ATTACHMENT C

RESPONDENT(S) ARGUMENT(S)
December 6, 2017

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Re: Respondents' Argument In the Matter of Calculation of Final Compensation of David A. Hall
Case. No. 2015-1236
Client-Matter: SI065/005

Dear Ms. Swedensky:

Respondents Silicon Valley Clean Water ("SVCW") and David Hall ("Hall") request that the California Public Employees' Retirement System ("CalPERS") Board of Administration ("Board") reject the Proposed Decision of the Administrative Law Judge ("ALJ") in the above referenced matter and decide the case upon the record or refer the matter to the ALJ to take additional evidence. (Gov. Code, § 11517(b)(2)(D)(E).)

SVCW had a Performance Compensation Program ("Performance Program") in place to reward its employees' superior performance and for achievement of specified performance goals.¹ The ALJ erred in finding that Performance Pay was not included in compensation earnable for the purposes of calculating retirement benefits.

The Performance Program impacts the benefits of approximately 33 employees and retirees, including Hall. For at least 15 retirees spanning a several year period, CalPERS requested documents from SVCW supporting the payment of Performance Pay. After reviewing those documents, CalPERS included Performance Pay in compensation earnable. In some cases, CalPERS even retroactively changed retirees' benefits to include Performance Pay after reviewing the relevant documents. Several years later, CalPERS reversed course without an interceding change in law and excluded Performance Pay from Hall's compensation earnable.²

SVCW and Hall request that the Board reject the Proposed Decision and elect to decide the matter itself or send the matter back to the ALJ for the taking of additional evidence.

¹ There is no dispute between the parties that a "bonus" under 2 CCR 571 is the relevant item of special compensation at issue in this appeal. (See Proposed Decision [PD], p. 13, ¶ 4.)
² CalPERS later sent letters to every employee and retiree who received Performance Pay advising them that the compensation would be excluded.
Factual Background Regarding the Performance Program

In 1984, SVCW announced a performance pay program policy. (PD, p. 4, ¶ 14.) The Performance Program is set forth in Administrative Policy No. 1984-01. (PD., p. 16, ¶ 12; Ex. G, H.) Each year, the SVCW Commission adopts a new management compensation resolution setting forth management employees’ terms and conditions of employment. (PD., p. 16, ¶ 12; Ex. E, F.) These resolutions include the Performance Program. (PD., p. 16, ¶ 12.)

The Performance Program was intended to create a more objective program for identifying performance and focused on employee safety, compliance with applicable laws and regulations regarding discharge of wastewater, and budget performance. (PD, p. 5, ¶ 17.) The Program is based on the following seven criteria: 1) personal goals, 2) lost time accidents, 3) recordable incidents, 4) the workers’ compensation experience rate, 5) permit excursions, 6) budgeting, and 7) individual performance. (Id., p. 6-7, ¶ 18-22.)

SVCW employees also receive a traditional performance evaluation, which is distinct and separate from the Performance Program. Only the goals portion of the traditional performance evaluation has any bearing on whether an employee qualifies for Performance Pay. Since the Performance Program measures different criteria and objective results, an employee may receive an average performance evaluation, but nonetheless have superior performance under the Performance Program. (Record Transcript [RT], 34:6-16.) Employees must receive a score of 5.01 or higher in order to receive any Performance Pay and must be employed on the date it is paid, which is the last pay period in June. (PD, p. 7, ¶ 23.)

In June 2014, Hall received a score of 6.225 under the Performance Program for the 2013-2014 fiscal year and received Performance Pay. (PD, p. 7, ¶ 24.) On July 28, 2015, CalPERS notified Hall and SVCW that Performance Pay would be excluded from the calculation of compensation earnable. SVCW and Hall timely appealed.

Argument in Opposition to the Proposed Decision

A. The ALJ erred in concluding that “superior” performance under the regulation cannot be based in part on group goals

Despite extensive testimony that the Performance Program is based on criteria in addition to the traditional performance evaluation, the ALJ relied only on the traditional performance evaluation, without a valid statutory or regulatory basis for doing so. (PD, p. 14, ¶ 7.)

The ALJ determined that it was a “problem” that some of the criteria under the Performance Program were based, in whole or in part, on management’s performance as a whole. (PD, p. 15, ¶ 9.) The ALJ stated that while this may have been a “very effective way to bolster cohesiveness among managers and foster recognition of their respective roles in the entity’s overall success,” it did not isolate individual performance. (Id.) There is no basis in the regulation to exclude group performance, especially where individual performance is also a
component. Indeed, the ALJ appeared to recognize the benefits of tying some criteria to management’s group performance from an organizational standpoint. (Id.) The ALJ’s decision to discount that objective is not grounded in the regulation. There is also no legal support for the ALJ’s determination that objective criteria, such as the workers’ compensation experience rate, cannot be a component of a bonus program. (Id.) Other than the language of the regulation, there is no guidance defining what type of “program or system” must be in place to evaluate “performance goals and objectives.” There is no guidance that even suggests, let alone compels, that bonus programs must be based exclusively on individual performance, and, therefore, the ALJ should not have concluded it should be excluded.

Similarly, other than stating that a bonus is “[c]ompensation to employees for superior performance such as ‘annual performance bonus’ and ‘merit pay,’” there is no guidance in the regulation or elsewhere that actually defines what is “superior” within the meaning of the regulation. At the hearing, CalPERS could not articulate any definition of “superior.” On the other hand, SVCW introduced unrebutted testimony that the Performance Program rewarded “superior” performance and that Hall’s performance was superior under the Performance Program. (RT, 34:24-35:16, 45:1-7; PD, p. 7, ¶ 23.) Therefore, SVCW’s Performance Program met the requirements of a bonus, Hall’s performance was “superior,” and SVCW and Hall request that the Board reject the Proposed Decision.

B. The ALJ correctly determined that SVCW’s Performance Program was set forth in a labor policy, but improperly determined that the score sheet must be set forth in the body of the labor policy

The ALJ correctly determined that SVCW had a labor policy setting forth the Performance Program. However, the ALJ erred in finding that the score chart must be included in the body of the labor policy.

The ALJ found that SVCW’s policy may be characterized as a “labor policy” and that the policies and resolutions are readily accessible to the public. (PD, p. 16, ¶ 12.) The ALJ concluded that the “requirements for any form of special compensation outlined in subdivision (b) of California Code of Regulations, title 2, section 571, are satisfied....” (Id.) However, the ALJ erred when he determined that the Performance Pay Program did not satisfy the requirement that the conditions of payment be stated in the labor policy because the score chart was not incorporated. (Id., p. 16, ¶ 13-14.) This analysis cannot fairly be applied to any bonus programs.

The traditional performance evaluation that forms the basis of many bonus programs is not typically set forth in the labor policy or agreement (e.g. an MOU or resolution). Under a typical bonus program, there is language in the MOU or resolution adopting a bonus program, but agencies typically use a performance evaluation or score sheet to evaluate performance (i.e. questions regarding performance and point valuation). In Respondents’ counsels’ experience, the actual performance evaluation and questions in the evaluation are never set forth in the MOU or resolution. Similarly, SVCW had a labor policy adopting the program and used a separate score sheet to assess performance, in the same way that a performance evaluation is normally
used. However, they serve the same purpose and there is no basis to treat SVCW’s program differently.

Accordingly, the ALJ erred in determining that the Performance Program did not satisfy all of the requirements of 2 CCR 571(b) simply because the scoring chart was not physically set forth in the “labor policy.”

C. CalPERS reviewed the Performance Program enabling documents on several occasions and consistently included Performance Pay in compensation earnable, including retroactively increasing retirement benefits to include Performance Pay. Therefore, the ALJ erred in rejecting Respondent’s equitable estoppel and laches defenses.

CalPERS reviewed documents related to the Performance Program on more than 15 occasions over a multi-year period and affirmatively increased retirees’ retirement allowances to include Performance Pay. (PD, p. 8, ¶ 27.) Thus, CalPERS actively represented to SVCW, after reviewing the Performance Program documents, that Performance Pay was included in compensation earnable and properly reported.

There was no follow-up from CalPERS after the documents were provided. (Id.) The Performance Pay was simply included in compensation earnable by CalPERS. In 2011, on at least two occasions, CalPERS made retroactive increases to retirees’ retirement allowances after additional documentation was provided by SVCW. (Id.) In 2014, shortly before Hall retired, SVCW asked CalPERS to review the documents. (Id., p. 8, ¶ 28.) No suggestion was made that Performance Pay was not reportable. (Id.)

SVCW and Hall were entitled to rely on the fact that CalPERS reviewed SVCW’s documents related to Performance Pay and affirmatively increased retirement benefits to include it in other cases and never excluded it until Hall retired. CalPERS intends that agencies comply when it makes a decision to include or exclude items of compensation.3 Indeed, SVCW would have had to disobey CalPERS’ prior determinations if it stopped reporting Performance Pay. CalPERS’ long-term treatment of Performance Pay shows that its own compensation review employees consistently believed that Performance Pay was reportable under the Public Employees’ Retirement Law. Thus, the ALJ erred in rejecting, SVCW and Hall’s affirmative defenses that hold to its long-term acceptance of performance pay.

1. The ALJ erred in finding that the elements of estoppel were not met and misapplied the facts to the applicable law

A party invoking equitable estoppel must show: (1) the party to be estopped is apprised of the facts; (2) the party to be estopped intended that its conduct shall be acted upon, or acts in a

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3 When CalPERS raised its concerns regarding Performance Pay to SVCW for the first time, SVCW offered to make any clarifying changes and take any action that would satisfy CalPERS. CalPERS did not provide any direction or allow SVCW to make clarifications or changes.
manner that the party asserting estoppel had a right to believe it was so intended; (3) the party invoking estoppel is ignorant of the true state of facts; and (4) the party invoking estoppel relies on the conduct to its injury. (Crumpler v. Board of Administration (1973) 32 Cal.App.3d 567, 581.) Estoppel against CalPERS is available where estoppel will not contravene the PERL. (City of Oakland v. Oakland Police and Fire Retirement System (2014) 224 Cal.App.4th 210, 243-245, as modified on denial of reh'g (Mar. 26, 2014).)

As noted above, over a multi-year period, CalPERS reviewed and consistently included Performance Pay in compensation earnable for SVCW’s retirees. (PD, p. 8, ¶ 27-28.) This compels a finding, at the very least, that inclusion of Performance Pay in compensation earnable would be a valid exercise of discretion, not an enlargement of CalPERS’ authority under the PERL. CalPERS’ reversal, after many years of affirmative ratification and directives to include Performance Pay in compensation earnable without any interceding change in law would unfairly punish SVCW and Hall, and would subject SVCW to inconsistent mandates over a several year period. (Id.) Although the ALJ speculates that CalPERS was not apprised of the facts, the testimony at the hearing was that the same documents were provided to CalPERS during CalPERS’ compensation review of other retirees as were provided for Hall. (RT, 58:15-23, 69:2-14, 77:5-10.) The ALJ did not properly apply the facts to the law concerning estoppel, and SVCW and Hall request that the Board reject the Proposed Decision on this basis.

2. The ALJ erred in determining the elements of laches were not met (18)


CalPERS’ delay was substantial, as the program has been in place for well over 20 years. Moreover, as discussed in detail above, CalPERS’ treatment of the Performance Program goes much further than mere acquiescence, as CalPERS actively and affirmatively approved of the Performance Program and its enabling documents on numerous occasions, for numerous employees, over many years. (PD, p. 8, ¶ 27-28.) SVCW, Hall, and others were prejudiced by this delay, as mitigating steps could have been taken to correct any perceived deficiencies or make clarifications. Therefore, the ALJ erred in finding that the elements for laches were not met, as CalPERS unreasonably delayed in changing course after making representations to SVCW, Hall, and others that the payments were included in compensation earnable.

D. The ALJ failed to properly apply rules of statutory construction and analyze CalPERS’ fiduciary duties in light of the facts of this case

It is well-established that the PERL must be applied liberally in favor of the pensioner, and any ambiguity or uncertainty regarding the interpretation must be resolved in favor of the pensioner. (Hudson v. Board of Admin. of Public Employees’ Retirement System (1997) 59 Cal.App.4th 1310, 1324.) However, the construction urged by the pensioner must be consistent
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with the statutory language and purpose of the statute. (Id.) CalPERS also owes its highest fiduciary duty to members of the pension system. (Cal. Const., art. XVI, § 17(a).)

CalPERS' change in interpretation, without any intervening change in the law, violates the duty owed to Hall and other current and former employees of SVCW. CalPERS' treatment of the Performance Program demonstrates that, at a minimum, there is inconsistency of opinion within CalPERS itself regarding whether Performance Pay is includable in compensation earnable and that reasonable minds could differ about its inclusion. (PD, p. 8, ¶ 27-28.) In fact, CalPERS' own witness agreed that there had been a difference of opinion within CalPERS in the past. (RT, 126:3-10, 127:13-16.) In such cases, the regulation must be liberally applied in favor of the pensioner. Therefore, the Performance Program payments should be included in compensation earnable for the purposes of calculating pension benefits.

III. **IF THE BOARD ADOPTS THE PROPOSED DECISION, THE DECISION SHOULD NOT BE MADE PRECEDENTIAL**

Even if the Board decides to adopt the Proposed Decision, the Board should not adopt the decision as precedential. The Proposed Decision does not contain “a significant legal or policy determination of general application that is likely to recur.” (Gov. Code, § 11425.60(b).) The Proposed Decision does not contain any novel legal analysis interpreting the Government Code or the regulation. The Proposed Decision also does not contain any analysis that would be generally applicable to other agencies. CalPERS characterized this as a “complex case” and different than the “normal situation” in large part because SVCW’s Performance Program is unique. (RT, 82:14-15, 118:25-119:1.) Thus, none of the elements for a precedential decision are present. Therefore, the Proposed Decision should not be made precedential.

IV. **CONCLUSION**

Based on the above, SVCW and Hall request that the Board reject the Proposed Decision, elect to decide the matter itself or send the matter back the ALJ, and include Performance Pay in Hall’s compensation earnable.

Very truly yours,

LIEBERT GASSIDY WHITMORE

Michael D. Yorulm

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