

ATTACHMENT C

**RESPONDENT'S ARGUMENT REGARDING THE
PETITION FOR RECONSIDERATION
(INCLUDED IN THE PETITION FOR RECONSIDERATION)**

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BY FAX AND BY MAIL

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Re: James Towns, Respondent
CalPERS Case No. 2014-0254, OAH Case No. 2014070494

Dear Ms. Swedensky:

Attached please find James Towns' *Respondent's Argument* for consideration by the Board of Administration at its December 21, 2016 meeting concerning Mr. Towns' *Request for Reconsideration* of the Board's adoption of the *Proposed Decision* issued by ALJ David B. Rosenman.

This *Respondent's Argument* is being filed by December 9, 2016, pursuant to the December 2, 2016 letter from General Counsel Matthew Jacobs.

The attached *Respondent's Argument* supplements the arguments made in Mr. Towns' *Request for Reconsideration* and in other pleadings and arguments made in the administrative process.

Should you have any questions or need further information, please do not hesitate to contact me.

Sincerely,



John Michael Jensen

JMJ:gm
Enclosure
cc: Matthew G. Jacobs, CalPERS General Counsel

James Towns' Respondent's Argument
CalPERS Case No. 2014-0254, OAH Case No. 2014070494

Respondent James Towns has filed a *Request for Reconsideration* of the Board of Administration's November 16, 2016 adoption of Administrative Law Judge David Rosenman's *Proposed Decision* in the above-captioned administrative appeal.

This *Respondent's Argument* supplements the *Request for Reconsideration* filed with CalPERS on December 2, 2016 pursuant to the December 2, 2016 letter from General Counsel Matthew Jacob and should be read in conjunction with it.

I. No "Conversion" or "Pension Spiking" by Mr. Towns

Mr. Towns wants to stress the need for the Board to conduct an *objective* and *neutral* evaluation of his *Request for Reconsideration* and the Board's endorsement of staff's reduction of Mr. Towns' retirement pension overall.

As demonstrated in the administrative record, CalPERS' analytical staff in the Benefit Services Unit and likely other divisions of CalPERS formed an opinion—as it turns out, one unsupported by the facts—early in the review process that Mr. Towns had engaged in intentional "conversion" of non-PERSible compensation and "pension spiking" prior to his retirement. CalPERS' legal staff, including outside counsel Steptoe & Johnson which represented CalPERS at the administrative hearing, furthered this fabrication by arguing in opening argument and in post-hearing written briefs that Towns had "unclean hands" and had essentially conspired to wrongly inflate his pension allowance.

These allegations were explicitly considered *and rejected* by the ALJ, who ruled in the *Proposed Decision* that there was insufficient evidence to prove (i.e., CalPERS had failed to demonstrate) that any conversion or attempted conversion occurred.

The allegations were also refuted by the sworn testimony of former SDRMA board member Ken Sonksen, the only surviving percipient witness to the board subcommittee that spent months evaluating and restructuring Mr. Towns' duties and ultimately offered the revamped position to Mr. Towns with a commensurate salary. As Mr. Sonksen testified at the hearing, the higher salary paid to Mr. Towns was to compensate him for the new duties and responsibilities SDRMA was retaining him to perform, and the subcommittee never considered and did not even know how much Mr. Towns had received in merit bonuses (the compensation that CalPERS' staff has alleged Mr. Towns "converted" or "attempted to convert").

The allegations were also directly contested by SDRMA, which stated in its May 24, 2013 appeal letter that "[i]t cannot be emphasized enough that at no point did SDRMA or Mr. Towns intend to or attempt to artificially inflate Mr. Towns' payrate for the purpose of increasing his retirement allowance. Rather, the compensation arrived at effective July 1, 2005, was approved by the Board after consideration of Mr. Towns' outstanding performance and the compensation paid to similarly situated chief executives of other similar agencies."

Yet CalPERS staff has continued the fiction after the *Proposed Decision* by issuing a Press Release on November 16, 2016, stating that Mr. Towns was attempting "pension spiking"

and "pension abuse" and sought to illegally "convert his merit bonuses to base salary in an effort to boost his pension".

II. History of Errors That Could Have Avoided This Dispute Had They Simply Been Raised to Mr. Towns

As the administrative body with ultimate authority over the actions of CalPERS' staff, the CalPERS Board is requested to direct staff to conduct a new and impartial evaluation of Mr. Towns' compensation and reach a fair determination of his final compensation and resulting pension calculation.

In support of this, Mr. Towns also offers the following evidence from the administrative record demonstrating that there were a number of errors made in the five years leading up to Mr. Towns' retirement by both SDRMA and CalPERS which contributed to this disputed proceeding. For example,

- CalPERS' August 13, 2012 audit of SDRMA found that SDRMA had misreported the increased compensation received by Mr. Towns from and after July 1, 2005. SDRMA never informed Mr. Towns of potential consequences of any such misreporting on his eventual retirement and pension allowance, nor did CalPERS ever inquire or instruct SDRMA to do so.
- CalPERS received reports of Mr. Towns' increased compensation for four years before his retirement. If, as CalPERS alleges, the increase somehow indicated "conversion" or other violations of the PERL, CalPERS never raised any questions or concerns to either SDRMA or Mr. Towns.
- Beginning in 2006 and continuing through 2009, CalPERS provided Mr. Towns with annual Member Statements every year which listed his contributions in the CalPERS accounts maintained in his name based on his higher salary.
- In early 2009, Mr. Towns purchased five (5) years of Additional Retirement Service Credit. CalPERS confirmed his reported compensation (another opportunity to investigate whether SDRMA had properly reported Mr. Towns' compensation) and then calculated the purchase price of the ARSC based on the higher salary, informed Towns of this calculation, and accepted payment from him.
- On October 30, 2009, CalPERS' staff provided Mr. Towns with a retirement allowance estimate and cover letter for a December 31, 2009 retirement date. The estimate utilized the payrate that CalPERS had known about for years and yet later disallowed.
- On November 3, 2009, Mr. Towns filed a Service Retirement Election with CalPERS selecting a retirement date of December 31, 2009. Testimony at the hearing, however, made clear that Mr. Towns always had the right (and would have exercised that right) to adjust this retirement date if any concerns had been raised about his expected pension allowance.
- On November 19, 2009, as Mr. Towns was drawing closer to his retirement, he

requested a review and confirmation of his payrate. Staff requested this be performed on an expedited basis.

- Finally, on December 7, 2009, CalPERS' staff performed the requested compensation and pension allowance review and confirmed, "Payrates are okay to use. Okay to calc from transcripts."

Again, any one of these multiple events or analyses could have identified possible areas of concern that might impact on Mr. Towns' pension allowance and provided the opportunity to resolve the concerns prior to his retirement. Yet nothing was ever brought to his attention until long after he had retired and his position at SDRMA had been given to another employee.

If any of them *had* been brought to Mr. Towns' or SDRMA's attention, Mr. Towns/SDRMA could have addressed such concerns before his retirement. Mr. Towns could also have delayed his retirement date to address any concerns CalPERS had, including the possible impact of the two-year "look back period" used in conjunction with Mr. Towns' three-year final compensation period.

To add insult to injury, CalPERS' staff cynically exploits this to claim that somehow *Mr. Towns* was responsible and that any damage he suffered was the result of his alleged "conversion" and "pension spiking" activities coming to fruition. Again, the ALJ that presided over the entire administrative proceeding found that there was no conversion nor any attempt at conversion.

III. CalPERS' Staff's Arbitrary and Capricious Calculation of Mr. Towns' Allowance

As pointed out in the written closing briefs to the ALJ, in Mr. Towns' *Respondent's Argument* prior to the Board's adoption of the *Proposed Decision*, and in the *Request for Reconsideration* now before the Board, CalPERS' staff has persuaded the Board that Mr. Towns is entitled to no increase in his final compensation beyond the 9.9% COLA increases received by the other SDRMA employees. This finding violates the mandate of the very section of the PERL that staff claims it is upholding in reducing Mr. Towns' final compensation.

Staff wrongly contends (a) that Mr. Towns was in a "group or class" of one, and (b) that the new compensation he received in late 2005 violates the mandate of PERL section 20636(e)(2) that compensation increases for employees not in a "group or class" must be limited to "the average increase in compensation earnable ... for all employees who are in the same membership classification."

Mr. Towns' *Request for Reconsideration* explains in detail how the "group or class" analysis performed by both CalPERS' staff and the ALJ were incorrect and contrary to the explicit terms of the PERL and directly precedential case law. Rather than repeat it here, Mr. Towns requests that the Board review that discussion.

What we focus on here is the fact that CalPERS' staff has failed to conduct the very compensation review and comparison it alleges it was required to perform.

- CalPERS' witness at the hearing admitted in sworn testimony that correctly applying

Section 20636(3)(2) meant CalPERS was mandated to look at the average of the increases received by everyone who worked at SDRMA. Yet she acknowledged that CalPERS never even *asked* about increases received by most of the SDRMA staff during its audit review and thus knew nothing about salary increases, merit promotions to higher steps on the salary scale, or any other increases.

- CalPERS' witness also admitted at the hearing that CalPERS *did* know about the salary increases received by others in the SDRMA chief officers' group, but CalPERS never included those increases in its calculation of average salary increases and instead simply assumed that the only increases any other employees received were COLA increases.
- At the very least, Mr. Towns is entitled to have his pension increased for the average percentage increase of other chief executive employees over the same time period. The *Proposed Decision* itself, as well as CalPERS' post-hearing written briefing, acknowledges that the annual salaries of others in the chief officers' group went from \$90,000 to \$129,000 during Mr. Towns' three-year final compensation period—i.e., *an increase of 43.3%*--and that they received the COLA increases *on top of* that.
- Moreover, Greg Hall, Mr. Towns' replacement as CEO, began as CEO the day after Mr. Towns' retirement at an annual salary of \$185,000. CalPERS' staff, however, has set Mr. Towns' final compensation at only \$164,610, more than \$20,000 less than the compensation received by a far less experienced and probationary CEO.

Yet CalPERS' staff has not taken any of this into consideration, despite its professed "application of the terms of Section 20636(e)(2)". Such cavalier action can only be fairly described as "unreasonable and capricious" and should not be permitted.

While Mr. Towns maintains his position that he is entitled to use all of the increased compensation in the calculation of his pension, and does not waive any of those arguments, it would go a long way toward justice if the Board grant his Petition for Reconsideration and direct CalPERS' staff to relook at its calculations of Mr. Towns' pension based on the actual terms of the PERL.

IV. Other Reasons for Granting Reconsideration

Rather than repeat the arguments made his *Request for Reconsideration*, Mr. Towns summarizes other reasons for granting reconsideration and urges the Board to review the *Request for Reconsideration* for more extensive arguments.

First, CalPERS' adoption of the *Proposed Decision* fails to acknowledge and act on the mandate that CalPERS is required to enact a *Final Decision* based on the correct law and consistent with the full and complete evidentiary record. This requirement is all the more important given CalPERS' constitutional and statutory fiduciary duties to its membership. (*Cal. Const.*, art. XVI, §17(b); *Gov't Code*, §20151.)

Second, the Board should direct CalPERS' staff to withdraw the November 16, 2016 Press Release with its false and frankly defamatory statements accusing Mr. Towns of

"conversion" and "pension spiking". The administrative record showed precisely the opposite, including an explicit finding by the ALJ in his *Proposed Decision*, and the Board should not permit the agency to be associated with such untrue statements.

Third, the Board should direct staff to discard its apparently preconceived notions about Mr. Towns' salary increase and instead consider the sworn testimony of former SDRMA board member Ken Sonksen, the only surviving percipient witness, demonstrating that the higher compensation was based on the fact that Mr. Towns would be performing new and more complex duties and responsibilities.

Fourth, the Board should direct staff to apply the law as it actually exists concerning whether Mr. Towns was part of a "group or class". This includes rejecting the arguments of CalPERS' staff and the findings of the *Proposed Decision* on at least three grounds:

(1) Any determination of "group or class" must apply the specific criteria laid out in PERL section 20636(e)(1). There is no authority to substitute other criteria never mentioned in the statutes.

(2) Any *Final Decision* must reconcile the mutually contradictory positions in the *Proposed Decision* that either (i) Mr. Towns performed the same duties as CEO after 2005 as he had before that (meaning he was now *sharing* those duties with COO Greg Hall) and they were thus in the same "group or class" and there is no authority to apply the two year "look back" period in evaluating Mr. Towns' 2005 salary) or (ii) Mr. Towns *no longer* performed the duties because they were now done by the COO, in which case Towns had *de facto* taken on a different position than he held before and thus is eligible for a corresponding new salary.

(3) Any determination of "group or class" must follow precedential case law that refutes CalPERS' staff's unsupported arguments that everyone in a "group or class" must make exactly the same salary, directly contrary to the findings in *Prentice v. Bd. of Admin., California Pub. Employees' Ret. Sys.* (2007) 157 Cal.App.4th 983 (finding that 42 managers and assistant managers were in the same group or class, yet obviously received different salaries) and in *Ventura County Deputy Sheriffs' Assn. v. Bd of Ret.* (1997) 16 Cal.4th 483 (finding that "items of 'compensation' paid in cash, *even if not earned by all employees in the same grade or class*, must be included in the 'compensation earnable' and 'final compensation' on which an employee's pension is based").

Finally, the Board should ensure that CalPERS' staff makes no effort to collect or recoup alleged pension allowance "overpayments" made to Towns, as CalPERS never raised the issue of recoupment in the *Statement of Issues* and so has no authority to carry it out without a new and separate administrative process.

V. Conclusion

By all accounts, Mr. Towns had a distinguished and honorable 38-year career dedicated to public service. The testimony, evidence and findings of the ALJ contradiction the position, statements and conclusions of CalPERS' staff.

The facts, combined with the numerous mistakes and oversight failures of CalPERS'

staff, clearly demonstrate that from the beginning of this case, there was a manufactured narrative by CalPERS' staff that has misled the Board of Administration about the facts in an attempt to support their pre-determined outcome. The facts simply do not support CalPERS' published conclusion.

The Board of Administration has the ability to reconsider and remedy this unfortunate and avoidable injustice. Mr. Towns would very much welcome the opportunity to discuss this matter further with the Board of Administration.

Mr. Towns therefore respectfully requests that the CalPERS Board (a) grant his *Request for Reconsideration*, (b) hold its own full hearing on the matter, (c) correct the errors in the *Proposed Decision* and (d) issue a new *Decision* awarding Mr. Towns the pension CalPERS originally calculated.

Anything less would be tantamount to flaunting CalPERS' mandate to act within the law simply because it enables CalPERS to reach a politically expedient result.

Dated: December 9, 2016


John Michael Jensen, Attorney for Respondent