

**ATTACHMENT E**  
**THE PROPOSED DECISION**

BEFORE THE  
BOARD OF ADMINISTRATION  
CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM  
STATE OF CALIFORNIA

In the Matter of the Appeal of:

JOSEPH M. TANNER,

Respondent,

and

CITY OF VALLEJO,

Respondent.

CalPERS Case No. 9796

OAH No. 2011060337

**PROPOSED DECISION**

This matter was heard before Administrative Law Judge Dian M. Vorters, State of California, Office of Administrative Hearings (OAH), on November 2, 3, and 4, 2011; March 26, 27, 28, 29; and May 22, 23, and 24, 2012, in Sacramento, California.

Jeffrey R. Rieger,<sup>1</sup> Attorney at Law, represented the petitioner California Public Employees' Retirement System (CalPERS).

John M. Jensen,<sup>2</sup> Attorney at Law, represented Joseph M. Tanner (respondent), who was present.

Sabrina L. Thomas,<sup>3</sup> Attorney at Law, represented the City of Vallejo (Vallejo).

Evidence was received and the record remained open for parties to submit written closing arguments. Three subsequent requests for extensions to file briefs were granted. On or about July 26, 2012, OAH received respondent's Motion for Official and Judicial Notice, Post Hearing Brief, and Renewal and Amended Motion for Jurisdictional Challenge Post Hearing which were marked as Exhibits ZZ, AAA, and BBB, respectively. On August 31,

<sup>1</sup> Jeffrey R. Rieger, Attorney at Law, Reed Smith LLP, 101 Second Street, Suite 1800, San Francisco, California 94105.

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<sup>3</sup> Sabrina L. Thomas, Attorney at Law, Renne Sloan Holtzman Sakai, LLP, 428 J Street, Suite 400, Sacramento, California 95814.

PUBLIC EMPLOYEES RETIREMENT SYSTEM

FILED

November 30, 2012

*Rathie K. Sabert*

2012, OAH received CalPERS' Request for Official Notice, Closing Brief and Opposition to Respondent's Jurisdictional Motion, which were marked as Exhibits 51 and 52. On September 5, 2012, OAH received CalPERS' Errata to Closing Brief which was marked as Exhibit 53. On October 16, 2012, OAH received respondent's Final Post-Hearing Brief, Final Renewed Motion for Jurisdictional Challenge Post Hearing, and Final Request for Judicial Notice.<sup>4</sup> These briefs were marked as Exhibits CCC, DDD, and EEE, respectively. The record closed on October 19, 2012.

## ISSUE

Whether CalPERS correctly excluded the value of certain components of respondent's pay that Vallejo had converted into payrate, as non-compliant with the Public Employees' Retirement Law (PERL) for purposes of calculating respondent's final compensation and retirement allowance?

## FACTUAL FINDINGS

1. The Statement of Issues was made and filed on May 24, 2011, by Marion Montez, Assistant Division Chief, Customer Account Services Division, CalPERS, in her official capacity.

2. Vallejo, as is expressly authorized by the Vallejo City Charter, is a contracting agency with CalPERS. (Charter, §§ 202, 807.) Vallejo contracted with the CalPERS Board of Administration to participate as a public agency member for administration of employee retirement benefits. The provisions for local public agencies contracting with CalPERS are set forth in the PERL. (Gov. Code, § 20460 et seq.)

3. Respondent is a retired member of CalPERS. His last qualifying employment was as City Manager of Vallejo. The City Manager functions as the chief executive officer of the city and is responsible to the City Council for the proper administration of the city's affairs and all duties as set forth in the city charter. Respondent was employed by Vallejo in this capacity from January 8, 2007 through June 1, 2009 (separation date).

Respondent's prior employment included City Manager of Pacifica, Redevelopment Consultant for the City of Alameda, Assistant City Manager for the City of Alameda, City Manager of Pleasant Hill, City Manager of Emeryville, and City Manager of Galt. By virtue of this employment (with the exception of his time as a Redevelopment Consultant), respondent was a miscellaneous member of CalPERS subject to the provisions of the PERL.

4. Respondent's date of retirement from all CalPERS contracting employers was June 2, 2009. His employment with Vallejo was effected under two contracts: the first "entered into on November 16, 2006" (November 2006 Contract or Initial Agreement) and the second "entered into as of March 8, 2007" (March 2007 Contract or Second

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<sup>4</sup> All requests for Official and Judicial Notice were granted pursuant to the provisions of Evidence Code sections 452, 453, and 454; and Government Code section 11515.

Agreement). It is noted that the March 2007 Contract was not signed by the parties (respondent and Mayor Anthony Intintoli) until May 8, 2009.

*Pre-Employment Contract Negotiations*

5. While still employed as City Manager at Pacifica, sometime prior to November 2006, respondent was contacted by William Avery, President of William Avery & Associates, Inc., an Executive Search and Labor Relations consulting firm.<sup>5</sup> During their discussion of compensation, respondent told Mr. Avery that he “desired a substantially higher salary than the salary Vallejo was initially offering.” Respondent expressed that the salary he sought was “higher than salaries of other Vallejo management-level employees and the predecessor Vallejo City Manager.” Respondent expressed that it would be difficult for the City Council to approve the salary he wanted. Respondent suggested that the City Council might be able to approve a compensation package that consisted of base salary and additional forms of compensation such as an auto allowance or deferred compensation contributions. The total compensation package could “later be converted to base salary after he finished a short period as Vallejo’s ‘interim’ City Manager.”

According to Mr. Avery’s statement, Vallejo had not engaged him to assist in locating an “interim” City Manager and during his discussions with respondent, he understood respondent to be seeking a regular position, not an “interim” position. Mr. Avery was not involved in contact negotiations after Vallejo selected respondent as a candidate for the position.

6. Respondent testified that he told Mr. Avery that he needed \$300,000 in “PERSable” income to move to Vallejo from Pacifica. Mr. Avery told respondent he would “get back to me.” Respondent subsequently met in closed session with the full City Council. John Thompson, the City’s Interim City Manager, negotiated respondent’s contract. Respondent also told Mr. Thompson that he required \$300,000 in “PERSable income.” Mr. Thompson conveyed that it “might be doable” and he would talk to the City Council to see if they were still interested in hiring him.

7. In the interim, Mr. Thompson began working on contract language with respondent. The contract provided for a term of employment of 36 months, “commencing on January 8, 2007, and continuing until January 7, 2010.” The Initial Agreement provided for an interim starting period as follows:

The City Manager shall initially be hired as a limited term employee and shall not be enrolled in [CalPERS]. On or before March 8, 2007, the City Manager shall become a permanent employee and be reinstated in PERS. (Exh. 6.)

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<sup>5</sup> Mr. Avery submitted two affidavits signed under penalty of perjury on June 18, 2011, and October 28, 2011, regarding his interaction with respondent.

8. At hearing, respondent articulated three reasons for insisting that he start as an “interim” City Manager. He stated that to collect his retirement benefit from the City of Pacifica, he had to retire from the Public Agency Retirement System (PARS), which is separate from CalPERS. PARS had recommended that respondent remain retired for 60 days after leaving his position in Pacifica. He also stated that Vallejo had a “horrible reputation” regarding its dealings with City Managers and this would give him time to ascertain if he wanted to stay. Finally, he wanted to be sure that his \$300,000 PERSable salary demand was carried forth. Respondent and Mr. Thompson “brainstormed” on how to achieve this salary. Respondent stated that he did not care how it was divided up, as long as the total was “\$300,000 PERSable.”

9. *Limited Term Employee v. Retired Annuitant.* Dennis Morris, Vallejo Human Resources Director (2005 to 2008), testified that an “Interim City Manager” works in that capacity only until the City obtains a “replacement.” The position is so important that they need someone in that “spot” during transition. Carlous Johnson, CalPERS Analyst, also testified that the term “limited term employee” normally means that an individual is going to perform those duties for a little while and then someone else will take over the job. A limited term employee can be enrolled in CalPERS.

Mr. Morris defined the term “retired annuitant” as someone who has retired and is collecting a retirement benefit from PERS, but still allowed to work. Their hours are limited under the PERL and carefully monitored by Vallejo.<sup>6</sup> (Gov. Code, § 21224.) Mr. Johnson testified that a retired annuitant’s income cannot be reported to CalPERS until they are reinstated into membership.

Respondent’s Initial Agreement did not use the term “retired annuitant,” it used the term “limited term employee.” The reason was explained in the contract itself; “the employee ...shall not be enrolled in the CalPERS” until March 8, 2007. There was a decision made by respondent to delay reinstatement. However, his PERS status during the first 60 days was separate and unrelated to the contract term of “36 months commencing on January 8, 2007, and continuing until January 7, 2010 (the initial ‘Termination Date’).”

10. *Approval of Respondent’s November 2006 Contract.* On November 14, 2006, the Vallejo City Council held a “special meeting in closed session” to address the hiring of a City Manager. (Gov. Code, § 54957.) Respondent was not present. On that date he received a call from Mr. Thompson stating that the City Council had approved a lower salary than respondent had requested. Respondent rejected the offer.

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<sup>6</sup> “A retired person may serve without reinstatement from retirement or interruption of benefits ... upon temporary appointment by the ...public agency employer... These appointments shall not exceed a total for all employers of 960 hours in any fiscal year, and the rate of pay for the employment shall not be less than the minimum, nor exceed that paid by the employer to any other employees performing comparable duties.” (Gov. Code, § 21224.)

Negotiations continued and an agreement was reached. On November 16, 2006, Mr. Thompson sent a Council Communication to Mayor Intintoli and members of the City Council stating that the Council had “completed its City Manager recruitment process and, in closed session on November 14, 2006, directed staff to convene a special session to approve respondent’s employment agreement.” A copy of the Initial Agreement was attached to the Communication which cited respondent’s “abundant experience as a City Manager in California in all aspects of municipal government.” Respondent’s start date was “January 8, 2007, for an initial term of three years and a starting base salary of \$216,000.” On November 16, 2006, the Council convened a “special meeting” and appointed respondent as City Manager by simple motion. The November 2006 Contract was signed by respondent, Mayor Intintoli, City Attorney Fred Soley, and the City Clerk (signature date unknown).

*CalPERS Identification of Issues with November 2006 Employment Agreement*

11. As respondent understood the November 2006 Contract, it provided him with “\$300,000 of PERSable income.” He testified that he knew it would have to be amended because of “management incentive pay and EPMC.”<sup>7</sup> He testified that “sooner or later we wanted CalPERS to bless this contract,” meaning “approve it.” Respondent started working for Vallejo on or about January 6, 2007.

12. *CalPERS January 26, 2007 Letter.* Debora Boutte, Vallejo Human Resources Manager, forwarded the November 2006 Contract to CalPERS. Carlous Johnson, Compensation Review Unit Analyst, reviewed the contract for compliance with the PERL. Mr. Johnson identified several problems with the contract and sent a letter dated January 26, 2007, to Ms. Boutte. The letter outlined provisions of respondent’s November 2006 Contract that were in conflict with the PERL.

a. Under “Compensation/PERS,” the contract stated:

The City contracts with the [CalPERS] for retirement benefits. The City will pay both the City’s share and the City Manager’s share for participation in the Public Employees’ Retirement System, or at the City’s option, the percentage contribution for the City Manager’s share shall be converted to base salary. While City Manager is not a PERS member, an equivalent benefit shall be paid by the City as deferred compensation.

b. Under “Compensation/Leave Allowance,” the contract stated:

(a) The City Manager shall be given 240 hours of annual leave credit effective upon the execution of this Agreement. The City Manager shall then begin accruing annual leave at a rate of 240 hours per year. Annually, on or before December 31 of any year, City Manager

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<sup>7</sup> Employer Paid Member Contributions (EPMC)

shall be allowed to sell back to the City up to 120 hours of accrued annual leave.

(b) The City Manager shall be entitled to 30 days of management leave per year, which shall be paid as salary.

c. Under "Compensation/Automobile," the contract stated:

The City Manager shall be provided a monthly automobile allowance of \$600 in exchange for making a vehicle available for the City Manager's own use and for City-related business and/or functions during, before and after normal work hours....This benefit shall be converted to base salary after March 8, 2007, after which the City Manager will be responsible for his own costs for use of his personal vehicle when on City business.

d. Under "Compensation/Deferred Compensation," the contract stated:

Section 457 Plan. The City will make, in equal proportionate amounts each pay period, an annual contribution equal to 15% of base salary for either a Section 457 or 401(a) deferred compensation plan. The City shall convert this benefit to base salary upon reinstatement to PERS and this benefit shall terminate.

e. Under "Separation/," the contract stated:

In the event the City Manager is terminated by the City Council during such time that the City Manager is willing and able to perform the City Manager's duties under this Agreement, then in that event the City agrees to pay the City Manager a lump sum cash payment equal to twelve months' base salary plus City-paid PERS contribution then in effect as provided in 4.A(1) and (2) above.

13. Mr. Johnson's January 26, 2007 letter cited Government Code section 20636, which defines reportable compensation and payrate. (Gov. Code, § 20636, subs. (a) & (b)(1).) His letter explained that respondent's beginning salary of \$216,000 qualified as reportable compensation. However, the statute did "not allow for converting additional compensation into base pay or adding non-reportable compensation to base pay for retirement purposes." Specifically, "payments such as management leave credits; automobile allowance; and deferred compensation should not be converted to salary and reported to CalPERS for retirement purposes."

Mr. Johnson's letter further explained that the value of EPMC and management incentive pay can be reported, but contract provisions must be implemented in accordance with regulations. (Cal. Code Regs., tit. 2, § 571.) For EPMC, Vallejo was required to adopt a resolution for a "group or class" of employees, such as "At Will Executive Staff." Mr. Johnson wrote, "The contract could be amended to reflect this provision."

Mr. Johnson noted that Vallejo already provided management incentive pay to other management staff amounting to 120 hours per year at their hourly rate. However, regulations did not allow employees to be granted an "option of either taking time off or receiving pay." Mr. Johnson wrote: "Therefore, in order for the City Manger's 'sell back of 120 hours of accrued leave' to qualify as management incentive pay, the option of time off or receiving cash payment must be taken out of the Managers contract and replaced by a ...clause similar to that found in the City's Memorandum of Understanding (MOU) for other management staff."

Finally, Mr. Johnson's letter stated that severance pay is considered "final settlement pay" and is not reportable to CalPERS for retirement purposes. He cited the applicable regulation which provides that "Final Settlement Pay may take the form of any item of special compensation not listed on Section 571. It may also take the form of a bonus, retroactive adjustment to payrate, conversion of special compensation to pay rate, or any other method of payroll reported to PERS." (Cal. Code Regs., tit. 2, § 570.)

14. Respondent testified that when Mr. Morris showed him the CalPERS' letter, he handed it back and said, "fix it." Mr. Morris responded, "We will talk to them," and reassured respondent that "we will fix this." Ms. Boutte, told respondent she was working on the issue with Mr. Johnson. Respondent also spoke to Mayor Intintoli, and several council members including Jerry Davis, and Tom Bartee on the issue. Respondent testified that the context of these conversations was, "We need to amend the contract to make my salary PERSable."

In respondent's opinion, he was a "retired annuitant" and his retired annuitant contract was "none of PERS' business" because CalPERS lacked jurisdiction unless he was a permanent employee. Respondent's November 2006 Contract did not state that he was a retired annuitant. It stated that he would begin as a "limited-term employee." According to Mr. Johnson, "limited term employees" can enroll in CalPERS. Further, this contract purported to cover both periods: his initial limited-term status through March 7, 2007, and his remaining permanent employee/reinstated status through January 7, 2010. As such, the November 2006 Contract was CalPERS' "business."

15. *Employer Paid Member Contributions (EPMC)*. Following Mr. Johnson's January 26, 2007 letter, he and Ms. Boutte communicated in writing and by phone on numerous occasions about the EPMC benefit. Monthly member contributions to CalPERS fund the retirement system. (Gov. Code, § 20053.) Vallejo employees paid nine percent of salary as their retirement contribution. Respondent's share of the contribution was eight percent with Vallejo paying one percent. As a benefit, an employer may offer to pay the employee's share of contributions and that value can included as reportable compensation.

However, the employer's share, in respondent's case one percent, is not reportable and cannot be converted into a member's base salary. By email dated March 15, 2007, Mr. Johnson reiterated to Ms. Boutte, "You can only report the value of the Employee's contributions. The extra 1% is the employer's portion. So the contract should read 8%, and the resolution should only show 8%. Have a great day."

Further, the EPMC benefit must be "available to all employees in the group or class, and one employee alone is not considered a group or class. (Gov. Code, § 20636, subd. (e)(1); Cal. Code Regs., tit. 2, § 571, subd. (a).) Since the City Manager was not part of a group or class, Mr. Johnson worked with Ms. Boutte to create a class of two. By letter dated March 8, 2007, CalPERS authorized Vallejo to report the value of EPMC for the "new City Manager and the City Attorney" as a group or class of Vallejo employees apart from the rest of the executive management group. This group would be called the "Council Appointed Executive Staff" because unlike other executives, they had independent contracts and were hired by the Board of Directors.<sup>8</sup>

#### *Respondent's March 8, 2007 Employment Agreement*

16. Vallejo Human Resources subsequently drafted a Second Agreement "entered into as of March 8, 2007" which "supercedes the November 18, 2007 Agreement." (Exh. 14.) Material changes included the new base salary that went from \$216,000 to \$305,844 annually, and the contract term of "36 months commencing on March 8, 2007, and continuing until March 8, 2010, (the initial 'Termination Date')."

The Second Agreement dealt with EPMC as follows: "The City contracts with CalPERS for retirement benefits. The City will pay both the City's share and the City Manager's share for participation in CalPERS which is also reportable as EPMC as outlined in Resolution 07-70 N.C." Omitted was language referring to conversion of the \$600 monthly car allowance to base salary, conversion of deferred compensation to base salary, 30 days of management leave to be paid as salary, and the employee's option to sell back 120 hours of accrued annual leave. The provision referring to the payment of 12 months severance pay was amended to add: "which is not reportable to CalPERS."

17. In February 2007, Ms. Boutte gave the Second Agreement to respondent for his review. Copies were also disseminated to City Council members. It was respondent's understanding that the difference between the two contracts was that "my salary was \$300,000, which I had demanded from my first conversation with the head hunter." Respondent asked Ms. Boutte and Mr. Morris if CalPERS was "okay" with the Second Agreement and they assured him that it was. It is noted that at this time, the Second Agreement had not been forwarded to CalPERS for review. Also, this Second Agreement was never "okayed" by CalPERS as PERL compliant

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<sup>8</sup> Ms. Boutte took immediate steps to implement the creation of this new group and presented a resolution to the City Council (Resolution 07-70), for adoption on March 27, 2007.

18. *Approval of Second Agreement by City Council.* To become binding, the City Council had to pass a resolution authorizing the mayor to sign the Second Agreement. In accord with this process, Mr. Morris distributed a March 27, 2007 Council Communication to Mayor Intintoli and members of the City Council. The "Subject" of the Communication was: "Consideration of the First Amendment to the City Manager's Employment Agreement." Under "Background and Discussion," the memorandum stated:

Mr. Tanner has completed his interim appointment as outlined in his original employment agreement, effective March 7, 2007. It is now time to prepare the necessary documents to begin Mr. Tanner's regular full-time appointment as City Manager. The original employment agreement contains provisions specific to the CalPERS Law related to the appointment as City Manager. After review of said language, CalPERS has recommended that the contract be amended to reflect the proper language regarding any PERSable compensation.

There is no additional fiscal impact of amending the language of the employment agreement. The language changes will not affect any cost factors and therefore, the total cost of the original employment agreement will not change.

The Communication proposed that the Council: "Approve the Resolution to authorize the Mayor to amend the City Manger's Agreement to ensure it complies with CalPERS regulations."

19. *Resolutions.* Copies of two related Resolutions were attached to the March 27, 2007 Communication, both effective March 8, 2007.

- Resolution 07-70 authorized applying the EPMC benefit to employees in the "Council Appointed Executive Group."
- Resolution 07-68 "authorize[ed] the Mayor to amend the original employment agreement to comply with CalPERS regulations." Resolution 07-68 "FURTHER RESOLVED that the language amendment will not change the total cost of the original employment agreement."

20. *March 27, 2007 Council Meeting.* The City Council convened a regular meeting on March 27, 2007. Respondent was present at the regular meeting; the mayor was not as he was on vacation. The matter of respondent's Second Agreement was placed on the Consent Calendar with several other proposed actions. The Consent Calendar and Approval of Agenda specifically stated, "All matters are approved under one motion unless requested to be removed for discussion by a Councilmember, City Manager, or member of the public subject to a majority vote of the Council."

- Calendar item (E) addressed “Consideration of First Amendment to the City Manager’s Employment Agreement.” The description stated that CalPERS had reviewed respondent’s “original employment agreement” and “after review of said language, CalPERS has recommended that the contract be amended to reflect the proper language regarding any PERSable compensation.”
- Calendar item (F) appeared to address only the City Attorney’s performance based salary adjustment (Resolution No. 07-69), but also included Resolution 07-70 to provide EPMC benefits to the City Attorney and City Manager.

According to the Minutes for the March 27, 2007 Council meeting, the Council approved on the Consent Calendar without discussion, Resolution 07-68 authorizing the mayor to amend respondent’s employment agreement, and Resolution 07-70 authorizing Vallejo to “report and pay the value of EPMC for the Council Appointed Executive Group.”

21. As of May 8, 2007, the mayor still had not signed the Second Agreement. On that date, Ms. Boutte sent him a memorandum urging him to review and sign the amended contract. The memorandum reads in relevant part:

The Human Resources staff has amended the agreements to comply with said regulations without changing the total cost of the original employment agreements as outlined in the resolution. *The necessary amendments involved moving the additional costs of the car allowance, deferred compensation, management leave and 1% of the Employer Paid Retirement Contribution be added [sic] to the base versus being reported separately as additional pay.* This change resulted in the base salary going from \$216,000 to \$305,844. In compliance with Resolution #07-68, the total cost salary and all benefits remain the same. The enclosed cost analysis provides the sections of the old contract that were added to the base salary.

*(Italics added.)*

22. Ms. Boutte attached to her memorandum a cost analysis entitled “City Manager Salary Computation March 8, 2007” (Cost Analysis). The Cost Analysis breaks down the components of respondent’s compensation under the Second Agreement. It is not clear if the Council reviewed the Cost Analysis prior to passing the related resolutions.<sup>9</sup> A review of the Cost Analysis shows that Human Resources rolled or converted five items into respondent’s original base salary of \$216,000 in order to arrive at a new base salary of \$305,844, as follows:

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<sup>9</sup> The March 27, 2007 Council Communication which was distributed in advance of the vote on the two resolutions, lists under “Documents Available for Review” only one document: “Resolution authorizing Mayor to amend the original employment agreement for the City Manager as required by CalPERS.”

<b>Component</b>	<b>Monthly Compensation</b>	<b>Annual Compensation</b>
<b>Base salary</b>	<b>\$18,000</b>	<b>\$216,000</b>
<b>Automobile Allowance</b>	<b>600</b>	<b>7,200</b>
<b>Deferred Compensation</b>	<b>2,790</b>	<b>33,480</b>
<b>Mgt Leave-30 Days</b>	<b>2,468</b>	<b>29,617</b>
<b>EPMC-1% Employer</b>	<b>239</b>	<b>2,863</b>
<b>Annual Leave Cash Out (120 hours)</b>	<b>1,390</b>	<b>16,682</b>
<b>New Base Salary</b>	<b>25,487</b>	<b>305,842<sup>10</sup></b>

23. All five components converted into respondent's original base salary of \$216,000 were addressed in Mr. Johnson's January 26, 2007 letter to Ms. Boutte. Two components, EPMC and Management Incentive Pay, were identified as allowable if certain steps were taken. Specifically, EPMC was allowed subject to a resolution applying this benefit to a group or class. Management incentive pay was already provided to other management staff at 120 hours per year at their hourly rate of pay. And, since regulations did not allow "the option to sell back 120 hours of accredited leave," this would need to be removed from respondent's contract, and replaced with a clause similar to that found in the MOU for other management staff. (Factual Findings 12 & 13.)

Vallejo Human Resources appears to have simply ignored CalPERS' instructions. Resolution 07-68 is flawed in that it purported to "amend the original employment agreement to comply with the CalPERS regulations" and to incorporate "the necessary language changes as recommended by CalPERS." In fact, the amendments did not "comply with the CalPERS regulations" and were not "recommended by CalPERS." These misstatements appeared in key documents including Resolution 07-68, the March 27, 2007 Council Communication, the March 27, 2007 Council Agenda, Ms. Boutte's March 8, 2007 memorandum to the mayor, and Mayor Intintoli's May 8, 2007 memorandum to the Council (see below). As such, the mayor and Council members may have been uninformed when acting on the matter of respondent's compensation.

24. On or about May 8, 2007, respondent, Mayor Intintoli, City Attorney Soley, and the City Clerk signed the Second Agreement. On that same date, Mayor Intintoli sent a memorandum to the City Council regarding the "Status of City Manager's Agreement." The memorandum reads, in relevant part:

This memo serves as a status report of finalizing the City Manager's Agreement. In accordance with Resolution #07-68, on March 27, 2007, the counsel gave me the authority to amend the City Manager's Employment Agreement to comply with the regulations of CalPERS.

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<sup>10</sup> The Annual Compensation adds up to \$305,842; however, the Cost Analysis created by Ms. Boutte displays a total of \$305,844.

The Human Resources staff has amended the agreement to comply with said regulations without changing the total cost of the original employment agreement as outlined in the resolution. The necessary amendments involved moving the additional costs of the car allowance, deferred compensation, management leave and 1% of the Employer Paid Retirement Contribution be added to the base versus being reported separately as additional pay. This change resulted in going from \$216,000 to \$305,844. In compliance with Resolution #07-68, the total cost salary and all benefits remain the same...

The mayor attached to this memorandum, the Cost Analysis prepared by Ms. Boutte. There is no evidence that the mayor ever spoke to CalPERS directly. But, by this memorandum, the mayor sanctioned an invalid amendment as it was not possible to comply with CalPERS regulations and simultaneously increase respondent's base pay to \$305,844.

25. On March 8, 2007, respondent submitted his application for reinstatement from service retirement. CalPERS reinstated him effective March 8, 2007, allowing him to begin accruing service credit as a member employee.

#### *Respondent's Separation from Vallejo*

26. During the spring of 2007, details of respondent's contract became the subject of public scrutiny. Human Resources received many phone calls and public records requests. Articles covering respondent's salary appeared in local and San Francisco Bay Area newspapers. In 2008, Vallejo filed for bankruptcy protection in the United States Bankruptcy Court, Eastern District of California (Case No. 08-26813-A-9). Respondent stated that he was "unpopular" with labor unions as he had recommended throwing out most labor contracts. He labeled the City Council as "pro-union" and felt that his "days were numbered." By April 2009, his relationship with Vallejo had "soured."

27. The City Council convened a special joint meeting to discuss Vallejo's financial situation and respondent's performance evaluation. The subject in the Agenda and Meeting Minutes was: "Consideration of whether or not to give written notice of non-renewal of employment agreement to City Manager [respondent] as set forth in Section 7.A(2) of his employment agreement."<sup>11</sup> This provision grants authority to the City Council to remove the City Manager "at any time, with or without cause, by a majority vote of its members." (Exh. 14.) The meeting minutes expressed concern that respondent's "contract is too expensive and burdensome for the community." Members also acknowledged that the "City must give notice of non-renewal at least 12 months in advance or the contract automatically renews."

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<sup>11</sup> The Separation Clause in respondent's November 2006 Contract appears at Section 7.A(2), Termination and Removal. In respondent's March 2007 Contract, the Separation Clause appears at Section 6.B(2).

On February 24, 2009, the City Council approved Resolution 09-27, "to give written notice of non-renewal of employment agreement to respondent." The next day, Vallejo sent notice to respondent of non-renewal of his March 8, 2007 Employment Agreement. The Notice of Non-Renewal indicated that the termination date of respondent's employment agreement remained March 8, 2010.

28. *Non-Renewal Provisions in Contract.* The term of respondent's employment agreement was three years, commencing on March 8, 2007, and continuing until March 8, 2010. The agreement was set to automatically renew unless Vallejo provided timely notice of non-renewal. The Second Agreement specifically stated: "The City must give the City Manager written notice of non-renewal at least 12 calendar months prior to the initial Termination Date or any succeeding Termination date," otherwise, the "Agreement shall automatically renew for an additional year ...". Under "Severance Pay," two options were provided:

- (1) In the event the City Manager is terminated by the City Council during such time that the City Manager is willing and able to perform the City Manager's duties under this Agreement, then in that event the City agrees to pay the City Manager a lump sum cash payment equal to twelve months' base salary plus City-paid PERS contribution then in effect as provided in 4.A(1) and (2) above of which is not reportable to CalPERS.
- (2) In the event the City Council gives the City Manager written notice of non-renewal of the Agreement, then in that event the City agrees to pay the City Manager a lump sum cash payment equal to six months' base salary plus the City-paid PERS contribution then in effect as provided in 4.A(1) and (2) above if the City Manager retires or resigns within six months of receiving such notice. This is not reportable to CalPERS.

29. On March 24, 2009, respondent gave notice to the City Council of his proposal to resign effective August 31, 2009. On May 19, 2009, the City Council convened a special joint meeting at which they considered adoption of a resolution approving a "Settlement Agreement and Release of Claims" between Vallejo and respondent, and directing the mayor to execute a Separation Agreement on behalf of Vallejo. At the May 19, 2009 meeting, the City Council adopted Resolution 09-107 to effect the terms of the Settlement Agreement, in which respondent would resign effective June 1, 2009, and received severance pay of \$390,000, in three equal payments of \$130,000.<sup>12</sup> Respondent and Mayor Osby Davis executed the Separation Agreement on May 20, 2009. Respondent submitted his application

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<sup>12</sup> Since Vallejo acted to give respondent "Notice of Non-renewal," and respondent resigned within six months of receiving such Notice, the second "Severance Pay" clause applied. However, on May 19, 2009, the Council voted to approve severance pay of \$390,000, which was 20 percent more than respondent's annual base salary of \$305,844 under the March 2007 Contract.

for service retirement from Vallejo on May 22, 2009. He reported his highest compensation period as June 1, 2007 to May 31, 2008.

*CalPERS Final Compensation Determination*

30. Mr. Johnson and Marion Montez, Assistant Division Chief, testified at hearing regarding respondent's retirement benefits. Mr. Johnson began his employment with CalPERS in 1994 as a benefit program specialist. Since January 2001, he has worked as a retirement program specialist in the Compensation Review Unit. His duties included reviewing reported compensation to verify whether it was in line with the retirement law.

31. Mr. Johnson explained that cases come to the unit's attention in several ways. They may be flagged because the payrate exceeds a certain dollar amount, or referred because of suspected "pension spiking." Pension spiking is when a person artificially inflates his or her compensation in order to receive a higher allowance. This may be done intentionally or unintentionally. Mr. Johnson explained that base salary is usually determined by contract agreement or salary schedules. Anything added to base salary that the law does not allow inflates income "artificially." To identify instances where base pay is artificially inflated, analysts look for inconsistent increases in salary and then look to the details of the contract. If the employee is in a group or class of one, analysts look at documents of prior and successor employees to see if the compensation is consistent with what the agency paid others in that position. (Gov. Code, § 20636, subd. (e)(1) & (2).)

32. Documents supporting CalPERS' findings generally come from the employer and sometimes from the member. Analysts will review any document provided by the employee to determine its relevance. This includes contracts for all forms of employment including permanent, interim, and retired annuitants. Mr. Johnson stated that retired annuitants should not earn more than an active employee. (Gov. Code, § 21224, subd. (a).) Ultimately, if the item of compensation does not fall within the law, CalPERS "rejects it."

33. *CalPERS' Review of Pacifica Contract.* Analysis of respondent's case encompassed a review of respondent's CalPERS employment history, including his contract with the City of Pacifica. Mr. Johnson stated that the Pacifica employment contract was similar to Vallejo's in that it "listed [respondent's] base salary and other items that were not allowable under the PERS." The Pacifica contract contained an election by respondent:

...to have the value of the City's pick up of his portion of the PERS contribution considered salary/compensation when calculating retirement benefits. Employee may, at his option, cease car allowance and in-lieu thereof receive an equivalent increase in salary/compensation...at his option, notify the City that in lieu of one month of paid administrative leave, he will receive an equivalent increase in compensation paid over a twelve month period....

On February 21, 2007, Mr. Johnson had sent a letter to Pacifica Human Resources and respondent, informing them that "certain income was disallowed" including conversion

of car allowance, 30 days paid leave, and the employer portion of EPMC. The letter explained that respondent's reportable PERS compensation with Pacifica was \$14,184.67 monthly or \$170,216 annually. Regarding the employer pickup of the employee's share of EPMC, Mr. Johnson advised Pacifica to provide a copy of the Board adopted resolution implementing this benefit to a group or class of employees. The letter cited all applicable statutes and regulations.

34. Mr. Johnson stated that CalPERS' position as expressed in his January 26, 2007 letter never changed. He was not involved in the process by which Vallejo drafted the Second Agreement. On March 13, 2007, Ms. Boutte sent an email to Mr. Johnson in which she wrote: "...the City will be revising the City Manager's contract to correctly reflect the base salary that is persable. Once this is done, I will be forwarding the contract to you for review." Resolution 07-68 which approved the Second Agreement was adopted by the City Council on March 27, 2007. Still, the amended contract was not sent to Mr. Johnson. On April 23, 2007, Mr. Johnson sent a letter to Ms. Boutte in which he acknowledged receipt of the EPMC Resolution No. 07-70, and asked her to "Please send a copy of the contract agreements between the City of Vallejo and the Council Appointed Executive Group(s)."

35. On May 7, 2007, one day before the Second Agreement was signed by Mayor Intintoli, and two months after it was approved by the Council, Ms. Boutte sent Mr. Johnson, the employment agreements for both Council Appointed Executive Group positions (City Attorney and City Manager). Upon receipt, Mr. Johnson looked at it briefly and saw that the salary had changed from \$216,000 to approximately \$305,000. He realized when he saw it that "it was going to take some time to review and more documentation would be required." He immediately wondered if Vallejo had taken all the items he told them were not reportable and lumped them into the higher salary.

36. *CalPERS Determination and Appeal Letter.* After respondent resigned from Vallejo and submitted his retirement application, CalPERS denied his reported final compensation. On December 3, 2009, Ms. Montez sent correspondence to respondent and Vallejo explaining CalPERS' determination and respondent's appeal rights. The letters indicated that CalPERS had reviewed the compensation reported by Vallejo and discovered items that did not qualify as reportable compensation. Ms. Montez cited Mr. Johnson's January 26, 2007 letter to Vallejo that identified disallowed items. She stated that "revising the agreement does not qualify the other items," and that converting these items into salary constituted final settlement pay. (Cal. Code Regs, tit. 2, § 570.) Further, the salary increase from \$216,000 to \$305,000 represented an increase which is also in conflict with retirement law. (Gov. Code, § 20636, subd. (e)(2).)

Ms. Montez explained that the new salary of \$305,842 (\$147.04 per hour), constituted the same compensation which CalPERS initially denied. She informed them that CalPERS would exclude the higher salary from respondent's retirement benefit calculation and requested Vallejo to reverse the disallowed compensation from the payroll system and report only 1) the original salary of \$216,000, 2) 120 hours of management incentive pay, and 3) eight percent (8%) EPMC on the correct payrate, plus any cost of living increases granted to

respondent which were consistent with increases granted to all other miscellaneous employees of Vallejo from January 2007 through June 2009.

37. Ms. Boutte responded by letter dated March 28, 2010, and requested Ms. Montez to reconsider her determination. In the letter, Ms. Boutte stated: "I am disappointed to receive yet another piece of correspondence in a long series of contradictory statements from CalPERS representatives concerning our Executive Contract Staff Group, our salary arrangements with members of this group, the content of the member contracts, and the subsequent EPMC." Ms. Boutte expressed that the "parties intent was instituted and brought into compliance in accordance with Carlous Johnson's March 8, 2007 review of Mr. Tanner's old Agreement." There is no evidence to support a finding that Mr. Johnson reviewed and communicated his approval of the Second Agreement on March 8, 2007.

Ms. Boutte also wrote that "In addition, [respondent's] salary was re-negotiated in light of the unique financial position and leadership demands of the City of Vallejo. The annual pay level was re-evaluated and was reviewed against other Cities and Counties executive management pay levels in Central and Northern California and set at an appropriate level to retain Mr. Tanner."

Ms. Boutte was referring to a survey she conducted of City Manager salaries which Mr. Morris reviewed. She prepared a chart labeled City Manager Survey Data –Monthly Total Compensation (Compensation Survey), effective October 30, 2006. The Compensation Survey shows the following monthly and annual salaries for Vallejo and neighboring cities:

<b>Agency/City</b>	<b>Monthly Base Salary</b>	<b>Annual Base Salary</b>
Berkeley	\$16,505.00	198,060.00
Concord	16,292.00	195,504.00
Richmond	16,666.00	199,992.00
Hayward	15,385.00	184,620.00
Vacaville	15,952.00	191,424.00
Fairfield	14,802.00	177,624.00
<b>Survey Average</b>	<b>15,934.00</b>	<b>191,208.00</b>
Vallejo (Kemp)	17,500.00	210,000.00
Respondent's Proposal	23,517.00	282,204.00
<b>Respondent's Final Agreement (as of 10/2006)</b>	<b>18,000.00</b>	<b>\$216,000.00</b>

38. The Compensation Survey showed that respondent was the highest paid City Manager in the region. Prior to respondent, the highest paid Vallejo City Manager was Roger Kemp, whose November 2004 contract provided for an annual base of \$198,000. According to Ms. Boutte's Compensation Survey, Mr. Kemp's annual base salary was \$210,000, but he did not receive EPMC or Deferred Compensation in his total compensation

package like respondent did.<sup>13</sup> The only other position in respondent's Council Appointed Executive Group was the City Attorney. City Attorney Soley's May 7, 2007 contract provided for an annual base salary of \$151,000.89.

### *Retirement Benefit Calculations*

39. David Clement has been a CalPERS Senior Pension Actuary since July 2007. He has been with CalPERS since October 1999 working in an actuarial capacity. He possesses a Bachelor of Science degree in Mathematics, Economics, and Actuarial Science from the University of California, Los Angeles. He is an Enrolled Actuary and possesses several relevant credentials. Mr. Clement is experienced and knowledgeable of how member contributions are calculated.

For purposes of calculating monthly retirement benefits, three factors are used: 1) Service, 2) Age, and 3) Salary. The salary is usually based on the last 12 or 36 months of service but the member can specify in their retirement application a different period of highest pay. Respondent retired at 61.75 years of age. His retirement factor increased based on years of service with CalPERS contracting employers (service credit). Respondent worked for six employers with the following service credits: Emeryville Services Authority (Service Credit: 2.928), City of Galt (10.726), Alameda (.655), City of Pleasant Hill (18.746), City of Pacifica (2.835), and City of Vallejo (2.418). The total service credit was 38.308.

40. Mr. Clement defined "PERSable compensation" as any compensation that qualifies as reportable to CalPERS (reportable compensation). It can include more than just salary and for respondent included EPMC and management incentive pay (MIP). To determine EPMC and MIP, the following calculations were made:

The base salary as determined by respondent was \$305,844. Mr. Clement divided this higher base salary by 2080 to determine the hourly rate which amounted to \$147.04 per hour. Respondent was entitled to MIP which amounted to \$17,644.84 (120 hours of MIP x 147.04 = \$17,644.84). Salary plus MIP was \$323,488.84 (\$305,844 + 17,644.84 = \$323,488.84). Finally, respondent was entitled to EPMC at eight percent which amounted to \$25,879.11 (323,488.84 x 8% = \$25,879.11). Hence, based on respondent's claimed salary, the total reportable PERS compensation was \$349,367.95 annually or \$29,113.99 monthly.

The base salary as determined by CalPERS was \$216,000. Mr. Clement performed the same MIP and EPMC calculations on the base salary of \$216,000. Mr. Clement thereby arrived at a total reportable PERS compensation of \$20,561 monthly, \$246,732 annually.

41. Mr. Clement prepared exhibits to demonstrate the effect on respondent's retirement benefit based on respondent's claimed reportable compensation (\$29,113) and that

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<sup>13</sup> According to Ms. Boutte's Compensation Survey, Mr. Kemp's total compensation package was \$278,852, compared to respondent's total compensation package of \$349,952; a difference of \$71,100.

determined by CalPERS (\$20,561). For comparison purposes, the “Unmodified Benefit” was calculated and shown.<sup>14</sup> Mr. Clement also calculated the apportioned costs to respondent’s six CalPERS employers. Since the employing agencies ultimately pay the costs of a retiree’s benefits, the benefit is apportioned by the amount of time the employee worked for each entity. If the pension is increased based on a higher final compensation amount, all the entities a retiree worked for pay for the increase. A comparison of respondent’s Monthly and Annual Retirement Allowance follows:

	Using CalPERS' Final Comp.	Using Respond's Final Comp.	Difference
<b>Reportable Monthly Compensation</b>	<b>\$20,561.00</b>	<b>\$29,113.00</b>	<b>\$8,552.00</b>
Monthly Allowance Paid by Vallejo	1,333.64	1,891.97	558.33
Annual Allowance Paid by Vallejo	16,004.00	22,704.00	6,700.00
Monthly Allowance Paid by Pacifica	1,457.26	2,063.38	606.12
Annual Allowance Paid by Pacifica	17,487.00	24,761.00	7,274.00
Monthly Allowance Paid by Pleasant Hill	8,664.61	12,268.51	3,603.90
Annual Allowance Paid by Pleasant Hill	103,975.00	147,222.00	43,247.00
Monthly Allowance Paid by Galt	4,925.53	6,987.59	2,062.06
Annual Allowance Paid by Galt	59,106.00	83,851.00	24,745.00
Monthly Allowance Paid by Alameda	302.75	428.67	125.92
Annual Allowance Paid by Alameda	3,633.00	5,144.00	1,511.00
Monthly Allowance Paid by Emeryville	1,353.35	1,916.26	562.91
Annual Allowance Paid by Emeryville	16,240.00	22,995.00	6,755.00
<b>Total Unmodified Monthly Allowance</b>	<b>18,037.14</b>	<b>25,556.38</b>	<b>7,519.24</b>
<b>Total Unmodified Annual Allowance</b>	<b>216,446.00</b>	<b>306,677.00</b>	<b>90,231.00</b>

<sup>14</sup> An unmodified benefit is the amount the member would receive before any optional settlement or divorce split. Members may elect to take a reduced benefit at the time of retirement in order to produce more for a spouse at the time of the member’s death. Or, a member’s monthly benefit may be divided amongst an ex-spouse resulting in a lower or modified benefit going to the retired member.

42. Mr. Clement also calculated the “present value of projected benefits” or the cost of respondent’s retirement benefits based on the two different highest compensation figures. The present value (PV) calculation starts with the benefit amount, which is projected to reflect benefits over the member’s life. The actuarial calculation applies a “long term rate of return” (interest rate) on assets and a cost of living protection (COLA) of two percent. Mr. Clement calculated the benefit using both the discount rate of 7.75 percent and the 30-year U.S. Treasury rate in June 2009 of 4.52%.<sup>15</sup> A comparison of the monthly and annual present value calculations follow:<sup>16</sup>

	Using CalPERS’ Final Comp.	Using Respondent’s Final Comp.	Difference
PV based on 7.75%	\$2,543,767.00	\$3,604,167.00	\$1,060,400.00
PV based on US T- rate (4.52%)	3,489,927.00	4,944,720.00	1,454,793.00

*Testimony of Vallejo Personnel*

43. Mr. Morris, Human Resources Director testified at hearing. Mr. Morris worked closely with Ms. Boutte. He read Mr. Johnson’s January 26, 2007 letter, discussed it with respondent, and told Ms. Boutte to revise the November 2006 Contract to incorporate suggestions from CalPERS which met their approval. Mr. Morris had no firsthand knowledge whether the problems could be solved by converting non-salary components into base salary.

44. Mayor Intintoli testified at hearing. He first held office in Vallejo in 1973 including seats on the Solano County School Board and City Council. He recalled that in November 2006, Vallejo had “budget issues” and difficult labor negotiations. On November 6, 2006, Mr. Thompson sent the Compensation Survey by email to the mayor and Council members Stephanie Gomes, Tony Pearsall, Gary Cloutier, Hermie Sunga, Jerry Davis, and Tom Barte. The email stated the following in pertinent part:

I’ve been back and forth with the candidate a number of times on his agreement terms. Based on the direction from the Council’s subcommittee...we have reached what I think is the final term sheet (see attached). The Mayor and Vice Mayor acknowledge that it is a big number but are recommending it to you. ...

I’ve attached an updated spreadsheet to show the total comp comparisons. His total package would be about \$70,000 over Kemp

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<sup>15</sup> Respondent’s retirement date was June 2, 2009.

<sup>16</sup> Mr. Clement also apportioned the present value calculations for each of respondent’s employing entities. That data is not replicated here but is submitted in evidence.

and about \$95,000 over a quick survey of other cities ...On the positive side this package costs out at about \$55,000 below his original offer....

I wouldn't advise making much change to this. I think this is the best deal you will get. From his vantage point, he'd be taking the job at about \$37,000/year less in reportable PERS earnings and deferred compensation than he is getting now. ...

(Underline in original.) The email further acknowledged that there might be public outcry over the numbers but that respondent was worth it. It is noted that with respect to reportable PERS earnings, the email is inaccurate in that respondent's reportable PERS earnings at Pacifica were \$170,216. (Factual Finding 33.) Respondent's reportable PERS earnings at Vallejo were \$246,732. (Factual Finding 40.) The evidence supports a finding that respondent actually increased his reportable PERS earnings by \$76,516.00.

45. Page two of Mr. Thompson's November 6, 2009 email included a list of terms and items of compensation for respondent's employment contract:

- 1) Three year contract commencing on January 8, 2007
- 2) Compensation: \$216,000 per year
- ...
- 4) Car allowance of \$600/month
- 5) 30 days annual leave
- 6) 30 days sick leave at commencement; annual accrual at 12 days
- 7) 30 days accrual of management leave, no administrative leave
- 8) Cell phone allowance of \$100/year; increased by CPI
- 9) City to contribute 15 percent of salary to deferred compensation plan
- 10) Employee to be hired on a limited term basis initially with reinstatement to PERS after two months of employment
- 11) Employee may convert deferred compensation and car allowance to salary upon reinstatement to PERS ...

Items 10 and 11 of this list establish that the November 2006 contract was constructed per respondent's original idea, as conveyed to Mr. Avery during negotiations. The goal was to get the contract past the City Council while netting respondent the higher salary he desired. (Factual Finding 5.)

46. Ms. Boutte testified at hearing. She has worked for Vallejo since 1994, starting as a Senior Benefits Manager. She is currently the Human Resources Director for Vallejo. She estimated communicating with CalPERS on hundreds of matters related to payroll processing, resolutions, contract changes, health benefits, and employment terminations. She has spoken to Mr. Johnson, the Chief Actuary, and various analysts many times.

Ms. Boutte testified that she disagreed with CalPERS' determination not to include certain items in respondent's Second Agreement. She wrote the letter to Ms. Montez dated

March 28, 2010, on behalf of Vallejo. She believes that CalPERS made “contradictory statements” regarding respondent’s employment agreements. She denied having any reason to think that the base salary contained in the Second Agreement was “not PERSible.” She was aware that respondent would not stay on the job if he did not receive the higher salary. She “ran the EPMC and March Agreement” by Mr. Soley who signed off on it as “approved to form.” Ms. Boutte’s assertion that CalPERS made contradictory statements is not supported by the evidence. Her claim that she had no reason to believe that the contract amendments were “not PERSible,” defies comprehension.

47. Mr. Soley testified at hearing. He began working for Vallejo as Deputy City Attorney in February 1988. In May 2001, the City Council appointed him City Attorney. His job was to represent City employees, City Manager, and City Council. Sometimes he was involved in the creation of contracts. He “usually” reviewed contracts prior to them going before the City Council. Mr. Soley had no independent recollection of reviewing respondent’s November 2006 contract before its adoption by the City Council. He stated that the terms would have been negotiated between the City Council and Mr. Thompson. He is consulted on contract negotiations only if they have a question. He acknowledged that he signed both contracts. He was not involved in activity leading up the March 2007 contract and had no recollection of participating in the formation of Resolution 07-68. The negotiations for the Second Agreement were also handled by Mr. Thompson. Mr. Soley had no recollection of explaining the provisions of the March 2007 Contract to the City Council. His understanding was that Human Resources was working with CalPERS and if they had particular questions, they would have sought his counsel. In that event, the matter would have been referred to outside counsel to obtain more expertise.

48. Stephanie Gomes was a second term City Council member in 2007. She stated that the Council would have talked about respondent’s contract in closed session, but any contract they approved had to come before the public. She identified two parts to respondent’s contract, the first being before he was reinstated to CalPERS. She stated, “The amendment was part of the second phase, it was to convert some of Items one through 16 into his base pay.” She was referring to Mr. Thompson’s November 6, 2006 email to the mayor and Council. (Factual Finding 45.) She was aware that the amendment also addressed problems identified by CalPERS with the November 2006 Contract. In making the necessary contract changes, she stated, “I would expect the City to protect the City. To follow CalPERS regulations that are necessary.”

#### *Challenges/Special Defenses filed by Respondent*

49. *Respondent’s Parole Evidence Objection Without Merit.* This case involved one initial contract for employment and a second contract purporting to “amend” the terms of the original contract. Resolution 07-68 uses the terms amend and amendment three times. The Council believed they were adopting an “amendment” that would “not change the total cost of the original employment agreement.” The only way to determine whether that was true, would be to inspect the terms of the November 2006 Contract. The Council also “resolved” that they were “incorporating the necessary language changes as recommended by CalPERS.” The only way to determine whether that was true would be to inspect the

November 2006 Contract and read CalPERS January 26, 2007 letter to Vallejo. Resolution 07-68 authorized the mayor to execute the "First Amendment to [respondent's] employment contract."

The "parol evidence rule" is codified in section 1856 of the Code of Civil Procedure. Generally speaking, it prohibits the introduction of extrinsic evidence, whether oral or written, to vary the terms of an integrated written agreement or to add terms to an integrated agreement that is also intended as a complete and exclusive statement of the parties' agreement. (Code of Civ. Proc., § 1856, subs.(a) & (b); *Pacific State Bank v. Greene* (2003) 110 Cal.App.4th 375, 383-384.) The rule does not apply to exclude "evidence of the circumstances under which an agreement was made or to which it relates, or to explain an extrinsic ambiguity or otherwise interpret the terms of the agreement, or to establish illegality or fraud." (Code Civ. Proc., § 1856, subd. (g).)

CalPERS is mandated to investigate claims for retirement benefits. "The Board may require a member or beneficiary to provide information it deems necessary to determine this system's liability with respect to, and an individual's entitlement to, benefits prescribed by this part." (Gov. Code, § 20128.) As such, the parole evidence rule does not apply as a bar to CalPERS' mandate to examine and interpret the terms of the Initial and Second Agreements, clear up any ambiguities, or assess whether an illegality or fraud is being committed. (Code Civ. Proc., § 1856, subd. (g).)

50. *Respondent's Jurisdictional Challenge is without Merit.* Vallejo was expressly authorized by the Vallejo City Charter to contract with CalPERS for the purpose of administering employee retirement benefits. (Charter, §§ 202, 807.) As such, Vallejo is subject to the provisions of the PERL. (Gov. Code, §§ 20022 & 20460.) (Factual Finding 2.)

The City Council approved a contract for respondent's employment in or about November 2006. An agency can, ostensibly, contract to pay its executives what the market will bear, guided only by its fiduciary duty to the public and other relevant laws. However, CalPERS is not obliged to accept the terms as compensable for purposes of calculating retirement benefits. As stated in *Molina*, respondent "fails to recognize the important difference between the amount he was paid by [the City], ...and the much narrower category of "compensation earnable" that can be taken into account for pension purposes, as established under PERL." (*Molina v. Board of Administration* (2011) 200 Cal.App.4th 53, 67.)

Respecting contracting agencies, Government Code section 20506 specifically states:

Any contract heretofore or hereafter entered into shall subject the contracting agency and its employees to all provisions of this part and all amendments thereto applicable to members, local miscellaneous members, or local safety members except those provisions that are

expressly inapplicable to a contracting agency until it elects to be subject to those provisions.

CalPERS' duty to its members requires that it "determine who are employees and is sole judge of the conditions under which persons may be admitted to and continue to receive benefits under this system." (Gov. Code, § 20125.) The assets of a public pension or retirement system are "trust funds." (*City of Sacramento v. Public Employees Retirement System* (1991) 229 Cal.App.3d 1470, 1494.) "The fiduciary of the public pension or retirement system shall discharge his or her duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to, participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system." (*Id.* at p. 1493; Cal. Const., art. XVI, § 17, subd. (b).) Further, the Board is obliged to investigate applications and pay benefits "only to those members who are eligible for them." (*McIntyre v. Santa Barbara County Employees' Retirement System* (2001) 91 Cal.App.4th 730, 734.) There is no question in law or fact that CalPERS has jurisdiction to administer and hear all matters related to respondent's application for service retirement.

51. *Respondent's Estoppel Argument is without Merit.* The affirmative defense of estoppel is inapplicable in the current case. When applied against a private party, the elements are: 1) the party to be estopped was apprised of the facts, 2) that party intended their conduct to induce reliance by the other, 3) the party asserting estoppel was ignorant of the facts, and 4) the asserting party suffered injury. (*Medina v. Board of Retirement, Los Angeles County* (2003) 112 Cal.App. 4th 864, 868.)

CalPERS had information that respondent's Pacifica Contract and November 2006 Contract with Vallejo were flawed in similar ways. CalPERS relayed this information clearly and succinctly to respondent and both contracting agencies. CalPERS intended that respondent, Pacifica, and Vallejo comport their reporting accordingly. Vallejo was not ignorant of the facts. In fact, they used the information provided by Mr. Johnson to manipulate the terms of a Second Agreement. Further, there is evidence that individuals in Human Resources were less than candid in their communications with the mayor and City Council. (Factual Finding 23.) Finally, respondent suffered no injury. In fact, his final contract netted him substantially more than his Pacifica reportable compensation, more than his Vallejo predecessor, and more than surrounding City Managers. (Factual Findings 37 & 38.) His argument fails factually.

Respondent's estoppel argument also fails from a well established public policy perspective. "[E]stoppel will not be applied against the government if to do so would effectively nullify 'a strong rule of policy, adopted for the benefit of the public...'" (*Ibid.*) CalPERS administers funds in trust for members and beneficiaries. As such, public policy is against application of an estoppel defense herein, even if the facts fit such an argument, which they do not.

52. *Respondent's Laches Argument is without Merit.* The equitable doctrine of laches may be applied when a public agency unreasonably delays in taking action against a

party and the party is prejudiced as a result of the delay. (*City and County of San Francisco v. Pacello* (1978) 85 Cal.App.3d 637, 644-645.) However, the laches defense is factually inapplicable to this matter.

The language of Mr. Johnson's January 26, 2007 letter is clear: "[P]ayments such as management leave credits; automobile allowance, and deferred compensation should not be converted to salary and reported to CalPERS for retirement purposes." This letter was timely. Then, Ms. Boutte received Mr. Johnson's email on March 15, 2007, which stated: "You can only report the value of the Employee's contributions. The extra 1% is the employer's portion. So the contract should read 8%, and the resolution should only show 8%." She used the "8%" language in Resolution 07-70, but converted the "one percent" employer portion into respondent's payrate. Mr. Johnson's March 15, 2007 email was sent to Ms. Boutte one week after the Second Agreement was taken before the Council (on March 8, 2007). In spite of this information, Ms. Boutte did not act to remove the disallowed one percent employer contribution, but allowed it to remain folded into respondent's base pay. The mayor signed the March 8, 2007 Contract two months later on May 8, 2007. Vallejo and respondent ignored timely CalPERS directives and determined to do covertly what they could not do overtly. Hence, the doctrine of laches is factually inapplicable.

So too, the doctrine of laches will not be applied to preclude a state agency from taking action when the action concerns a public policy. (*City and County of San Francisco v. Ballard* (2006) 136 Cal.App.4th 381, 395.) CalPERS' authority to administer the public retirement system is a matter of great and fundamental public policy, protected by the California Constitution. (*City of Sacramento, supra* 229 Cal.App.3d at p. 1493; Cal. Const., art. XVI, § 17.)

53. Any other assertions put forth by any party at hearing and in closing briefs, and not addressed herein are found to be irrelevant, collateral to the central issues in this case, or without merit. As such, they are not further addressed herein.

## LEGAL CONCLUSIONS

### *Applicable Statutes and Regulations*

1. CalPERS is a "prefunded, defined benefit" retirement plan. (*Oden v. Board of Administration* (1994) 23 Cal.App.4th 194, 198). The formula for determining a member's retirement benefit takes into account: (1) years of service; (2) a percentage figure based on the age on the date of retirement; and (3) final compensation. (Gov. Code, §§ 20037, 21350, 21352, 21354; *City of Sacramento v. Public Employees Retirement System* (1991) 229 Cal.App.3d 1470, 1479.)

2. Government Code section 20630 defines "compensation" as the remuneration paid out of funds controlled by the employer in payment for the member's services performed during normal working hours or for time during which the member is excused from work because of holidays, sick leave, industrial disability leave, vacation, compensatory time off, and leave of absence. Compensation shall be reported in accordance

with section 20636 and shall not exceed compensation earnable, as defined in section 20636. (Gov. Code, § 20630, subs. (a) & (b).)

3. “Compensation earnable” is composed of (1) pay rate, and (2) special compensation, as defined in Government Code section 20636.

4. “Pay rate” means the normal monthly rate of pay or base pay of the member paid in cash to similarly situated members of the same group or class of employment for services rendered on a full-time basis during normal working hours. “Pay rate” for a “member who is not in a group or class, means the monthly rate of pay or base pay of the member, paid in cash and pursuant to publicly available schedules, for services rendered on a full-time basis during normal working hours, subject to the limitations of paragraph (2) of subdivision (e).” (Gov. Code, § 20636, subd. (b)(1).)

5. “Special compensation” of a member includes a payment received for special skills, knowledge, abilities, work assignment, workdays or hours, or other work conditions.” (Gov. Code, § 20636, subd. (c)(1).)

“Special compensation shall be limited to that which is received by a member pursuant to a labor policy or agreement or as otherwise required by state or federal law, to similarly situated members of a group or class of employment that is in addition to payrate. If an individual is not part of a group or class, special compensation shall be limited to that which the board determines is received by similarly situated members in the closest related group or class that is in addition to payrate, subject to the limitations of paragraph (2) of subdivision (e).” (Gov. Code, § 20636, subd. (c)(2).)

“Special compensation shall be for services rendered during normal working hours and, when reported to the board, the employer shall identify the pay period in which the special compensation was earned.” (Gov. Code, § 20636, subd. (c)(3).)

6. “The board shall promulgate regulations that delineate more specifically and exclusively what constitutes ‘special compensation’ as used in this section...” (Gov. Code, § 20636, subd. (c)(6).)

7. Special compensation does not include: “(A) Final settlement pay, (B) Payments made for additional services rendered outside of normal working hours, whether paid in lump sum or otherwise, or (C) Other payments the board has not affirmatively determined to be special compensation.” (Gov. Code, § 20636, subd. (c)(7).)

8. A “group or class of employment” means a number of employees considered together because they share similarities in job duties, work location, collective bargaining unit, or other logical work related grouping. One employee may not be considered a group or class. (Gov. Code, § 20636, subd. (e)(1).)

“Increases in compensation earnable granted to an employee who is not in a group or class shall be limited during the final compensation period applicable to the employees, as well as the two years immediately preceding the final compensation period, to the average

increase in compensation earnable during the same period reported by the employer for all employees who are in the same membership classification..." (Gov. Code, § 20636, subd. (e)(2).)

9. California Code of Regulations, title 2, section 570 defines "Final Settlement Pay" to mean any pay or cash conversions of employer benefits in excess of compensation earnable, that are granted or awarded to a member in connection with or in anticipation of a separation from employment. (Gov. Code, § 20636, subd. (f); Cal. Code Regs, tit. 2, § 570.)

Final settlement pay may take the form of any item of special compensation not listed in Section 571. It may also take the form of a bonus, retroactive adjustment to payrate, conversion of special compensation to payrate, or any other method of payroll reported to PERS. (Cal. Code Regs, tit. 2, § 570.)

10. California Code of Regulations, title 2, section 571 exclusively identifies and defines special compensation items for members employed by contracting agency that must be reported to CalPERS if they are contained in a written labor policy or agreement. (Cal. Code Regs., tit. 2, § 571, subd. (a).) The Board has determined that all items of special compensation listed in subsection (a) are:

- (1) Contained in a written labor policy or agreement as defined at Government Code section 20049, provided that the document:
  - (A) Has been duly approved and adopted by the employer's governing body in accordance with requirements of applicable public meeting laws;

[redacted]...[redacted]
- (2) Available to all members in the group or class;
- (3) Part of normally required duties;
- (4) Performed during normal hours of employment;
- (5) Paid periodically as earned;
- (6) Historically consistent with prior payments for the job classification;
- (7) Not paid exclusively in the final compensation period;
- (8) Not final settlement pay; and
- (9) Not creating an unfunded liability over and above PERS' actuarial assumptions.

[redacted]...[redacted]

(Cal. Code Regs., tit. 2, § 571, subd. (b).)

- (c) "Only items listed in subsection (a) have been affirmatively determined to be special compensation. All items of special compensation reported to PERS

will be subject to review for continued conformity with all of the standards listed in subsection (b).” (Cal. Code Regs., tit. 2, § 571, subd. (c).)

- (d) “If an item of special compensation is not listed in subsection (a), or is out of compliance with any of the standards in subsection (b) as reported for an individual, then it shall not be used to calculate final compensation for that individual.” (Cal. Code Regs., tit. 2, § 571, subd. (d).)

### *Legal Cause*

11. An applicant for retirement benefits has the burden of proof to establish a right to the entitlement, absent a statutory provision to the contrary. (*Greator v. Board of Administration* (1979) 91 Cal.App.3d 54, 57.)

12. Respondent did not meet his burden to establish that compensation he received for his automobile allowance, employer paid deferred compensation, 30-day leave allowance, or the one percent employer cost of member contributions, are properly included as compensable earnable for the purpose of calculating his retirement benefits. The value of these components of respondent’s pay is specifically excluded by the PERL. (Gov. Code, § 20636, subd. (g)(4)(E), (F), (H) & (I).) They do not constitute special compensation and cannot be converted into respondent base payrate.

13. Respondent elected a final compensation period of June 1, 2007 to May 31, 2008. Respondent’s compensation in excess of compensation earnable during his last 16 months of employment, from March 8, 2007 through his retirement date of June 1, 2009, constitutes final settlement pay which includes a “retroactive adjustment to payrate.” (Cal. Code Regs., tit. 2, § 570.) Final settlement pay is specifically excluded as a component of either “payrate” or “special compensation.” (Gov. Code, § 20636, subd. (g)(4)(G); Cal. Code Regs., tit. 2, § 570.)

### *Legal Analysis*

14. CalPERS contends that respondent engaged in “pension spiking” in that his compensation as reported by Vallejo included several components specifically excluded under the PERL. For the reasons stated above, CalPERS’ determination is supported by the weight of the evidence.

15. Respondent argues that hiring and compensation of municipal employees generally are matters pertaining to municipal affairs. Also, that Vallejo followed all required procedures in the City Charter in negotiating, contracting, and adopting the March 8, 2007 employment agreement. The language of Resolution 07-68 resolved to do two things: 1) “to amend the original employment agreement to comply with the CalPERS regulations,” and 2) “that the language amendment will not change the total cost of the original employment agreement.” The March 2007 Contract did not effect either of these provisions. To the contrary, the amended contract was in conflict with the PERL and the higher salary represented therein would increase Vallejo’s costs in the short and long term. Respondent

retired on June 2, 2009, just 13 months after the Second Agreement was signed on May 8, 2011. The new salary of \$305,844 would result in an increase of \$90,231 in respondent's unmodified allowance, with Vallejo's share being \$38,708.00 annually. (Factual Finding 41.)

Respondent is correct that an agency such as Vallejo may contract to provide benefits and salary to its employees as it sees fit, constrained by applicable law and its own fiduciary duty to its citizens. It is noted that Vallejo filed for bankruptcy protection during respondent's tenure. However, CalPERS is not bound to accept Vallejo's financial decisions in contravention of the PERL. (*Molina, supra* 200 Cal.App.4th at p. 67.)

16. Case law supports a finding that the benefits at issue here are not a part of compensation earnable for purposes of calculating retirement benefits. "An employee's compensation is not simply the cash remuneration received, but is exactly defined to include or exclude various employment benefits and items of pay." (*Oden v. Bd. of Admin. Of the Public Employees' Retirement System* (1994) 23 Cal.App.4th 194, 198.) This constitutes "final settlement pay" and is an impermissible salary increase under the PERL. (Gov. Code, § 20636, subd. (e)(1) & (f); Cal. Code Regs., tit. 2, § 570.) The conversion of components of compensation does not alter the nature of the pay. The law does not respect form over substance. (Civ. Code, § 3528; *Dept. Veterans Affairs v. Superior Court* (1999) 67 Cal.App.4th 743, 758.)

#### *Conclusion*

17. CalPERS correctly determined that respondent's compensation earnable for purposes of calculating his retirement benefits cannot include amounts previously paid to respondent as an automobile allowance, employer paid deferred compensation, 30-day leave allowance, one percent employer portion of PERS contributions, or 120-hour annual leave cash out option. (Factual Findings 22 and 23.) The contract amendment sought to convert these values into payrate in contravention of explicit directives of CalPERS and clear wording of the PERL. CalPERS' adjustment to respondent's compensable earnable is supported by the PERL and is upheld. (Gov. Code, § 20636; Cal. Code Regs., tit. 2, §§ 571, 570.)

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**ORDER**

The appeal of respondent Joseph M. Tanner and respondent City of Vallejo to include prohibited items of compensation into respondent Tanner's compensable earnable, as reflected in his increased hourly rate, for purposes of calculating his service retirement allowance is **DENIED**.

**DATED: November 20, 2012**



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**DIAN M. VORTERS**  
**Administrative Law Judge**  
**Office of Administrative Hearings**