of Proposition 13 resulted in a "bail out" law by which the state supplied more than

*Attorney, Honolulu, Hawaii.

$4 billion to compensate localities for lost revenues. As a condition for receipt of state bail-out funds, the state required the localities to limit employee wage increases to no more than that accorded state employees, a requirement that placed a cloud over many negotiated salary increases. This confusing situation was not remedied until the California Supreme Court struck down the restriction as an unconstitutional impairment of contract.[1] The bail-out law also attempted to freeze the level of fire and police services by requiring that the level of police and fire protection actually provided in the 1977–1978 fiscal year be continued for the 1978–1979 fiscal year.

The publicity from Proposition 13 fueled taxpayers dissent in other states. In rapid succession, limitations were adopted. Five states—Arizona, Hawaii, Michigan, Tennessee, and Texas—adopted spending or revenue limits in 1978. Four more states—Louisiana, Nevada, Utah, and Washington—adopted limits in 1979. In 1980, Delaware, Idaho, Oregon, and South Carolina continued the trend. As of August of last year, 16 states had such limits applicable to state expenditures or revenues. In addition, nine other states had limits applicable to local government units.

Since these cap laws apply to total spending by a municipality or a state, you may ask: How can they impact an arbitrator? The impact is clearly brought out in a case called *Policemen's Assn.* v. *Town of Irvington.*[2] In that case the Town of Irvington was faced with a maximum 5-percent increase in spending imposed by the New Jersey cap law. Increases in insurance premiums and utilities costs were in excess of 5 percent and eroded the amount available for salary increases for employees. The town, in a final-offer arbitration with the police, offered a 5-percent salary increase. The Policemen's Association asked for substantially more. The town presented evidence that if it had to comply with the union's demand, it would be forced to lay off many essential employees, and it argued that these layoffs would aggravate present "skeleton" crews and hence be detrimental to the citizens of Irvington. The arbitrator, however, found that the union's economic proposals were "more fair and reasonable" than those put forth by the town.

In seeking confirmation of the arbitrator's order, the union

[1]*Public Employees* v. *County of Sonoma,* 100 LRRM 3044 (1979).
[2]102 LRRM 2169 (1979).

brought the matter before the courts. The New Jersey Supreme Court made the following finding: The costs incurred in implementing compulsory arbitration awards are subject to the cap law. The court noted that the statute providing for interest arbitration required that the arbitrator "give due weight" to eight enumerated factors and that three of them, (a) "the interests and welfare of the public," (b) "[t]he lawful authority of the employer," and (c) "the financial impact [of the award] on the governing unit, its residents and taxpayers" required the arbitrator to consider a municipality's cap-law restraint prior to the rendition of an award.

Arbitrators can take comfort in the standard adopted for judicial review of the arbitration award. The court inquiry was limited to whether the award was supported by substantial credible evidence in the record and whether the arbitrator gave due weight to each of the eight statutory factors and rendered an award that was "reasonable." The court found that the award was reasonable and enforceable even though the award, when added to other proposed expenses, would result in an increase in total expenditures in excess of 5 percent. The court stated: "The manner in which the Town will comply with the award without running afoul of the Cap Law proscriptions is a matter which neither we nor the arbitrator have the authority to decree." That decision lies with municipal officials.

The court in that case quotes a prophetic assemblyman who was a member of the study commission which proposed the compulsory interest arbitration law:

> "The cap laws have put a new element into this whole picture that makes the work of the arbitrator, I would say, even more difficult than it would have been before because he now has to take into consideration not only the dispute that is before him, but what the requirements of the governing body, whatever it may be—a board of education, a municipality, a county—are in other aspects of governance, what other employees have to get, what the increases in insurance, utilities and all the other things that go into making up a budget represent. So he does have to take that into consideration. It becomes a more complicated process."

It is probable that in every state with a cap law, the government entity will attempt to point out the spending-limit constraints. Under *Irvington,* the arbitrator has to consider the entity's cap situation before rendering his decision. Although he is not automatically bound by its percentage limitations, his

decision must be reasonable in light of statutory factors. I think it will be a troublesome area for arbitrators. For example, in many states the spending limitation is determined by the growth in the state's economy or the growth in personal income.[3] If there is no growth as measured by these indicators, can an arbitrator award pay raises and still have his decision considered reasonable? This is more likely to become a problem in California because that state's spending limit is tied in part to increases in population, and some cities have been losing population.

One thing is clear, however. Each arbitrator in a cap-law jurisdiction will have to learn the mechanics of the law. He must know how the cap is calculated, how much has been committed to non-collective-bargaining expenditures, and how much remains for collective bargaining costs. While that may sound simple, in practice it is not. Hawaii underwent its first collective bargaining negotiation under the state's cap law which limits increases in general-fund expenditures to the growth in personal income. Ted Tsukiyama and I served as fact-finders as part of the dispute-resolution process. The state government argued that the spending ceiling limited the amount of their offer. To gauge the true impact of the ceiling, however, it was necessary to focus only on general-fund expenditures. Since many employees were paid by special funds or by federal funds, a separate cost accounting was required. In Hawaii, the governor is required to submit a budget which complies with the spending ceiling. Since that budget would include the negotiated collective bargaining costs, we found ourselves reviewing his budget to find the true constraints. Since the legislature was already in session, it had in the meantime made significant changes in the governor's budget, so it was difficult to get a true reading of what the allocation was.

Our experience is not unique. In another case in New Jersey,[4] an arbitrator had to consider the effect on the cap limit of a shortfall of $1.1 million in anticipated collection of delinquent taxes. All of these technical issues, when raised, have to be considered by the arbitrator in order to meet the standard set forth under *Irvington.* Thus, in addition to issues which all arbitrators are familiar with, such as the inflation rate, comparative pay in other jurisdictions, and the U.S. Department of Labor's

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[3]Austermann, *The Tax Revolt Transformed,* State Legislatures, July–August 1980.

[4]*New Jersey State Policemen's Benevolent Assn.* v. *City of East Orange,* 164 N.J. Super 436 (1978).

typical-family-of-four statistics, the arbitrator now has a whole new technical and factual topic to consider.

The constraints imposed by these cap laws are alleviated where the legislative body has the power to approve or reject arbitrated or negotiated agreements. For example, in Hawaii the state legislature and the county councils retain that right and, as a result, can review the cost of the agreement in light of other government expenditures and the spending limit. All state legislatures have retained the power to approve or reject state collective bargaining agreements.[5] However, that right is not granted to all county or municipal governments. In those cases the arbitrator has broad authority to determine the fiscal priorities of a city since his award must be funded. I don't know which is the better solution. Where the legislative body retains the right to approve or reject, the arbitrator's decision is clearly not final and may be rejected, as it was in Hawaii in 1979. Where the arbitrator's award is not subject to legislative approval, I expect more court challenges of the awards when municipal officials are faced with a large award that utilizes most, if not all, of the allowable increases.

In addition to the passage of cap laws, the taxpayers' concern over government spending has also resulted in laws that limit or more narrowly define the role of the arbitrator in public collective bargaining. Some of these laws are subtle, such as final-offer arbitration or residency requirements for arbitrators. But there also are more direct ones. For example, the Financial Emergency Act for the City of New York, in recognition of the large salary increases granted employees previously, required arbitration awards rendered pursuant to the city's collective bargaining law to consider and give "substantial weight" to the city's financial ability to pay such increases without requiring increases in the level of city taxes existing at the commencement of arbitration proceedings.[6] In addition, it created the Emergency Financial Control Board which could return awards to the negotiators if the parties had not demonstrated that the agreement was in compliance with wage guidelines.[7]

I also came across a Massachusetts statute which, under certain conditions, limits to 50 percent the amount of contributions

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[5] *See Minnesota Ed. Assn.* v. *State of Minnesota,* 103 LRRM 2195, 2197 (1979).

[6] *See De Molia* v. *State of New York,* 100 LRRM 2625 (1978).

[7] Anderson, *Local Government-Bargaining and the Fiscal Crisis: Money, Unions, Politics and the Public Interest,* 27 Labor L.J. 512 (1976).

public employers may make to public employees' health insurance premiums.[8]

The New York compulsory arbitration law was amended in 1978 to require arbitrators not just to specify the basis of their findings, but to assign them weight. It also included a provision that the determination of the arbitration panel is subject to review by a court of competent jurisdiction. Citing the above changes, a New York court remanded for further consideration a three-member arbitration panel's decision which the court held did not elaborate sufficiently on its reasons for various contract proposals and thus did not meet the law's requirements.[9]

In summary, I believe the cap laws are here to stay and will probably be passed in more and more states. Public dissatisfaction with government taxes and services will remain high as long as the total tax burden keeps growing, and as long as we have persistent inflation combined with slow growth in personal income. Caps or ceilings provide the mechanism by which the taxpayer can gauge whether his elected officials are controlling growth in government. Whereas the calculation of the limit may be a technical exercise, the taxpayer need only ask, "Did they exceed the ceiling?"

Since salary costs represent a significant portion of any governmental entity's budget, these cap laws will have a pronounced impact on collective bargaining. Indeed, in the *Irvington* case, the town asserted that salaries and fringe benefits account for 75 percent of its overall budgetary appropriations.

If a jurisdiction has a cap law, that law will become a major item of discussion. How the cap law is calculated, how much has been allocated prior to bargaining, and how wage proposals affect the ceiling will be common issues. An arbitrator will have to know the answers to these questions in order to render a reasonable award. In addition to learning an entirely new area, the arbitrator will find his award more likely to be criticized if salary awards exceed the percentage growth for the budget as a whole. Concurrently, as taxpayers, concerned about government spending, see employee salary expenses rise faster than the percentage growth in the municipality as a whole, we will see

[8] *See School Comm. of Holyoke* v. *Duprey*, 102 LRRM 3007 (1979), and *Medford School Comm.* v. *LRC*, 103 LRRM 2059 (1979).

[9] *In the Matter of the Application of Buffalo Police Benevolent Assn.* v. *City of Buffalo, State of New York*, Supreme Court of Erie County (Sept. 30, 1980), as reported in 894 GERR 24.

more limitations and restrictions placed upon arbitrators. We have already seen a growing tendency to send arbitration awards to court for review. If the trend continues unabated, there may come a time when interest arbitration no longer provides finality and the process is so cumbersome that its utilization will diminish in the public sector.

I hope that the foregoing has laid out the current trends and the problems that lie on the horizon.