

AMERICAN ARBITRATION ASSOCIATION

In the Matter of Arbitration Between:

Metropolitan District Commission

and

Materials Innovation and Recycling Authority, formerly Connecticut Resource Recovery  
Authority

**RULING ON LIABILITY**

For a detailed background of this ongoing dispute between these parties, which has reached epic proportions, reference is made to two previous arbitration awards (the so-called Eagan Panel Award dated May 19, 2000 and the Hodgson Panel Award dated July 29, 2005) and to a Memorandum of Decision by Judge Aurigemma of the Connecticut Superior Court in *MDC v. CRRA* dated August 8, 2011-Docket No.: CV-10-6016708-S.

The current dispute, like the others, arises out of an October 1984 contract between the parties for the operation of the MidConn facility. The facility and the contract are described below. This dispute is over liability under the contract between the parties for pension costs, health costs, unemployment compensation costs, increased unemployment compensation contribution costs caused by termination layoffs, costs relating to job transfers, health insurance benefit costs and various other employee benefit and operation related costs, all of which MDC claims should have been reasonably anticipated upon the expiration of the October, 1984 agreement between the parties which occurred on December 31, 2011. MDC claims that all of these costs are the responsibility of CRRA.

CRRA has denied that it is responsible for nearly all of these costs, claiming that they are the sole responsibility of MDC, and has refused to make any payments to MDC for the costs that MDC has billed to CRRA.

Reference is made to MDC's Petition for Relief in its Amended Claim For Arbitration in this matter dated January 16, 2013.

By agreement of the parties, approved by the panel, the arbitration is bifurcated into liability and damages. This award concerns the liability phase only. It follows lengthy presentations of evidence and extensive and detailed written submissions. Both sides have been represented by very able and well-prepared counsel.

### **The Parties**

The Metropolitan District Council is a public non-profit municipal corporation created by the General Assembly in 1929 to provide quality potable water and sewer systems for people and businesses in the Hartford area. It has eight member towns. The Connecticut Resource Recovery Authority was created in 1973 for the purpose of developing economically sound, environmentally responsible solutions for managing the state's solid waste. Its MidConn facility, which is the subject of this dispute, served some 70 towns in central Connecticut. On June 6, 2014, the Materials Innovation and Recycling Authority ("MIRA") was established by Public Act 14-94 as the successor authority to CRRA. As of that date, MIRA assumed control of all of CRRA's assets, rights, duties and obligations. Because the events that are the subject of this arbitration occurred before MIRA was created, this award typically refers to CRRA when describing the relevant events but to MIRA when noting arguments made and positions taken.

The MidConn facility that is the subject of this arbitration is primarily a solid waste disposal and recycling facility located in Hartford. It operates by accepting trash from member towns and private haulers, burning the trash to generate steam, and then selling the steam to The

Connecticut Light and Power Company, which CL&P uses to generate electricity. MDC's role was to operate the plant and, for a period of time, to provide other services such as landfill operation, transfer station operation and trash hauling. CRRA's decision to remove MDC from functions other than plant operations was the subject of an earlier arbitration.

The dispute between the parties primarily concerns whether the costs for which MDC seeks payment are recoverable under the contract. (MIRA has also raised equitable defenses including waiver and estoppel.) We will address below each of the categories of claimed costs: 1) what are called OPEB (other post-employment benefits, chiefly medical payments for retirees and their families); 2) pension benefits; 3) severance payments and similar costs for employees who had worked at the MidConn project; and 4) other expenses related to termination, such as defense of employee claims alleging unlawful treatment. Preliminarily, we address the parties' conflicting interpretations of the contract.

### **The Budget Process**

Much of the parties' disagreement focuses on the significance of the budget process. MIRA contends that it was MDC's duty to include its projected costs for each year in the annual budget it submitted to CRRA, and if MDC did not include a cost in the appropriate annual budget, it cannot recover. The contract language that MIRA principally identifies as creating this limitation is the requirement that "[t]he District shall prepare an Annual Budget" and "The Authority shall pay the District the actual cost of the services and materials provided. Such costs shall be defined and projected in the Annual Budget." To support its interpretation of this language, MIRA points to the context of the language and the role of the parties' agreement in the MidConn process.

The context that MIRA points to is the elaborate and detailed structure that the contract creates for the budget, including many categories and subcategories. In addition, the budget

process itself includes a timeline for submissions and a process for addressing unanticipated costs. MIRA also emphasizes the importance of accurate budget forecasting: CRRA set the price it charged the Towns for the waste they brought to the facility (the so-called “tip fee”) based in part on the costs it had budgeted to pay MDC to operate the plant. If CRRA had to pay costs outside the budget, it would have to pass these costs along to the towns in the form of a higher tip fee in a subsequent year. In this regard, CRRA also points to what it refers to as interlocking contracts: its contracts with CL&P and with the various towns all based charges on the annual budget to run the plant. Moreover, during the bonding process for funding construction of the plant, MDC’s representative represented that the budget would be controlled by the budget process. Therefore, CRRA contends, the contract did not contemplate that MDC could recover costs that it had initially omitted from its proposed annual budgets. Additionally, CRRA points to its contractual right to replace MDC as the contractor for particular functions; to exercise that right intelligently, CRRA says, it would need to know the costs involved as they were being incurred rather than learning of them only much later.

MDC responds that the contract does not preclude a later claim for costs that have for whatever reason been omitted from a given annual budget. MDC points out that the contract provides that “The Authority shall pay the District the actual cost of the services and materials provided” and reads the following sentence -- “Such costs shall be defined and projected in the Annual Budget” – as not limiting the preceding one. In that connection, MDC emphasizes a different theme of the contract negotiations and contract language: what MDC says was the understanding between the parties that, because MDC was making no profit on the contract, it should bear no risk of loss.

The panel concludes that to be collectible “actual costs” within the meaning of the contract, such costs must have been identified by MDC in its budget submissions to CRRA.

### **The Indemnification Provision**

MDC also points to the indemnification language in Article VIII as a potential source of recovery outside the budget process. Article VIII provides, in part, “The Authority shall indemnify, defend and hold harmless the District, its Commissions and Boards, employees and agents, its Successors or Assigns, as it is now or hereafter may be constituted from and against all liability...” MDC points as well to the succeeding sentence, which links MDC’s lack of profit potential to protection from risk: “It is the intent of this Article that the Authority shall hold the District fully harmless from any risk of any loss whatsoever in respect hereof, by reason of the absence of any economic interest of the District herein.” MDC interprets this indemnification provision as being broad enough to cover costs that might have been budgeted in an earlier year but were not included until a later year, based on the fact that it would have – and now says it does have – liability for costs that it might have but did not include in its proposed budgets for earlier years.

MIRA responds that the indemnification provision should not be read to override all the budgeting requirements that take up much of the contract. In support of its reading it points not only to the provisions described above but also to provisions such as those in the indemnification article discussing insurance (suggesting that indemnified risks would be at least principally insurable risks) and indemnification provisions elsewhere in the contract that would be unnecessary if the indemnification under Article VIII were broad enough to cover every cost MDC might incur.

The panel concludes that the indemnification Article does not extend to items that were properly part of the ordinary budgeting process.

## **The Release**

After the July 29, 2005 arbitration award by the panel chaired by Judge Hodgson, the parties negotiated a series of issues. These negotiations culminated in an agreement to modify the contract in certain respects. As part of the negotiations, in December 2006 MDC executed a release of all claims it had against CRRA, with the exception of any “charges for services provided during the year 2006.” The agreement also provided that “the duty of CRRA to indemnify the MDC in accordance with the terms of Article VIII of the amended agreement is not released by this agreement.” As we have concluded above, however, the indemnification provisions of the contract do not apply to items that were properly part of the ordinary budgeting process.

We now turn to the specific categories of claimed damages.

## **Retiree Medical Costs**

The parties’ dispute concerning responsibility for retiree medical costs is based in part on their course of dealing. MIRA points to an October 1991 letter from Richard Ludwig, then MDC’s Manager of Solid Waste, to Paul Mazzaccaro, then CRRA’s Project Manager for the MidConn project. Mr. Ludwig was responding to Mr. Mazzaccaro’s request for clarification of “how accrued time and other benefits get charged when a long-term MDC water and/or sewer employee transfers to the Mid-Connecticut Project and then retires after a few years.” Mr. Ludwig responded that there were at that time two such employees and said that their “accrued time upon retirement” was charged to MidConn, while “[a]ll benefits including [all medical categories] are presently being paid by the District” and “noted that the accrued time for employees who have worked at the Mid-Connecticut Project and posted out and retire while at another District function will be charged to the function they were in when retired.” CRRA concedes that retiree medical expenses are an “Employee Benefit[ ]” that is an “[e]xample of [a]

[c]ompensable [i]tem[]” under Exhibit G of the contract, but contends that the parties excluded this item when implementing the contract, making it no longer compensable. MIRA also points to what it considers persuasive evidence that MDC did not seek to recover retiree medical costs until late in the life of the contract.

MDC responds that it did, in fact, submit and recover payment for retiree medical expenses. The weight of the evidence, however, is that these expenses were not submitted until late in the life of the contract. More persuasively, MDC contends that the 1991 letter could not operate to amend the contract because Article X requires amendments to be in writing (and MIRA does not claim that the letter is an amendment); that it could not be the kind of “course of dealing” that sheds light on the intent of the contracting parties since it did not involve anyone who participated in the drafting of the contract and did not occur until seven years after the contract was executed; and that in any case neither Mr. Ludwig nor Mr. Mazzaccaro was authorized to bind their principals into the future. The panel concludes that the parties’ course of dealing did not operate to relieve CRRA from all responsibility for retiree medical costs. However, as we now explain, MDC’s recovery for retiree medical expenses is limited by the limited extent to which it included retiree medical expenses in the annual budgets.

The cost of medical services for retirees was never included by MDC in the budget it submitted to CRRA every year until the 2008-2009 fiscal year, and then only as part of the “MDC Contract Separation Costs.” The 2009-2010 fiscal year budget again included a lump sum for “potential termination costs” including “unfunded other post employment benefit (OPEBs) expenses.”

The first time retiree medical costs appear as a separate line item is in the MDC budget for fiscal year 2010-2011 in the amount of \$350,000. In the 2011 stub period budget, the retiree medical costs were again included in the “MDC Contract Separation Costs.”



Whether MDC failed to include retiree medical costs in any form in earlier budgets because of the so-called “Ludwig letter agreement,” *see supra*, or because of mere oversight by MDC, is not really relevant. The panel concludes, after consideration of all the evidence on this issue, MDC should recover its actual costs incurred during the 2008-2009 and 2009-2010 budgetary periods for retirees from the MidConn project (and their spouses/dependents as may be provided in the applicable collective bargaining agreements). For the 2010-2011 and July-December 2011 budgetary periods, MDC should recover its actual medical costs incurred for MidConn retirees as well as future reimbursable medical costs (as defined in the applicable collective bargaining agreements) incurred by those MDC employees who retired from the MidConn facility between July 1, 2010 and December 30, 2011.

In the damage phase of these proceedings, the panel will hear evidence on the quantification of that past liability, measured by actual costs incurred by MDC, as well as the future liability, whether measured by actual reimbursement, insurance cost, lump sum present value, or otherwise.

### **Pension Costs**

The claim for pension costs in some ways resembles the claim for retiree medical costs, but there are distinctions that make differences in treatment appropriate. Both involve claims for benefits earned during the contract but payable after its expiration. However the post-contract pension costs, unlike the retiree medical costs, were projected all during the course of the contract. The dispute concerning pension costs arises from the fact that MDC neither fully funded its future pension obligations nor made provisions to have done so by the expiration of the contract. Instead, until late in the day it amortized its unfunded pension obligations over a period, typically 20 years, that extended well past the expiration of the contract. It only began fitting the amortization period to the contract duration when there were three years left to go in



the contract, proposing amortization periods of three years, then two, then one. This truncation of the amortization period multiplied by severalfold the funding necessary to amortize the unfunded pension liability. MDC is not entitled to recover this entire amount of unfunded liability because much of it is properly considered to be costs for which reimbursement should have been sought, if at all, during prior years.

That said, however, while the Contract may not permit MDC to recover the greatly enhanced pension fund contributions it claims for the fiscal years 2009-2010, 2010-2011 and July through December 2011, there is no question that MDC did: 1) include pension fund contributions as a line item in its proposed budget for each of those fiscal periods, and 2) incur -- and presumably pay -- some pension fund obligations for those time periods for the employees working at the MidConn facility. Fairness -- as well as CRRA's contractual obligation to reimburse MDC for its actual costs included in the annual budget -- dictates that MDC recover those costs.

An examination of the total pension contributions for the preceding fiscal years of 2006-2007; 2007-2008; and 2008-2009 reveals the average pension contributions for all MidConn employees, using the extended amortization period, was approximately \$578,000. Further, the evidence indicates that for the 2009-2010 fiscal year, MDC's actual contribution to the pension fund for the MidConn facility employees was not the \$3.1 million included in that year's budget but instead some payment substantially less. Accordingly, in the damage phase of this arbitration, the panel would entertain evidence as to what CRRA's pension fund contributions would have been for the period July 1, 2009 through December 30, 2011 had there been no change in the amortization period, and what contribution MDC actually made to the pension fund for those employees assigned to the MidConn facility during that time period, which has not been reimbursed by CRRA. It appears from the budgets and other evidence that those amounts

would be between \$500,000 and \$700,000 each year. That would be the limit of MDC's recovery on this claim item; CRRA is not liable for any under-funding of MDC's pension obligations or any increased contributions resulting from truncating the amortization period.

Additionally, though MDC's decision to switch its amortization period as the contract was nearing its end appears to have been insufficiently justified because MDC knew all along that the contract had a finite duration and might not be extended, a more justifiable triggering event did occur near the end of the contract. On December 16, 2010, the CRRA board voted not to renew the contract and instead to retain another organization, NAES, to operate the MidConn plant. It was at that point that MDC truly was in a different position from where it had been before, justifying a change in treatment of pension liabilities. In addition to the liabilities described in the preceding paragraph, therefore, CRRA is liable for the past and future pension benefits payable (as defined in the applicable collective bargaining agreements) to those MDC employees who retired from the MidConn facility between December 16, 2010 and December 30, 2011 only. In the damage phase of these proceedings, the panel will hear evidence on the quantification of that liability.

#### **Contract Termination Costs**

MDC claims it is entitled to recover certain personnel costs incurred as a result of the Contract's conclusion on December 30, 2011, including those relating to unemployment compensation, separation pay for unused earned vacation, personal time and sick time, labor relations disputes, layoff / reassignment claims, and the like. These apparently fall under the rubric "MDC Contract Separation Costs," which MDC first included in its 2008-2009 annual budget.

The finite length of the Contract was obvious at the time it was executed, and so both parties knew there might come a day when the employees MDC had assigned to the MidConn

facility would come back to MDC looking for positions in its water and sewer operations, and all the personnel costs associated with that dislocation would then be confronted. That day of reckoning occurred, of course, in December 2011, and, in anticipation of that, MDC began in 2008 to put into its annual budget a line item for “MDC Contract Separation Costs.” In the narrative section of that budget, MDC explained that sum “has been budgeted to start accruing for liabilities (such as unfunded other post retirement expenses and unfunded pension liability) associated with the termination of the MDC/CRRA agreement on December 31, 2011. These separation costs are currently estimated at approximately \$12.2 million.” In the 2008-2009 budget, \$3 million was included for these items; in the 2009-2010 budget, \$8.3 million was included; in the 2010-2011 budget the number was \$12.8 million, and for the stub period budget it was \$39.6 million.

The evidence suggests that there were, in fact, certain personnel costs in the nature of severance and dislocation expenses that were incurred by MDC, presumably as a result of its employees who had been assigned to the MidConn facility but could not be reabsorbed into MDC’s workforce for its water and sewer operations in their previous or similar positions when the contract ended. MDC should be allowed to recover such expenses actually incurred for such employees, but only to include severance payouts for unused sick and vacation time; unemployment compensation; COBRA; early retirement costs; outstanding workers’ and so-called “red circle” claims, if any. In addition, MDC should recover its claim for debt service on the vehicle maintenance facility and payment of the outstanding workers’ compensation claim, both of which we understand from the evidence CRRA accepts. During the damage phase, the panel will entertain evidence limited to those termination costs only. MDC does not have a right under the Contract to recover costs of labor relations disputes, discrimination claims, litigation defense costs, or the like.

## CONCLUSION

The parties are directed to meet and confer concerning the analysis and computation of damages. To the extent there are disagreements, the parties are encouraged to attempt to mediate them. The parties shall jointly report to the panel in writing no later than 60 days following receipt of this Award concerning the status of their discussions. Thereafter, the panel and the parties will meet to discuss what further proceedings, if any, are necessary.

SO ORDERED:



Honorable Alan H. Nevas

Date: 8/20/15



David N. Rosen

Date: 8/21/15



Louis R. Pope

Date: 8/21/15