

ATTACHMENT A
THE PROPOSED DECISION

BOARD OF ADMINISTRATION
CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM

In the Matter of the Calculation of Final
Compensation of

JOHN F. FOLEY,

Respondent,

and

SEWER AUTHORITY MID-COASTSIDE,

Respondent.

Case No. 2010-1214

OAH No. 2013080604

PROPOSED DECISION

Administrative Law Judge Perry O. Johnson, Office of Administrative Hearings, State of California (OAH), heard this matter on December 10, 2013, at Oakland, California.

Senior Staff Counsel Jeanlaurie Ainsworth represented petitioner Karen DeFrank, Chief (petitioner), Customer Account Services Division, Public Employees' Retirement System, State of California (CalPERS).

Attorney at Law Kenneth J. Philpot, of Tufts, Stephenson and Kasper, LLP, 235 Montgomery Street, Suite 1035, San Francisco, California 94104 represented respondent John F. Foley, who was present at the administrative adjudication proceeding.

Respondent Sewer Authority Mid-Coastside¹ was not represented at the hearing of this matter.

The record was held open to afford opportunities to the parties to file written closing arguments, and if necessary, reply briefs. On January 31, 2014, OAH received petitioner's "Closing Statement" along with attachments "A" and "B." (Attachment "A" is CalPERS's precedent decision² No. 12-01 for Case No. 8705, titled *Craig F. Woods and Tahoe-Truckee*

¹ On October 22, 2013, Sewer Authority Mid-Coastside filed with OAH its notice of "Withdrawal of Appeal."

² Government Code section 11425.60.

PUBLIC EMPLOYEES RETIREMENT SYSTEM

FILED MAY 6, 2014

[Handwritten Signature]

Sanitation Agency. Attachment “B” is the decision in Case No. 2011-9722, titled “Durand Rall and Omnitrans). Petitioner’s Closing Statement and attachments are marked as exhibit “17.” On February 3, 2014, OAH received “Respondent Foley’s Closing Argument,” which are marked as exhibit “J.” Also, on February 3, 2014, OAH received petitioner’s “Request for [Official] Judicial Notice” along with a declaration of M.A. Sanders with Legislative Intent Services, Inc., and a compact disc with a copy of the 985-page Legislative History for Senate Bill 53 (1993-1994), which amended Government Code section 20636. The materials from Petitioner as filed on February 3, 2014, are marked as exhibit “18.” On February 12, 2014, OAH received petitioner’s “Reply Brief,” which is marked as exhibit “19.” Also, on February 12, 2014, OAH received respondent Foley’s “Opposition to [petitioner’s] Request for [Official] Notice,” which is marked as exhibit “K.” And, on February 12, 2014, OAH filed respondent Foley’s “Reply to [petitioner’s] Closing Statement,” which is marked as exhibit “L.” On February 14, 2014, OAH, by the undersigned administrative law judge, issued an “Order Reopening the Record” for the purpose of prompting the parties to file supplemental written arguments regarding the import of official notice being taken of the voluminous Legislative History for Senate Bill 53 (1993-1994). On February 19, 2014, petitioner filed a letter replying to respondent’s objection and opposing official notice being taken of the above referenced legislative history. Petitioner’s letter was marked as exhibit “20.” On February 20, 2014, OAH, by the undersigned administrative law judge, issued a letter setting a briefing schedule on the topic of the significance of the aforementioned topic of legislative history of a Senate Bill. Also, on February 20, 2014, respondent Foley filed a letter with OAH regarding opposing petitioner’s briefing on the legislative history topic and requesting an extension for time to April 4, 2014, to file respondent’s reply. The letter is marked as exhibit “M.” On March 13, 2014, petitioner filed “Response in Support of Request for Official Notice of Legislative History,” which is marked as exhibit “21.” On March 17, 2014, a letter was issued from OAH requesting a written memorandum or brief as to petitioner’s identification of the specific pages or sections of the 985-page Legislative History that are deemed critical by petitioner for resolution of the controversy. On March 21, 2014, petitioner filed with OAH a letter, which is marked as exhibit “22,” regarding the pages of importance in the legislative history may aid in resolving the instant controversy. On April 16, 2014, respondent Foley filed with OAH a written argument opposing official notice of the Legislative History for Senate Bill 53 (1993-1994), and offered further argument in support of his appeal. Respondent Foley’s written argument was marked as exhibit “N.”

On April 16, 2014, the parties were deemed to have submitted the matter for decision and the record closed.

ISSUES

I. In determining compensation earnable for the calculation of the retirement benefit for the subject individual respondent, did petitioner correctly disallow an aggregate amount of remuneration paid to respondent John F. Foley as to certain categories of compensation, namely the value of a car allowance, the value of deferred compensation as

well as the value of education registration fees along with the value of licensee fees, that were expressed in an employment contract, executed during May 2003, and then amended in December 2004, between respondent John F. Foley and respondent Sewer Authority Mid-Coastside?

II. Did petitioner properly determine that the subject categories of remuneration received by respondent John F. Foley, in excess of his base contract salary, were not “special compensation” within the meaning of California Code of Regulation, title 2, section 571, subdivision (a)?

III. Can the Board of Administration apply principles of equity to recognize that during December 2011, that is one year after the retirement date of the individual respondent and the end of his employment with the respondent agency, that respondent John F. Foley and the Sewer Authority Mid-Coastside, under the authority of the principles established under the Civil Code section 3399, properly engaged in measures for the reformation of the contract of employment originally entered into by them during May 2003, and as amended in December 2004? And may the Board of Administration accept that the initially characterized categories of remuneration (deferred compensation, the value of a car allowance, as well as the value of license dues and educational registration fees) may be now included as the general payrate, or as compensation earnable, for calculation of respondent John F. Foley’s final compensation in setting his retirement benefit (pension)?

IV. In accordance with Government Code section 20636, subdivision (b)(2)(A), for purposes of determining payrate in calculating the retirement benefit (pension), did the December 2004 amendment to the original May 2003 contract of employment, between respondent John F. Foley and respondent Sewer Authority Mid-Coastside, require CalPERS to disregard any distinction for the treatment of deductions from an individual’s salary as payments directly made by an employee into deferred compensation versus a local agency’s indirect payment to a public employee the value of a contribution that could be deposited into a deferred compensation plan when the form of remuneration was not categorized as salary? (In particular, respondent Foley contends that an unreasonable distinction exists in the subject Government Code section that precludes money paid directly by a local agency, under a contractual provision, being included in the employee’s payrate in ascertaining compensation earnable for purposes of determining the employee’s retirement benefit. Respondent Foley advances that CalPERS must alter its interpretation of the import of the value of deferred compensation as payable by the local agency to an employee so that that amount of remuneration may be included in payrate as compensation earnable.)

V. Must CalPERS deny the appeal as initially filed by respondent John F. Foley together with respondent Sewer Authority Mid-Coastside regarding the matter of the payments calculation of the final compensation for purposes of defining the pension to be received by respondent John F. Foley?

FACTUAL FINDINGS

Respondent Foley's Membership in CalPERS

1. Respondent John F. Foley III (respondent Foley) was born during 1946. Currently, he is nearly 68 years old.

2. Respondent Foley is a member of CalPERS as a result of his employment with respondent Sewer Authority Mid-Coastside (sewer authority). During the duration of his work history with sewer authority, respondent Foley held the civil service position of manager.

Respondent Foley's Application for CalPERS Retirement Benefits

3. On February 10, 2010, respondent Foley signed an Application for Service Retirement, which was filed with CalPERS on February 11, 2010.

Respondent Foley retired effective May 22, 2010. Since that date he has received from CalPERS a retirement benefit (pension payments), which CalPERS has calculated to reflect its analysis of the proper and accurate amount due respondent Foley as prescribed by law.

Procedural Matters Background

4. On July 8, 2010, respondent Foley's attorney sent a letter to CalPERS containing arguments relative to items of remuneration paid to respondent Foley by sewer authority that should have been included in payrate and earnings so as to qualify for an increased reportable compensation for retirement purposes.

5. By a letter, dated August 5, 2010, the CalPERS Section Manager for Compensation and Employer Review Unit dispatched to respondent Foley, with a copy of the same to sewer authority, a written analysis containing a determination as to compensation paid to respondent Foley by sewer authority.

The August 2010 letter advised respondents that discovery had been made that certain components of gratuities, benefits or remuneration received by respondent Foley did not qualify as reportable compensation for retirement purposes. The categories of remuneration in question were payments to respondent Foley beginning in May 2003 that were designated the value of a car allowance, the value of deferred compensation and the value of education registration fees along with the value of licensee fees. And the letter noted that any special compensation calculated as payrate for final compensation for retirement purposes, under controlling regulations (Cal. Code Regs, tit. 2, § 571, subd. (a)), must meet prescribed criteria; and, because the categories of remuneration were not included on the list of expressed items of allowable compensation, the payments of the remuneration or gratuities to

respondent Foley could not be included as payrate for determining compensation earnable for calculation of the retirement benefit payable by CalPERS to respondent Foley.

And, the letter conveyed that certain components of remuneration or gratuities paid to respondent Foley, at best, “were paid for special compensation purposes.” Because a regulation promulgated by CalPERS prescribes an exclusive list of special compensation items that can be factored into calculating the retirement benefit (pension), the value of those categories of remuneration in controversy in this matter could not be included in calculating the retirement benefit as those categories were not included in the prescribed exclusive list of special compensation items.

6. By letter, dated October 11, 2010, Glenn J. Borromeo, Esq., of Catalyst Counsel APLC, requested an administrative hearing on behalf of respondent Foley and the sewer authority, also known as SAM. Certain factual and legal issues were raised in the October 2010 letter.

7. In an undated letter, consisting of 10 numbered pages with attachments³ labeled as “exhibit A” through “exhibit H”, Attorney at Law Kenneth J. Philpot filed additional appeal documents on behalf of respondent Foley. A comprehensive set of arguments were laid out in the letter by Mr. Philpot on behalf of respondent Foley.

8. CalPERS accepted respondents’ letters as duly filed appeals. Petitioner, in her capacity as Chief, Employer Services Division, CalPERS, issued the Statement of Issues on August 14, 2013. The matter proceeded to hearing on December 10, 2013. (Before the date of the hearing of this matter, sewer authority withdrew as a respondent.)

³ The attachments to respondent Foley’s attorney’s letter are: *Exhibit A* (the three-page CalPERS letter, dated August 5, 2010); *Exhibit B* (seven page “At Will Employment Agreement for Manager” dated May 2, 2003; “Amendment No. 1 to At Will Employment Agreement for Manager,” dated December 20, 2004; *Exhibit C* (eight pages of minutes regarding “Staff Report” presented at Closed Session of meeting on December 20, 2004, of the sewer authority; two-page memorandum, dated December 9, 2004, from Ad Hoc Personnel Committee to sewer authority’s Board of Directors regarding “Public Employee Performance Evaluation-Manager” along with five pages supportive information); *Exhibit D* (four page CalPERS Member Services Division report regarding estimate of costs to member (Foley) for purchase of additional service credit, dated September 28, 2005); *Exhibit E* (16 pages relating to CalPERS Member Services Division report pertaining to respondent’s Foley’s eligibility to purchase additional service credit, along with package of forms to effect the ARSC purchase); *Exhibit F* (six page CalPERS letter, dated June 6, 2006, with attached charts regarding estimate of service retirement); *Exhibit G* (11 page CalPERS letter, dated March 19, 2009, regarding an estimate per calculation of potential future benefits); and, *Exhibit H* (12 page letter, dated May 14, 2009, regarding an estimate per calculation of potential future benefits. The letter carried a notice at the bottom of page one that reads, “Unofficial. Estimate contains information that has not been validated.”)

CalPERS Evidence at the Hearing

9. Relevant information was established through Ms. Lolita Lueras's credible, persuasive and compelling testimony.

Ms. Lueras is a Retirement Program Specialist One. Her duties, functions and responsibilities include effecting retirement review studies of "reportable" compensation paid by local agencies to employees in accordance with the Public Employees Retirement Law.⁴ Ms. Lueras is exceedingly conversant with the regulations and statutes at issue in this matter.

Ms. Lueras persuasively testified that after CalPERS reviewed information submitted by respondent Foley and sewer authority, she concluded that certain categories of remuneration that respondent Foley received from sewer authority did not qualify as "final compensation" under pertinent statutes and regulations. Under the law, the amount of an individual pension recipient's service retirement allowance is calculated by applying a percentage result arrived at by use of the retiree's age on the date of retirement, the individual's years of service and the individual's final compensation. Because of notorious examples in recent history of abusive pension payouts, CalPERS personnel closely scrutinize salary information submitted by a local agency employer on behalf of an individual employee contemplating retirement so that only the items authorized under the Public Employment Retirement Law, and CalPERS's regulations, will be included in an applicant retiree's final compensation for the purpose of calculating the retirement allowance, which is paid by CalPERS for the remaining lifetime of the retiree or his/her spouse.

10. During her review, Ms. Lueras found that for the period of respondent Foley's employment as the manager of sewer authority there was no "publicly available pay schedule" for the position held by respondent Foley. The payrate, as reported by the local agency for respondent Foley, could only be discerned by the Retirement Program Specialist through the written employment contract-related documents between respondent Foley and sewer authority. The documents, which were unpersuasively described by respondent Foley's witnesses as intended as a "pay schedule," were crafted by an accountant for purposes of setting sewer authority's budget. And the documents that set out respondent Foley's compensation were not available to public scrutiny.

Ms. Lueras established that the employment contract, and its amendments, as crafted between respondent Foley and sewer authority's board of directors, did not meet the requirements for a publicly available pay schedule because the contract was formulated and finalized in a closed session of the board of directors for sewer authority.

11. During the process of her review, Ms. Lueras, on behalf of CalPERS, determined that sewer agency had improperly included in the monthly payrate for respondent Foley: the value of a car allowance (initially \$300 per month, then increased in December

⁴ Government Code section 20000, et seq.

2004 to \$1,000 per month), the value of deferred compensation (\$1,000 per month), and the value of education, registration and licensee fees (\$1,000 per month). Under sewer authority's submission of respondent Foley's compensation, his payrate for the affected years was reported to be \$19,084.26 to \$19,805.78 each month for the final years for respondent Foley's provision of employment services for the subject local agency. (The range in the monthly pay resulted from supposed increases in remuneration paid to respondent Foley.)

Upon making her close review of documents and the law, during early 2010, Ms. Lueras reasonably excluded from the calculation for pension purposes as respondent Foley's final compensation the items falling within the categories of deferred compensation, car allowance and non-reportable education incentive fees as well as license fees. Those categories could not be part of the payrate for respondent Foley. The monthly payrate for respondent Foley, under the refined calculation by CalPERS, was reduced to \$14,335.79 for the period of July 3, 2008, to December 4, 2009, and \$14,908.36 for the period of January 3, 2010, to May 4, 2010.

12. Ms. Lueras reasonably established that sewer agency's contractual agreement with respondent Foley was contrary to CalPERS regulations regarding the definition of a "compensable earnable" as monetary figures allowable for the calculation of the lawful pension to which respondent Foley may expect to be paid by CalPERS .

And Ms. Lueras persuasively demonstrated that petitioner's Division personnel's determinations in this matter were correct within the meaning of the applicable Government Code and California Code of Regulations provisions. Petitioner's representative, Ms Lueras, was credible when she testified that the excluded categories (namely, the value of deferred compensation, car allowance, and non-reportable education incentive with licensure fees) are not lawfully eligible to be included in the calculation of respondent Foley's payrate in the process of prescribing the pension to be paid him by CalPERS. And those items could not be deemed as "special compensation."

13. As part of her thorough analysis, Ms. Lueras determined that the matter of deferred compensation, despite Amendment No. 2, executed in December 2004, was not includible as payrate for purposes of ascertaining the final compensation for retirement benefit calculation for respondent Foley. And the Retirement Program Specialist advanced that the attempt by respondent Foley and sewer authority to craft an agreement during November 2011 could not alter the category of the deferred compensation. Such efforts to reform terms of the employment contract after respondent had entered retirement status caused the reformation of the value of the deferred compensation to fall into the meaning of "final settlement pay," which cannot be used to calculate the retirement benefit (pension).

14. Ms. Lueras was persuasive when she offered extensive testimony regarding the topic of "deferred compensation," even with regard to the definition as set out in "Amendment No. 1 to the At Will Employment Agreement for Manager." Although the agreement reads, "[sewer authority] shall pay [respondent Foley] one-twelfth of the maximum annual IRS authorized level each month for each month [respondent Foley] is

employed by [sewer authority] under this Agreement, so long as [sewer authority] maintains its present retirement program of 2%/ 55 years PERS program.” Ms. Lueras deemed the amendment to make no difference to the CalPERS analysis. No difference in the CalPERS analysis comes about because the Amendment No. 1 language continued to be viewed as a conversion into benefits for payrate analysis. Such a conversion constitutes a fiction that is intended to impermissibly inflate the retirement benefit to respondent Foley.

15. In addition to the foregoing, Ms. Lueras persuasively outlined that the contractual categories of a car allowance, deferred compensation, payments for educational registration fees and licensure payments on behalf of respondent Foley were deemed to be reimbursements. As a reimbursement scheme, the funds so paid to respondent Foley cannot be included in payrate for purposes of determining final compensation.

16. Ms. Lueras was thorough, reasonable and objective in her review of the information provided by respondent Foley and the sewer authority. Ms. Lueras correctly interpreted the Public Employees Retirement Law and the CalPERS regulation that are applicable to the facts of this matter.

17. Ms. Lueras provided a thorough review of final settlement pay as defined under the CalPERS regulations (Cal. Code Regs., tit 2, § 571, subd. (b).) And, she offered compelling testimony regarding reportable compensation. In particular, Ms. Lueras pointed to a CalPERS pamphlet, as published during October 2007, that noted that as special compensation, which are items not reportable to CalPERS for calculation of pensions, excluded items include: “employer payment to deferred compensation,” any “automobile allowance,” or “conversion of benefits to salary.”

18. Ms. Lueras presented compelling and persuasive testimony regarding the notorious *City of Bell* matter. In that case, an abuse upon the CalPERS system arose with regard to the distortion of “salary” in an instance, such as the matter involving respondent Foley, where there was no publicly available pay schedule for highly compensated senior management personnel. The *City of Bell* case casts a shadow over this matter because of the question of “spiking” compensation. Spiking is a scheme, by a local agency employer to dramatically inflate the pension benefit to a favored employee of the local agency through a fiction perpetuated upon CalPERS and its legion of members, by creatively enhancing final compensations components.

Respondent Foley’s Evidence at the Hearing

SCOTT THOMAS BOYD

19. Scott Thomas Boyd (Mr. Boyd) offered evidence on behalf of respondent Foley.

Mr. Boyd is currently a member of the board of directors for sewer authority. He was a member of the board when respondent Foley was first hired in 2003 to work for sewer authority.

20. Mr. Boyd offered an historical account of the rationale of sewer authority's board in setting compensation for respondent Foley, who was viewed as assuming duties and functions that would have required the subject board to hire two professionals to perform the duties assigned to respondent Foley. Hence, the board had an intention to fully compensate him for his expansive duties and responsibilities as well as to assure that he received a pension commensurate with his services to sewer authority. Hence, according to the account given by Mr. Boyd, sewer authority's board uniformly believed that the value of a car allowance, the value of education allowance, the value of license fees, and deferred compensation were to be a part of the calculation for setting respondent Foley's pension.

21. During 2011, Mr. Boyd was the chairman of sewer authority's board of directors that ratified a contractual amendment that retroactively revised the employment contract between the sewer authority and respondent Foley. The contract amendment, which was executed on November 11, 2011, retroactively revised the terms of the December 20, 2004, contract of employment.

22. Mr. Boyd unbelievably asserted at the hearing of this matter that during 2004 he and sewer authority's board members were under the mistaken impression that all aspects of the remuneration paid to respondent Foley were "pensionable." He further unconvincingly advanced that only in recent years after respondent Foley had entered retirement status, did sewer authority's board members realize that a mistake had occurred in crafting the original contract of employment so as to set out categories of remuneration to respondent Foley under descriptions of "car allowance," "deferred compensation," as well as "education, registration and license" fees.

23. Mr. Boyd was not persuasive with regard to measures taken by the board of directors for sewer authority in order to amend the items of gratuities paid to respondent Foley so that all the money paid to him "fit" into the allowable criteria for calculation of final compensation as grounded upon payrate. In particular, on November 11, 2011, sewer authority's board of directors passed a resolution that ratified an agreement with respondent Foley that was characterized as a "settlement agreement." Under the agreement, sewer authority retroactively amended its employment contract with respondent Foley to December 20, 2004. By way of a document called "Amendment No. 2," a deletion was made of the previously mentioned value of all money paid as auto allowance, education allowance, registration expenses and license fees. Those items were recast or recategorized as payments of all-inclusive salary to respondent Foley.

24. The scheme by sewer authority's board of directors, through its November 2011 resolution to recast the value of otherwise excludible items of remuneration paid to respondent Foley, constituted the making of a "final settlement pay" arrangement. Such

sums are not permissible as money that can be calculated in arriving at the CalPERS retirement allowance that can be disbursed to respondent Foley for the rest of his lifetime.

25. Mr. Boyd was not credible when he asserted that sewer authority's board of directors along with respondent Foley suffered under a mutual mistake in first crafting the 2003 employment contract that paid remuneration to respondent Foley through categories that were not lumped into a base salary. Mr. Boyd was not believable in his testimony that the parties to the local agency's employment contract meant for the categories in controversy to have been deemed "compensation earnable" and placed into the payrate used to calculate the retirement benefit for respondent Foley.

26. Mr. Boyd could not establish that when respondent Foley worked for sewer authority there was a publicly available pay schedule for the position of general manager, which was the position into which the individual respondent was hired. The subject local agency never published a publically available pay schedule for respondent Foley.

27. Mr. Boyd did not refute the determination reached by CalPERS personnel that sewer authority set out during late 2011 to unduly enhance the retirement benefit payable to respondent Foley to the detriment of all other CalPERS retirees through a scheme to "fit" the disputed categories of remuneration into compensation earnable. Mr. Boyd provided insufficient evidence that petitioner erred in disallowing into payrate for compensation earnable. He was not believable that in 2003 and 2004 the value of a car allowance, the value of deferred compensation as well as the value of education registration fees along with the value of licensee fees were intended by the board of directors for sewer authority as being inclusive in the entire "pensionable" compensation paid to respondent Foley as opposed to those categories of remuneration being distinct fringe benefits paid to the senior manager for sewer authority.

28. Sewer authority board's action during November 2011 constituted the making of a final settlement agreement.

MS. JEANNETTE TRACY

29. Ms. Jeannette Tracy offered testimony at the hearing of this matter.

Sewer authority has employed Ms. Tracy since 1985.

30. When respondent Foley served as general manager for sewer authority, Ms. Tracy held the classification of Supervisor of Administrative Services. Among the duties performed on behalf of sewer authority, Ms. Tracy made all reports regarding contributions to CalPERS for all employees. While Mr. Boyd did not participate in the day-to-day operations of sewer authority regarding reports made to CalPERS, Ms. Tracy was the sewer authority's employee who was the key functionary who interacted with CalPERS.

Ms. Tracy was credible when she testified that neither Mr. Boyd nor any board member asked her about the reports that she made to CalPERS regarding respondent's Foley's compensation.

31. When Ms. Tracy made reports to CalPERS regarding contributions for sewer authority employees, there were approximately a dozen to 14 employees of the subject local agency. Respondent Foley was the only employee of sewer authority who received remuneration in addition to salary for such benefits as a car allowance, reimbursement for educational course registration expenses and deferred compensation for use in building a 457 retirement fund account.

32. Ms. Tracy established that although other sewer authority employees worked under publically published MOUs (memorandum of understanding) under documents pertaining to salary ranges, respondent Foley's position as manager had no such publically available pay schedule.

33. Ms. Tracy acknowledged that she did not realize a difference between remuneration payable to an employee that was taxable earnings versus "pensionable compensation" as reportable to CalPERS.

Ms. Tracy's credible testimony contradicted the essential elements of respondent Foley's testimony and arguments.

34. Ms. Tracy was credible in the portion of her testimony that directly contradicted the assertions made by Mr. Boyd when he testified.

RESPONDENT JOHN F. FOLEY

35. Respondent Foley offered testimonial evidence at the hearing of this matter.

36. On May 2, 2003, respondent Foley and sewer authority executed an employment contract. The original employment contract provided respondent Foley with a salary of \$10,375 per month. In addition to his salary he was paid a monthly car allowance, made eligible to participate sewer authority's 457 deferred compensation plan, and given the monetary benefit of professional license fees, dues, as well as costs of educational conferences and subscriptions to professional publications.

Respondent Foley's contract was first amended so as to have an effective date of December 20, 2004. The amendment recognized respondent Foley's right to collect from the sewer authority a car allowance, the value of a monthly 457 contribution (deferred compensation), and an aggregate amount of \$1,000 for the value of education costs, educational registration fees, and license fees.

37. During December 2005, respondent Foley finalized an agreement with CalPERS that allowed him to purchase additional retirement service credits. In 2006,

respondent Foley began making payment under the “ARSC” program. The payments were taken from his salary at a monthly rate of \$4,553.70 for 52 months. The ARSC purchase resulted in respondent Foley receiving five years of service credit being added to the service credit earned by him. His then-prospective retirement benefit was accordingly increased.

38. Respondent worked as the manager for sewer authority for seven years as he retired during 2010.

39. Respondent Foley did not prove that the money paid by sewer district for a car allowance, employer-paid deferred compensation and education, registration and license reimbursement fees, come within the statutory and regulatory definition of payrate, or that the money may be classified as special compensation.

40. Respondent Foley was not persuasive that the doctrine of equitable relief (Civil Code section 3399) should be applied in this matter in order to allow the November 2011 reformation of the contract between sewer authority and respondent Foley. Such acceptance of the November 2011 Amendment Number Two would redefine the items of remuneration to become part of the gross payrate for respondent Foley. There is no proper basis for application of equitable relief on this topic so as to reverse the determination made by CalPERS.

Ultimate Findings

41. Neither fraud nor mutual mistake of the respondent Foley and sewer authority revolved around the original employment contract or its first amendment on the topic of the categories of remuneration that would be paid to respondent Foley. It is not credible that six years after the parties first agreed to the employment contract and one year after respondent Foley entered retirement status that a mistake was identified that would enable the parties to reform the employment contract so as now to spike the pension allowance (retirement benefit) that CalPERS must now pay respondent Foley and his spouse into the future.

42. CalPERS perpetrated no unlawful injury upon respondent Foley by the action taken through the determination made, and expressed, through the CalPERS letter issued during August 2010.

LEGAL CONCLUSIONS

Burden of Proof

1. The burden of proof rests upon respondent Foley to establish that the exclusion by CalPERS of challenged categories of reimbursement paid to him as the public employee was erroneous with regard to determining compensation earnable in calculating the retirement benefit to which CalPERS is obligated to disburse. (*In the Matter of the Final*

Compensation Determination of George Abbond (1999) CalPERS Precedential Decision 99-02; *McCoy v. Board of Retirement* (1986) 183 Cal.App.3d 1044, 1047.)

The Constitutional Mandate

2. Article XVI, section 17 of the California Constitution provides as follows:

The assets of a public pension or retirement system are trust funds and shall be held for the exclusive purpose of providing benefits to participants . . . and defraying reasonable expense of administering the system.

Administration of the Retirement Fund

3. The CalPERS retirement fund was established as a trust, to be administered in accordance with the provisions of the Public Employees Retirement Law solely for the benefit of the participants. (Gov. Code, § 20170.) The management and control of the retirement system is vested in the CalPERS Board of Administration. (Gov. Code, § 20123.) The CalPERS Board of Administration has the exclusive control of the administration and investment of the Retirement Fund. (Gov. Code, § 20171.)

The Nature of the Fund and Determination of Service Benefits

4. As noted in *Hudson v. Board of Administration* (1997) 59 Cal.App.4th 1310, 1316, the Public Employees' Retirement Law (PERL) establishes a retirement system for employees of the State of California and participating local public agencies. CalPERS personnel determine employees' retirement benefits based on years of service, final compensation and age at retirement. The system is funded by employer and employee contributions calculated as a percentage of employee compensation. CalPERS determines employer contribution rates based on compensation figures and actuarial assumptions. CalPERS periodically adjusts employers' rates to compensate for any inaccuracy in those actuarial assumptions. Employee rates, in contrast, are fixed by statute.

A CalPERS member's pension is "calculated to equal a certain fraction of the employee's 'final compensation,' which is multiplied by a fraction based on age and length of service." (*City of Sacramento v. Public Employees Retirement System* (1991) 229 Cal.App.3d 1470, 1478.) The determination of the benefits and the items for payrate as properly includible in final compensation are critical to computing the member's ultimate retirement benefit (pension). The PERL, and the CalPERS regulations, set forth detailed rules to guide that determination.

5. In a similar vein *Pomona Police Officers' Assn. v. City of Pomona* (1997) 58 Cal.App.4th 578, 584, noted that CalPERS is a defined benefit plan that sets an employee's retirement benefit upon the factors of retirement age, length of service and final compensation. Retirement allowances are therefore partially based upon an employee's

compensation. 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. The scope of compensation is also critical to setting the amount of retirement contributions, because CalPERS is funded by employer and employee contributions calculated as a percentage of employee compensation. And "statutory definitions delineating the scope of CalPERS compensation cannot be qualified by bargaining agreements. [Citation omitted.] Nor can the CalPERS Board characterize contributions as compensation or not compensation under the PERL, those determinations are for the Legislature. [Citation omitted.]" (*Pomona Police Officers' Assn. v. City of Pomona*, supra, 58 Cal.App.4th 578, 585.)

A member's final compensation is based on his "compensation earnable" over a defined period of time. And very important to the resolution of this controversy is the concept that final compensation cannot exceed a civil servant's compensation earnable. (Gov. Code, §§ 20037 and 20630.)

Pertinent Statutory Authority

6. Government Code section 20630 provides in pertinent part:

As used in this part, 'compensation' means the remuneration paid out of funds controlled by the employer in payment for the member's services performed during normal working hours. . . . When compensation is reported to the board, the employer shall identify the pay period in which the compensation was earned regardless of when reported or paid. Compensation shall be reported in accordance with Section 20636 and shall not exceed compensation earnable, as defined in Section 20636. (Emphasis added.)

7. Government Code section 20636 provides, in pertinent part:

(a) 'Compensation earnable' by a member means the payrate and special compensation of the member, as defined by subdivisions (b), (c), and (g), and as limited by Section 21752.5.

(b)(1) 'Payrate' 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. 'Payrate,' 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 pay schedules, for services rendered on a full-time basis during normal working hours, subject to the limitations of paragraph (2) of subdivision (e)

(c)(1) Special compensation of a member includes any payment received for special skills, knowledge, abilities, work assignment, workdays or hours, or other work conditions.

(2) 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).

(3) Special compensation shall be for services rendered during normal working hours...

[¶] . . . [¶]

(6) The board shall promulgate regulations that delineate more specifically and exclusively what constitutes 'special compensation' as used in this section. A uniform allowance, the monetary value of employer-provided uniforms, holiday pay, and premium pay for hours worked within the normally scheduled or regular working hours that are in excess of the statutory maximum workweek or work period applicable to the employee under Section 201 et seq. of Title 29 of the United States Code shall be included as special compensation and appropriately defined in those regulations.

(7) *Special compensation does not include* any of the following:

(A) Final settlement pay.

[¶] . . . [¶]

(C) Any other payments the board has not affirmatively determined to be special compensation

[¶] . . . [¶]

(e)(1) As used in this part, '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. Under no circumstances shall one employee be considered a group or class.

(2) Increases in compensation earnable granted to any 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, except as may otherwise be determined pursuant to regulations adopted by the board that establish reasonable standards for granting exceptions.

(f) As used in this part, 'final settlement pay' means any pay or cash conversions of employee benefits that are in excess of compensation earnable, that are granted or awarded to a member in connection with or in anticipation of a separation from employment. The board shall promulgate regulations that delineate more specifically what constitutes final settlement pay.

....

(Emphasis added.)

8. Government Code section 20042 provides in pertinent part:

On the election of a contracting agency . . . 'final compensation' for a local member employed by that agency whose retirement is effective or whose death occurs after the date of the election and with respect to benefits based on service to the agency shall be computed under Section 20037 but with the substitution of the period of one year for three consecutive years. . . .

Legislative History of Government Code section 20636

9. Although offered after the close of the hearing, because the request from CalPERS was made before the submission of the matter, official notice, as defined at Government Code section 11515, is taken of the 985-page Legislative History for the revised Government Code section 20636, which is set out in pertinent part, above.

The Legislative History of Government Code section 20636 begins with Senate Bill 53. That bill provided a variety of statutory changes “in response to the recently uncovered, but apparently widely used, practice of ‘spiking’ (intentional inflation)” of remuneration so as to reach a more attractive final compensation amount, which is the foremost basis upon which a retirement pension is derived for employee of local contracting agencies in the CalPERS network.

The Legislative History further makes known that before the revision of Government Code section 20636, the past PERL definition of compensation was “clearly flawed.”

Also, the Legislative History sets out that Governor Pete Wilson proclaimed that Senate Bill 53, which provided the amendment of Government Code section 20636 “would enact several changes to the Public Employees Retirement Law in an effort to curb pension abuse at the local level. This bill represents a comprehensive attempt to eliminate pension abuse in the nearly 1,700 city, county and special districts.

The Legislative History for Government Code section 20636 underscores that local agency employers are not unilaterally allowed to reclassify or redefine categories for the forms of remuneration or gratuities that comprise payrate for purposes of reaching the calculation for final compensation. Local agencies may not retroactively redefine categories of remuneration in determining the pension that CalPERS will be obligated to pay the retiring local agency employee for the balance of the individual’s lifetime.

Pertinent Regulatory Authority - Determining “Final Compensation”

10. CalPERS’s analytical approach to determine whether disputed payments should be included in a member’s “final compensation” is grounded by the California Code of Regulations, title 2, section 571, subdivision (a).

California Code of Regulations, title 2, section 571 defines “special compensation” in pertinent part as follows:

(a) The following list 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:

[¶] . . . [¶]

(b) The [CalPERS] Board has determined that all items of special compensation listed in subsection (a) are:

- (1) Contained in a written labor policy or agreement;
- (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 [CalPERS] actuarial assumptions.

(c) *Only items listed in subsection (a) have been affirmatively determined to be special compensation.* All items of special compensation reported to [CalPERS] will be subject to review for continued conformity with all of the standards listed in subsection (b).

(d) If an item of special compensation is not listed in subdivision (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.*

(Emphasis added.)

Special Compensation Does Not Include the Value of Deferred Compensation or the Value of Remuneration Paid In Lieu of Fringe Benefits Such as Car Allowance or Educational Expenses

11. Under the requirements of Government Code section 20636, subdivision (c)(6), CalPERS promulgated a regulation regarding a specifically and exclusive list of matters that constitute “special compensation.” The CalPERS Board of Administration exclusively has delineated all items of “special compensation” that may be made part of final compensation for purpose of determination of the proper retirement allowance. The delineation of such items is set out in California Code of Regulations, title 2, section 571. The value of deferred compensation or the gratuity paid in lieu of a car allowance or for the value of educational courses or licensure renewal fees as set out in the contract of employment between respondent Foley and sewer authority are not recognized under the subject regulation that governs the determination by CalPERS in calculating a retirement allowance.

Very important to this topic is that the categories of remuneration extended to respondent Foley were not set out in a generalized labor policy of the local agency. And there are rigid rules that prevent any local agency from artificially increasing the retirement

benefits for a preferred employee, such as the senior manager for sewer authority, by enabling the employee to be granted the tremendous compensation increases, which had not been made available to other similarly situated employees. (*Prentice v. Board of Administration* (2007) 157 Cal.App.4th 983, 993-995.)

Contract Negotiated in Contemplation of Retirement

12. California Code of Regulations, title 2, section 570 prohibits inclusion of final settlement pay in calculations for retirement purposes under the PERL. “Final settlement pay,” under the regulation, means “any pay or cash conversions of employee 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.” Final settlement pay is excluded from payroll reported to CalPERS, in either the form of pay rate or “compensation earnable.” And final settlement pay may take the form of any item of special compensation that is not listed in section 571 of title 2 of the California Code of Regulations.

Respondent’s Contentions as Supported by the Sewer Authority

13. Respondent Foley and sewer authority raised as a dominant contention the quality of respondent Foley’s performance in the provision of diligent, conscientious services as the manager to sewer authority directly relate to the scope of compensation that was paid him. Accordingly, they contend that the prerogative of sewer authority to set respondent Foley’s remuneration is paramount, and that the local agency’s right to reward respondent Foley’s performance of the work was grounded on those parties’ good faith in setting the significant amount of compensation for the local agency’s manager.

Respondent Foley may have rendered excellent services in his employment with the sewer authority. However, service retirement benefits are not based on a formula involving the value of the services provided by an employee. Sewer authority had the authority to set respondent Foley’s compensation as its general manager and to award him premium pay for superior performance. CalPERS does not dispute sewer authority’s right to determine how its employees should be compensated. Such compensation must be included in a publically available pay schedule. And, sewer authority cannot calculate service retirement benefits based on compensation when compensation does not qualify as “final compensation” under applicable statutes and regulations.

In this matter, sewer authority and respondent Foley attempted to manipulate the characterization of the benefits or gratuities paid to respondent Foley. Among the manipulations was their effort to represent that the November 2011 Amendment Number Two to a 2004 contract of employment did not constitute a scheme to spike the retirement benefit (pension) payable by CalPERS. The evidence, however, lead to a determination that spiking was inherent in the late 2011 final settlement agreement that resulted in the November 2011 Contract Amendment Number Two. The efforts by sewer authority and respondent Foley run counter to the controlling statute, which came about through the Legislature’s directive during 1993, in establishing clear criteria to qualify for payrate. The

reformation of the employment contract at a time that is post retirement of respondent Foley cannot serve to spike the pension that CalPERS must now pay to respondent Foley.

Effect of CalPERS Statutes and Regulations

14. In the event of a conflict between an employer's view of an employee's payrate and the calculation of CalPERS, the statutes comprising the Public Employees' Retirement Law (Gov. Code §§20000 et seq.; hereafter the PERL) supersede all employment contracts, agreements, resolutions, policies and Memoranda of Understanding as promulgated by an employer. (*Longshore v. County of Venture* (1979) 25 Cal.3d. 14, 23; *Miller v. State* (1977) 18 Cal.3d 808, 815; *Boren v. State Personnel Board* (1951) 37 Cal.2d 634, 641.)

Inappropriateness of Equitable Relief to Allow Amendment to the Employment Contract.

15. When a party seeks to reform a written contract under the authority of equitable relief as permitted by Civil Code section 3399,⁵ the party must show fraud, mutual mistake of the parties, or a mistake by one party where the mistake was suspected or known by the other party. But none of the grounds for application of equitable relief exist in this matter that would enable reformation of the 2003 contract and its 2004 amendment. A paramount requirement for application of the doctrine that reformation of objectionable language in a contract must be reformed is that the mutual mistake must be proved by "clear and convincing evidence." (*Perry v. Bedford* (1965) 238 Cal.App.2d 6.) Neither respondent Foley nor sewer authority provided clear and convincing proof of the mistake existing at the time of either the contract's drafting or its first amendment.

Furthermore, respondent Foley and sewer authority have not met the requisite criterion for reformation of the contract of employment because of "mutual mistake" under equitable principles so as to now bind CalPERS. The criterion is that the contemplated reformation can be only effected without inflicting prejudice to the rights of a third party. Should the employment contract for respondent Foley and sewer authority be reformed so as to impact compensation earnable, the result would be to allow money now excluded from calculation to be used to calculate retirement benefits payable by CalPERS to respondent Foley. Such new calculation will increase costs to CalPERS in making the prospective retirement disbursement payments to respondent Foley and his spouse. Also the future contributions that might be made by sewer authority, and its current and future employees, to CalPERS will correspondingly increase unfairly so as to pay the retirement benefit to respondent Foley.

⁵ Civil Code section 3399 provides that "[w]hen, through fraud or a mutual mistake of the parties, or a mistake of one party, which the other at the time knew or suspected, a written contract does not truly express the intention of the parties, it [contract] may be revised on the application of a party aggrieved, so as to express that intention, so far as it can be done without prejudice to rights acquired by third persons, in good faith and for value."

Another impediment to reformation is the doctrine of laches. Here, respondent Foley and sewer authority have allowed many years to pass, including the passage of respondent Foley's actual retirement date, without seeking equitable relief.

Another significant barrier to reformation of the contract is the matter of jurisdiction and proper use of pleadings. The doctrine of reformation of contract requires a civil suit in equity through properly crafted pleadings as filed in the superior court. This administrative adjudication proceeding before the CalPERS Board of Administration is the improper forum for a ruling to be attained on application of the doctrine of reformation of the employment contract at issue.

Final Settlement Pay

16. CalPERS Precedential Decision⁶ 12-01, titled *In the Matter of Appeal Regarding Calculation of Final Compensation of Craig F. Woods, Respondent, and Tahoe-Truckee Sanitation Agency, Respondent*, is controlling and dispositive of issues in this controversy.

The *Craig F. Woods* precedent decision includes: "CalPERS correctly determined that respondent's compensation earnable for purposes of calculating benefits cannot include amounts previously paid to respondent as an automobile allowance and employer paid deferred compensation CalPERS adjustment to respondent's final compensable earnable is supported by the PERL. (Gov. Code, § 20626; Cal. Code Regs., tit. 2, §§ 571 and 570.)"

In essence the regulations provide a precise, exclusive list of categories of payments to public employees that can fit into "special compensation," which can be included in the calculation for the final compensation for purposes of setting the retirement benefit (pension). If a local agency pays an employee under a heading or category of remuneration that does not fall within the regulation's ambit, the money cannot be used to calculate the future pension.

Ultimate Determinations

19. CalPERS lawfully and properly excluded from payrate categories of money, namely deferred compensation, car allowance and non-reportable education incentive money, paid to respondent Foley under contracts beginning during 2003 and amended in

⁶ Government Code section 11425.60. Of particular note is the last sentence of subdivision (b) of the subject statutory provision that reads, "An agency's designation of a decision . . . as a precedent decision is not subject to judicial review." And the first sentence of subdivision (b) of the statute recognizes the ability of an agency "to be able to make law and policy through adjudication as well as through rulemaking." (Law Revision Commission Comments to Stats. 1995, ch 938 § 21 (Senate Bill), following Gov. Code, § 11425.60.)

November 2011. And those categories or items of remuneration cannot be included in the calculation used to determine the retirement pay (pension) that is to be disbursed by CalPERS to respondent Foley, or his spouse, for their remaining respective lifetime.

20. CalPERS properly determined the forms of remuneration received by respondent Foley, which was comprised of amounts for deferred compensation, car allowance and non-reportable education incentive money, did not qualify as special compensation within the meaning of California Code of Regulation, title 2, section 571, subdivision (a).

Dispositive Conclusion

21. Good cause exists to sustain the determination of the CalPERS Chief of Customer Account Services Division that the disputed categories of remuneration, paid to respondent Foley in connection with his service as manager for sewer authority, must be excluded from the calculation of his service retirement benefit allowance.

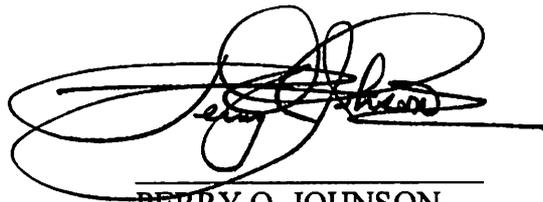
This conclusion is based on the Factual Findings and on all Legal Conclusions.

ORDER

The determination by the Chief, Employer Services Division, CalPERS, that the disputed amounts for deferred compensation, car allowance and non-reportable education incentive money, made available to John F. Foley in connection with his service as manager for Sewer Authority Mid-Coastside, be excluded from the calculation of his service retirement benefit allowance, is sustained.

The appeal of respondent John F. Foley is denied.

Dated: May 2, 2014

A handwritten signature in black ink, appearing to read "Perry O. Johnson", is written over a horizontal line. The signature is stylized and somewhat cursive.

PERRY O. JOHNSON
Administrative Law Judge
Office of Administrative Hearings