ATTACHMENT B

STAFF'S ARGUMENT

STAFF'S ARGUMENT TO ADOPT THE PROPOSED DECISION

Respondent Daniel Klaff (Respondent Klaff) was employed by the Association of California Water Agencies – Joint Powers Insurance Authority (Authority). The Authority was a local public agency that contracted with CalPERS to provide retirement benefits to its employees. By virtue of his employment, Respondent Klaff was a local miscellaneous member of CalPERS. Respondent Klaff service retired. Following a review of his file, CalPERS determined that a lump sum payment made to Respondent Klaff in the final year of his employment, prior to his service retirement, could not be included in Respondent Klaff's final compensation for purposes of calculating his service retirement allowance. Respondent Klaff appealed CalPERS' determination and a hearing was held on October 29, 2014.

Prior to the hearing, CalPERS explained the hearing process to Respondent Klaff and the need to support his case with witnesses and documents. CalPERS provided Respondent Klaff with a copy of the administrative hearing process pamphlet. CalPERS answered Respondent Klaff's questions and clarified how to obtain further information on the process.

The facts in this matter are not in dispute. Respondent Klaff testified that he was first employed by the Authority in 1991. In 1995, he was appointed to be the Chief Executive Officer (CEO) of the Authority. Respondent Klaff continued to work for the Authority in the capacity of CEO. The Authority and Respondent Klaff entered into a written employment contract in 2007, the terms of which were in effect at the time of Respondent Klaff's service retirement in 2011. The written contract provided, in relevant part, as follows:

> "3.9 Pay Upon Termination of Employment
> 3.9.1 – If the Authority terminates the CEO for any reason other than gross incompetence,...or if the CEO terminates his employment on or after his 65th birthday, the CEO shall be paid <u>as severance pay</u>, a lump sum cash payment equal to 2 months salary at his then current rate. If the Authority terminates the CEO for gross incompetence, the CEO shall be paid no <u>severance pay.</u>"
> (Emphasis added.)

Respondent Klaff testified that, when he retired in October 2011, his monthly salary was $18,333.33. He also stated that he had turned 65. Accordingly, consistent with the above-quoted terms of the written employment agreement, the Authority made a one-time, lump sum payment to him in the amount of $36,666.67. The Authority had reported this payment to CalPERS and had characterized it as an item of special compensation, specifically "Management Incentive Pay."

Respondent Klaff testified that the provision to pay him two months salary was intended as an incentive to keep him working for the Authority as its CEO up to and beyond his 65th birthday.

A Retirement Program Specialist II (RPS II) testified that the lump sum payment to Respondent Klaff in his final year of employment did not meet the definition of Management Incentive Pay. Rather, it met the definition of Final Settlement Pay and, as such, had to be

excluded from Respondent Klaff's final compensation for purposes of calculating his service retirement allowance.

"Special compensation," as defined in the California Public Employees' Retirement Law (PERL), "includes a payment received for special skills, knowledge, abilities, work assignment, workdays or hours, or other special conditions." (Government Code section 20636(c)(1)). The $36,666.67 payment to Respondent Klaff was not made for any of those reasons. By regulation, items of special compensation must also meet additional criteria including that they not be "paid exclusively in the final compensation period" nor be considered "final settlement pay." (Cal. Code of Regulations, title2, section 571 (b)(7) 7 (8).)

Final settlement pay is defined in the PERL as "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 pay rate or compensation earnable." (Cal. Code of Regulations, title 2, section 570.)

After considering all of the documentary evidence and testimony, the Administrative Law Judge (ALJ) found as follows:

> "CalPERS correctly determined that the $36,666.67 reported by the Authority as 'management incentive pay' was in essence 'final settlement pay' as defined under the PERL. This type of compensation received in the final compensation period is excluded from payroll reporting to CalPERS as either payrate or compensation earnable. As such, it cannot be used in the calculation of respondent's retirement allowance."
> (Factual Finding No. 13.)

The ALJ concluded that Respondent Klaff's appeal should be denied. The Proposed Decision is supported by the law and the facts. Staff argues that the Board adopt the Proposed Decision.

Because the Proposed Decision applies the law to the salient facts of this case, the risks of adopting the Proposed Decision are minimal. The member may file a Writ Petition in Superior Court seeking to overturn the Decision of the Board.

February 19, 2015

Rory J. Coffey

RORY J. COFFEY
Senior Staff Attorney