

STAFF'S ARGUMENT TO DECLINE TO ADOPT THE PROPOSED DECISION

I THE BOARD'S REQUEST FOR A FULL BOARD HEARING

At its September 17, 2014, meeting, the CalPERS Board of Administration (Board) declined to adopt the Proposed Decision in this matter and to instead decide the matter on the record after affording the parties an opportunity for further argument.¹ The Proposed Decision issued by the Administrative Law Judge (ALJ) on June 30, 2014, found that Christine Monsen (Respondent Monsen) was entitled to a CalPERS pension based on the payrate of \$17,104.92 per month that she received from the Alameda County Transportation Improvement Association (ACTIA). The ALJ rejected the position of the CalPERS staff that Respondent Monsen and ACTIA had added amounts to her final compensation that were not "compensation earnable" and therefore should not be used to calculate Respondent Monsen's retirement allowance. The Board rejected the ALJ's Proposed Decision, and determined that the matter should be brought to a Full Board Hearing at the Board's October 2014 meeting, in order to review the facts and the law.

II SUMMARY OF THE CASE

Respondent Monsen was originally hired by ACTIA in 1995 as the Deputy Director for Special Projects, and became the ACTIA Executive Director in 1998.² Respondent Monsen, by virtue of her employment, is a miscellaneous member of CalPERS. As Executive Director, Respondent Monsen was the top ranking official at ACTIA, which was governed by a board. She filed an application for service retirement and retired in 2010.

During her employment, Respondent Monsen urged ACTIA to create a 457 savings plan with CalPERS for ACTIA's employees, which ACTIA did.³ During Respondent Monsen's employment, the ACTIA board agreed to provide employer-paid deferred compensation to Respondent Monsen, in addition to payrate increases.⁴ ACTIA initially paid 50% of the maximum amount that could be contributed to a 457 savings plan. When Respondent Monsen requested further pay increases, the ACTIA board expressed concerns about public perception of the salary level of public executives, and determined to increase her remuneration in smaller salary increases and also by increasing (to 100%) the amount of employer-paid deferred compensation paid directly into her 457 account.⁵

¹ Attachment E p. 8 of 9.

² Attachment F p. 32 of 130, line 3-6. p.33 of 130, lines 19-20.

³ Attachment F p. 32 of 130, line 16-21.

⁴ Attachment F p. 34 of 130, lines 4-14. This occurred between 1997 and 2007, but Respondent Monsen could not recall the year it occurred.

⁵ Attachment F p. 34 of 130, lines 19-25; p. 35 of 130, lines 1-15.

In 2007, ACTIA's board, at a confidential meeting to discuss payrate,⁶ awarded Respondent Mosen a three percent salary increase (less than she requested), and as a separate compensation adjustment, the ACTIA board, her employer, agreed to rollover the full amount of her employer-paid deferred compensation to salary.⁷ Respondent Mosen herself told the financial officer that he should make that change in her salary, and he did.⁸ Respondent Mosen testified that she had no recollection of there being an open session of the ACTIA board on the issue of that salary change.

Upon Respondent Mosen's application for service retirement in 2010, CalPERS determined that her employer-paid deferred compensation was not "compensation earnable,"⁹ even though in 2007 that benefit had been rolled into her salary. CalPERS staff noted that ACTIA and Respondent Mosen added the exact amount of employer-paid deferred compensation (which is not compensation earnable) to Respondent Mosen's salary, increasing Respondent Mosen's final compensation amount creating final settlement pay three years prior to her retirement. CalPERS determined that adding the amount of the employer deferred compensation to Respondent Mosen's salary did not change its nature to compensation earnable.¹⁰ CalPERS determined that ACTIA had over-reported the compensation earnable of Respondent Mosen (in the amount of the employer-paid deferred compensation which had been rolled into payrate), in the last three years of her employment. Respondent Mosen and ACTIA filed a timely appeal of this determination (Attachment H, Exhibit 6).

A hearing was held on March 5, 2014 and June 13, 2014, on the issue of whether employer-paid deferred compensation can be included in the calculation of Respondent Mosen's final compensation simply by calling it salary instead of employer-paid deferred compensation. In other words, the Administrative Law Judge (ALJ) was asked to decide whether Respondent's compensation earnable could include the employer-paid deferred compensation after it was rolled, for that purpose, into Respondent Mosen's payrate during her final three years of employment.

At the hearing, Respondent Mosen and her witness testified that her remuneration was initially characterized as employer-paid deferred compensation to placate the public, whom they and the ACTIA board feared would be upset by large salary increases.¹¹ CalPERS staff explained the relevant sections of the California Public Employees' Retirement Law (PERL). CalPERS staff testified that CalPERS staff must determine the nature of the remuneration to determine if it is compensation earnable. Merely

⁶ Attachment F p. 36 of 130, line 7-25.

⁷ Attachment F p. 36 of 130, lines 16 -25.

⁸ Attachment F p. 38 of 130, line 4-18.

⁹ "Compensation earnable" by a member, means the payrate and special compensation of the member... "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, pursuant to publicly available pay schedules... (Government Code §20636)

¹⁰ Employer-paid deferred compensation is not part of payrate, and cannot be added to final compensation. Employee-paid deferred compensation is part of payrate, when paid to the employee and then directed to deferred compensation accounts.

¹¹ Attachment F p. 24 of 130, lines 19-25; p. 25 of 130, lines 1-16; p. 35 of 130, line 11-15.

reclassifying the payment did not transform the over 10 year employer-paid deferred compensation benefit payment into compensation earnable. CalPERS staff cited the CalPERS Precedential Decision 12-01 *Craig F. Woods, Respondent and Tahoe Truckee Sanitation Agency, Respondent*, in support of their position. This Decision established that employer-paid deferred compensation is not compensation earnable, and cannot be included in final compensation for the calculation of a member's pension, even when reclassified as salary.

The ALJ issued a Proposed Decision on June 30, 2014, which proposed granting the appeals by Respondent Monsen and ACTIA and rejecting the determination by CalPERS staff denying Respondent Monsen's claim to employer-paid deferred compensation as part of compensation earnable. In the Proposed Decision, the ALJ held that the evidence showed that Respondent Monsen's monthly salary of \$17,104.92 per month was "publicly available" as required by the PERL. However, the ALJ did not specify what evidence supported her ruling. The ALJ also rejected the analogous reasoning in CalPERS Precedential Decision 12-01 *Craig F. Woods, Respondent and Tahoe Truckee Sanitation Agency, Respondent*, and held that Respondent Monsen's salary of \$17,104.92 did not include deferred compensation paid by her employer. The Proposed Decision concluded that Respondent Monsen was entitled to claim the additional remuneration from employer-paid deferred compensation as compensation earnable once the employer-paid deferred compensation was reclassified as salary by the employer.

III ISSUES PRESENTED

CalPERS staff argues that Respondent Monsen should not be allowed to include the amount of the employer-paid deferred compensation in final compensation, even though ACTIA and Respondent Monsen "re-labeled" that amount as payrate three years prior to her application for retirement. Staff's argument is based on the following:

- A. The Board's Precedential Decision 12-01, *Craig F. Woods, Respondent and Tahoe Truckee Sanitation Agency, Respondent* held that employer-paid deferred compensation is not "compensation earnable" for the purpose of calculating retirement benefits because it is specifically excluded by the PERL (Government Code section 20636, subd.(g)(4)(E)).
- B. The ALJ failed to identify reliable evidence of a published payrate; additionally, evidence that a pay schedule was purposely manipulated to keep salary information from the public defeats the statutory requirement of "publicly available pay schedules." (Government Code sec. 20636(b)(1), California Code of Regulations, title 2, section 570.5).
- C. The Proposed Decision does not address whether the compensation excluded by CalPERS is final settlement pay. If it is final settlement pay, it cannot be included in the calculation of Respondent Monsen's pension.

The Board and CalPERS staff have a fiduciary duty not to pay benefits in excess of those authorized by the PERL. CalPERS staff contends that the following reasons prohibit the inclusion of the reclassified employer-paid deferred compensation (\$1708.34/month) in final compensation:

- A. The Board's Precedential Decision 12-01, *Craig F. Woods, Respondent and Tahoe Truckee Sanitation Agency, Respondent* held that employer-paid deferred compensation is not "compensation earnable" for the purpose of calculating retirement benefits because it is specifically excluded by the PERL (Government Code section 20636, subd.(g)(4)(E)).

The ALJ should have applied the reasoning of the *Craig F. Woods* Precedential Decision to find that the amount of employer-paid deferred compensation that was rolled into Respondent Monsen's payrate was not compensation earnable, no matter how ACTIA and Respondent Monsen tried to disguise the true nature of those funds by rolling them into salary in 2007. If the Proposed Decision in this case were allowed to stand, it would provide CalPERS members a simple road map for accomplishing a type of pension spiking that the law has been designed to prevent. Any employer could merely inflate the base pay of any employee to account for the amount of deferred compensation that the employer had paid. This would be legal, according to the ALJ in this case, because the employer would not be (or would no longer be) DIRECTLY paying the amount into a deferred compensation plan on behalf of the employee. Surely, this would be elevating form over substance, which the law abhors.

The ALJ attempted to distinguish the *Craig F. Woods* Precedential Decision on the basis that after 2007, the employer-paid deferred compensation amount of \$1,708.34 per month was rolled into Respondent Monsen's salary, and she herself then directed it into her deferred compensation plan. Thus, the ALJ decided these amounts are not considered "employer payments" and are included in a member's payrate. (Government Code section 20636, subd. (b)(2)(A)). However, such a late re-characterization cannot change the actual character of the benefit, creating a situation where for over 10 years there was no indication it was compensation earnable. In the last three years, with its new identity, it is still not compensation earnable.

The ALJ also rejected the application of the reasoning in the *Craig F. Woods* Precedential Decision to this matter because in *Craig F. Woods*, the ALJ asserted, the employer-paid deferred compensation was directly paid by the employer into the deferred compensation plan, and because the employer's board intended to include in final payrate two different portions of Woods' salary that the board knew were disallowed. The ALJ contrasted that with Respondent Monsen's (as opposed to the employer's) direction of her deferred compensation after 2007. This misstates the facts of the *Craig F. Woods* case, where the facts closely track the facts in *Monsen*, and the ALJ's superficial analysis completely ignores the policy against spiking, elevating form over substance.

In *Craig F. Woods*, three of the Factual Findings, as follows, are pertinent to this discussion:

4. ...Respondent and CalPERS staff engaged in numerous correspondence over CalPERS' exclusion of certain amounts **paid directly to Respondent by TTSA in addition to his monthly base pay.** The additional payments consisted of a monthly car allowance of \$800 and a **\$920 monthly allowance for his deferred compensation plan (PERS 457 program)...**(Emphasis added.)

6. ...(c) Paragraph six of Agreement #2 stated that **TTSA would pay Respondent an additional \$920 per month "for deposit in Employee's retirement fund, PERS 457 program, additional retirement service credit and/or similar retirement programs."**...(Emphasis added.)

10. ...Hence, amendment #2 sought to delete all references to two components of Respondent's original compensation package: car allowance and deferred compensation, **and to subsume these components into one rate of pay.** (Emphasis added.)

The facts in the Monsen case are practically identical to those in *Craig F. Woods*. Here, the ACTIA board in 2007 gave an increase to Respondent Monsen of a three percent raise and the additional amount of \$20,500.00 (\$1708.34/month), identified as "deferred compensation." ACTIA no longer deposited any amount directly into a deferred compensation plan on Respondent Monsen's behalf, as it had for the previous 10 years. However, neither did the employer in *Craig F. Woods*. In *Craig F. Woods*, as here, the contract amendment combined into one hourly rate Woods' base salary, \$800.00 per month for an auto allowance, and \$920.00 per month for deferred compensation. As the ALJ bluntly stated in *Craig F. Woods*, "The restructuring of components of compensation does not alter the nature of the pay. The law does not respect form over substance." As such, the employer-paid deferred compensation, which had been rolled into the employee's base pay and reflected in an increased hourly rate, could not be used for purposes of calculating service retirement. The same analysis applies equally to the instant case.

B. The ALJ failed to identify reliable evidence of a published payrate; additionally, evidence that a pay schedule was purposely manipulated to keep salary information from the public defeats the statutory requirement of "publicly available pay schedules." (Government Code sec. 20636(b)(1), California Code of Regulations, title 2, section 570.5).

The ALJ should have determined that there was no publicly available pay schedule, as required by Government Code section 20636 subd.(b)(1) and California Code of Regulations, title 2, section 570.5. The now defunct agency, ACTIA, did not present at the hearing any credible proof of publication of its pay schedules. To the contrary, testimony at the hearing by witnesses for ACTIA and Respondent Monsen actually supported a finding that there were no publicly available pay schedules. Testimony

established that Respondent Monsen's payrate was discussed in closed sessions of the ACTIA board.¹² Respondent Monsen's testified that the amount of payrate and changes to payrate were occasionally reported,¹³ but no witness could credibly point to a process or requirement that made these pay schedules publicly available. An agency's mere willingness to respond with such information, if asked, does not constitute public availability. The most that this testimony established was that subsequent entities, which supplanted ACTIA, created websites that contained Respondent Monsen's payrate information, without reference to when that happened.

Additionally undermining Respondent Monsen's testimony on this point, both Respondent Monsen and her witness testified that neither could verify publishing her payrate information during the time the pay schedule was in effect, and they admitted they did not want the public to know the payrate details due to concerns the public would react negatively to this information.¹⁴ While ACTIA and Respondent Monsen wanted to provide Respondent Monsen with a six percent pay increase, the testimony from the Mayor of Union City and Respondent Monsen was that a salary increase that large was not politically palatable, so they reduced the raise to three percent and boosted the employer contribution to deferred compensation (previously only half of the maximum 457 contribution) to 100 percent of the maximum 457 plan contribution. This was an attempt to conceal the pay increases by awarding them through a vehicle other than payrate. ACTIA wanted to have its cake and eat it too: Respondent Monsen would receive high pay increases, the money would be cloaked in another method of remuneration (employer-paid deferred compensation), the public would not be upset by provocatively high salaries, and in the last three years of Respondent Monsen's employment the payments could be reclassified as salary thereby benefiting Respondent Monsen by increasing the amount of her pension. They could please the public and employees.

In response to Respondent Monsen's affirmative defense that she and the ACTIA board were merely attempting to conceal a pay increase to keep from upsetting the public with the large salaries paid to public servants, and that Respondent Monsen wanted to "relieve the angst of the Board" over this concern for the public's displeasure, CalPERS staff submits this is the very type of behavior that the requirement for published payrates was created to combat. The Statement of Issues set forth the statutory requirement of published payrates. Respondent Monsen's reasons for concealing payrate - to avert political disapproval - undercut the statutory requirements for compensation earnable. This attempt to conceal pay increases was an attempt to subvert the publicly published payrate requirement.

There is no credible evidence in the record to support the assertion that Respondent Monsen's pay schedules were published. To the contrary, there is plentiful testimony that both ACTIA and Respondent Monsen were trying to disguise the true total

¹² Attachment F p. 36 of 130, lines 11 – 24; p. 37 of 130, line 1.

¹³ Attachment F p. 36, lines 21 to 25; page 37, lines 1 – 11.

¹⁴ Attachment F p. 24 of 130, lines 19 -25; page 25, lines 1 – 22; page 26 of 130, lines 3 – 21; page 34 of 130, lines 7 – 25; and page 35 of 130, lines 1-17.

remuneration paid to Respondent Monsen.¹⁵ This lack of credible evidence could explain why the ALJ did not cite to any evidence to support her conclusion that Respondent Monsen's payrate information had been publicly available. Employer-paid deferred compensation is not compensation earnable. ACTIA, having taken elaborate steps to conceal from the public the amount of pay increase it gave to Respondent Monsen, should be legally constrained from then re-characterizing the employer-paid deferred compensation as an increase in base pay.

C. The Proposed Decision does not address whether the compensation excluded by CalPERS is final settlement pay. If it is final settlement pay, it cannot be included in the calculation of Respondent Monsen's pension.

California Code of Regulations, title 2, section 570 establishes that "Final settlement pay' 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 reporting to PERS, in either payrate or compensation earnable...it is generally, but not always paid during the period of final compensation."

The ALJ did not make any findings addressing the issue of "final settlement pay." Respondent Monsen presented evidence from two witnesses (in her case, prior to CalPERS questioning) that Respondent Monsen did not originally intend to retire three years after she, as Executive Director, rolled her employer-paid deferred compensation into her payrate.¹⁶ Respondent Monsen testified that she retired in 2010 because she did not want to re-apply for her position when ACTIA was absorbed into another agency.¹⁷ Her testimony put the issue of final settlement pay before the hearing officer. However, while Respondent Monsen was attempting to refute the violation of the final settlement pay rules, her testimony was neither logical nor credible. She stated that while she did not want to retire, she did not apply for the job because others might be discouraged by her application.¹⁸ That is not the action of an employee who wants to maintain her job.¹⁹

IV CONCLUSION

Based on the Government Code sections on compensation earnable, publicly available payrate and final settlement pay, as well as the findings and conclusions in CalPERS Board Precedential Decision *Craig F. Woods*, CalPERS staff urges the Board to reject

¹⁵ Attachment F p. 24 of 130, lines 19-25; p. 25 of 130, lines 5-17; p. 35 of 130, lines 2-15.

¹⁶ Attachment F p. 39 of 130, lines 4-15.

¹⁷ Attachment F p. 39 of 130, lines 16-25; p. 40 of 130, lines 1-11.

¹⁸ Attachment F p. 40 of 130, lines 1-14

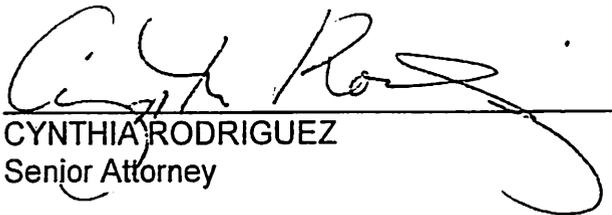
¹⁹ Attachment F p. 24 of 130, lines 7-8.

Also, Respondent Monsen's witness Mayor Green testified: "In my opinion, had she applied, she would have been given the position." Attachment F p. 23 of 130, lines 13-15.

Mayor Green also testified that "I repeatedly tried to get her to apply and I was repeatedly, unfortunately, denied her doing so." Attachment F p 24 of 130, lines 7-8.

Respondent Monsen's appeal of the CalPERS determination that she should not be allowed to consider her employer-paid deferred compensation as final compensation. The Board's final Decision should be in full support of the Board's Precedential Decision in *Craig F. Woods*.

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