Office of Audit Services

Public Agency Review

City of Pleasant Hill

Employer Code: 0510
CalPERS ID: 7166539881
Job Number: FR12-009

July 2013

California Public Employees' Retirement System
Office of Audit Services
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July 26, 2013

Employer Code: 0510
CalPERS ID: 7166539881
Job Number: FR12-009

City of Pleasant Hill
Freda Warren, Human Resources Manager
100 Gregory Lane
Pleasant Hill, CA 94523

Dear Ms. Warren:

Enclosed is our final report pertaining to the employee/employer relationship and membership status of the City of Pleasant Hill's affiliated entity employees. Your written response, included as an appendix to the report, indicates you do not agree with the finding noted in the report. We reviewed the information contained in your agency's response pertaining to the finding and our recommendation remains as stated in the report. In accordance with our resolution policy, we have referred the issue identified in the report to the appropriate division at CalPERS. Please work with this division to address the recommendation specified in our report. It was our pleasure to work with your agency and we appreciate the time and assistance of you and your staff during this review.

Sincerely,

Original Signed By Margaret Junker
MARGARET JUNKER, Chief
Office of Audit Services

Enclosure

cc: Risk and Audit Committee Members, CalPERS
Peter Mixon, General Counsel, CalPERS
Karen DeFrank, Chief, CASD, CalPERS
Anthony Suine, Chief, BNSD, CalPERS

CITY OF PLEASANT HILL

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RESULTS IN BRIEF

The California Public Employees' Retirement System (CalPERS) Office of Audit Services (OAS) previously issued its draft compliance review of the City of Pleasant Hill's (City) payroll reporting and enrollment reporting procedures in May 2013 (Job number P10-045). This report did not include a determination or opinion as to whether employees were correctly enrolled and reported by the City. Consequently, OAS performed a second review and examined the employee/employer relationship of the individuals that worked for an affiliated entity, but were reported as common law employees of the City. A detail of the finding is noted in the Results section beginning on page three of this report.

CITY BACKGROUND

The City was incorporated as a general law city in 1961 and operates under a Council-Manager form of government. The City provides services such as police, highways and streets, public improvements, planning and zoning, general administration and redevelopment. Memoranda of Understanding (MOU) and employment agreements outline all City employees' salaries and benefits and state the terms of employment agreed upon between the City and its employees. The City contracted with CalPERS effective July 1, 1963 and provides retirement benefits for miscellaneous, police and fire employees.

All contracting public agencies, including the City, are responsible for the following:

- Determining CalPERS membership eligibility for its employees.
- Enrolling employees into CalPERS upon meeting membership eligibility criteria.
- Enrolling employees in the appropriate membership category.
- Establishing the payrates for its employees.
- Approving and adopting all compensation through its governing body in accordance with requirements of applicable public meeting laws.
- Publishing all employees' payrates in a publicly available pay schedule.
- Identifying and reporting compensation during the period it was earned.
- Ensuring special compensation is properly identified and reported.
- Reporting payroll accurately.
- Notifying CalPERS when employees meet Internal Revenue Code annual compensation limits.
- Ensuring the employment of a retired annuitant is lawful and reinstating retired annuitants that work more than 960 hours in a fiscal year.

CITY OF PLEASANT HILL

SCOPE

OAS performed and issued its draft compliance review of the City's payroll reporting and enrollment reporting procedures in April 2013. During the course of performing this review, OAS identified a potential common law employee enrollment issue in connection with individuals that provided services for the City's transportation program. As a result, OAS performed a follow-up membership enrollment review to further analyze this issue.

This follow-up review is limited to the examination of records pertaining to the employee/employer relationship of sampled employees working for the City's transportation program. The on-site fieldwork to gather additional information for this review was conducted from March 5, 2013 through March 6, 2013. The review objectives and a summary of the procedures performed are listed in Appendix B.

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OFFICE OF AUDIT SERVICES REVIEW RESULTS

Finding 1: An affiliated entity's common law employees were erroneously enrolled and reported by the City.

Recommendations:

The City should ensure that only its common law employees are enrolled and reported to CalPERS. The City should not report the common law employees of other entities.

The City should work with CalPERS Customer Account Services Division (CASD) to assess the impact of the membership enrollment issue and make the necessary adjustments to all active and retired member accounts pursuant to Government Code Section 20160.

Condition:

The City erroneously enrolled and reported the earnings of individuals who were providing services for a transportation program to CalPERS as City employees. The transportation program employees received employment benefits commensurate with City employees, including CalPERS membership.

The City indicated that the individuals in question were City employees eligible for CalPERS membership under the City's contract with CalPERS. According to City staff, the individuals followed the City's rules and regulations and the City could discipline and terminate them.

To determine whether these individuals were common law employees of the City, OAS reviewed the following documents:

- The City's published employee roster
- The City's published pay schedule
- The City's organizational Chart
- The City's comprehensive annual financial reports
- City resolutions
- A master cooperative agreement
- An administrative services agreement
- Employees' personnel files
- Employment opportunity announcements
- Employee evaluations

- Employee pay and promotion approvals
- Employee timesheets
- Employment relationship questionnaires
- Budget pages listed in the master cooperative agreement
- An administrative code
- City Invoices seeking reimbursement

OAS identified the following common law factors that support a finding of control as the individuals to CalPERS were not common law employees of the City.

1. The City Council did not create the position utilized by the individuals.
2. The City Council did not authorize nor approved the individuals' salaries.
3. The individuals do not belong to any of the City's bargaining groups.
4. The City's organization chart does not identify affiliated entities as divisions of the City.
5. The City was hired as a contractor to provide professional services.
6. The job announcements in the employees' files identify another entity as the employer.
7. The entity recruited employees through the City of Pleasant Hill.
8. The City did not approve the individuals' employment, promotions and pay increases.
9. The evaluations/salary increases for the individuals were not approved by the City.
10. The City was reimbursed for the cost associated with the individuals. The cost included the actual direct costs, and normal employee costs including program management, retirement benefits, maintenance/computer hardware and software, rent, utilities, utilities/telephone, marketing, postage, printing, office supplies.
11. The individuals' scope of work was not under the authority of the City as other City employees.
12. The City charged the entity for the costs associated with providing office space to the individuals.

After reviewing the information provided by the City, OAS determined control over the sampled individuals did not lie with the City. Therefore, the City should not have enrolled or reported the individuals' earnings to CalPERS.

For the purposes of the Public Employees' Retirement Law (PERL) and for programs administered by the Board of Administration of CalPERS (Board), the standard used for determining whether an individual is the employee of another person is the California common law as set forth in the California Supreme Court case titled *Tieberg v. Unemployment Ins. App. Bd*., (1970) 2 Cal. 3d 943, which was cited with approval in *Metropolitan Water Dist. v. Superior Court (Cargill)*, (2004) 32 Cal. 4th 491, and which was adopted by the Board in a precedential decision, *In the*

Matter of Lee Neidengard, Precedential Decision No. 05-01, effective April 22, 2005.

Applying the California common law, the most important factor in determining whether an individual performs services for another as employee is the right of the principal to control the manner and means of job performance and the desired result, whether or not this right is exercised. Where there is independent evidence that the principal has the right to control the manner and means of performing the service in question, CaIPERS will determine that an employer-employee relationship exists between the employee and the principal.

Where there is no clear independent evidence that the principal has the right to control the manner and means of an individual's performance of the services in question, CaIPERS, applying the California common law, will consider the following additional factors in determining whether an individual is an employee:

(a) whether or not the one performing services is engaged in a distinct occupation or business;
(b) the kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of a principal or by a specialist without supervision;
(c) the skill required in the particular occupation;
(d) whether the principal or the individual performing the services supplies the instrumentalities, tools, and the place of work for the person doing the work;
(e) the length of time for which the services are to be performed;
(f) the method of payment, whether by the time or by the job;
(g) whether or not the work is a part of the regular business of the principal; and
(h) whether or not the parties believe they are creating the relationship of employer-employee.

In the City's written response to our draft report, it asserted that the transportation program was not a separate, independent legal entity and the individuals that provided services for the transportation program were common law employees of the City. OAS evaluated the statements contained in the City's response; however, based on the information provided and facts obtained, OAS' recommendation remains as stated above.

Criteria:

Government Code: § 20028(b), § 20056, § 20125, § 20160 (a), § 20502

CITY OF PLEASANT HILL

CONCLUSION

OAS limited this review to the area specified in the scope section of this report and in the objectives as outlined in Appendix B. OAS limited the membership enrollment test to employee samples selected from the City's employee roster that were identified as providing services for its transportation program. OAS found that individuals who were providing services for the transportation program were erroneously enrolled and reported to CalPERS as City employees.

The finding and conclusions outlined in this report are based on information made available or otherwise obtained at the time this report was prepared. This report does not constitute a final determination in regard to the findings noted within the report. The appropriate CalPERS divisions will notify the agency of the final determinations on the report findings and provide appeal rights, if applicable, at that time. All appeals must be made to the appropriate CalPERS division by filing a written appeal with CalPERS, in Sacramento, within 30 days of the date of the mailing of the determination letter, in accordance with Government Code Section 20134 and Sections 555-555.4, Title 2, California Code of Regulations.

Respectfully submitted,

Original Signed By Margaret Junker
MARGARET JUNKER, CPA, CIA, CIDA
Chief, Office of Audit Services

Date: July 2013
Staff: Cheryl Dietz, CPA, CIA, Assistant Division Chief
Michael Dutil, CIA, CRMA, Manager
Alan Feblowitz, CFE, Manager
Jose Martinez

APPENDIX A

BACKGROUND

CITY OF PLEASANT HILL

BACKGROUND

California Public Employees' Retirement System

CalPERS provides a variety of programs serving members employed by more than 2,500 local public agencies as well as state agencies and state universities. The agencies contract with CalPERS for retirement benefits, with CalPERS providing actuarial services necessary for the agencies to fund their benefit structure. In addition, CalPERS provides services which facilitate the retirement process.

CASD manages contract coverage for public agencies and receives, processes, and posts payroll information. In addition, CASD provides services for eligible members who apply for service or disability retirement. In addition, CASD provides eligibility and enrollment services to the members and employers that participate in the CalPERS Health Benefits Program, including state agencies, public agencies, and school districts. CalPERS Benefit Services Division (BNSD) sets up retirees' accounts, processes applications, calculates retirement allowances, prepares monthly retirement benefit payment rolls, and makes adjustments to retirement benefits.

Retirement allowances are computed using three factors: years of service, age at retirement and final compensation. Final compensation is defined as the highest average annual compensation earnable by a member during the last one or three consecutive years of employment, unless the member elects a different period with a higher average. State and school members use the one-year period. Local public agency members' final compensation period is three years unless the agency contracts with CalPERS for a one-year period.

The employer's knowledge of the laws relating to membership and payroll reporting facilitates the employer in providing CalPERS with appropriate employee information. Appropriately enrolling eligible employees and correctly reporting payroll information is necessary to accurately compute a member's retirement allowance.

APPENDIX B

OBJECTIVES

CITY OF PLEASANT HILL

OBJECTIVES

The objectives of this review were limited to the determination of:

- Whether the City complied with applicable sections of the California Government Code (Sections 20000 et seq.) and Title 2 of the California Code of Regulations.
- Whether prescribed reporting and enrollment procedures as they relate to the City's retirement contract with CalPERS were followed.

This review covers the period of January 1, 2008 through December 31, 2010.

SUMMARY

To accomplish the review objectives, OAS interviewed key staff members to obtain an understanding of the City's personnel and payroll procedures, reviewed documents, and performed the following procedures.

✓ Reviewed:
- o Provisions of the Contract and contract amendments between the City and CalPERS
- o Correspondence files maintained at CalPERS
- o City Council minutes and City Council resolutions
- o City written labor policies and agreements
- o City personnel records and employee hours worked records
- o City payroll information including Summary Reports and CalPERS listings
- o Other documents used to specify payrate, special compensation, and benefits for all employees
- o The City's published employee roster
- o The City's organizational Chart
- o The City's comprehensive annual financial reports
- o A master cooperative agreement between the City and the Contra Costa Transportation Authority
- o The administrative services agreement between the City and 511 Contra Costa
- o Employment opportunity announcements
- o Employee evaluations
- o Employee timesheets
- o Employment relationship questionnaires
- o Budget pages listed in the master cooperative agreement
- o The administrative code of the Contra Costa Transportation Authority
- o City Invoices seeking reimbursement from the Contra Costa Transportation Authority

CITY OF PLEASANT HILL

- ✓ Reviewed the employee/employer relationship of the City's affiliated entity employees to determine if the employees were City employees or affiliated entity employees.

APPENDIX C

CITY'S WRITTEN RESPONSE

recycled paper

City of Pleasant Hill

June 27, 2013

Employer Code: 0510
CalPERS ID: 7166539881
Job Number: FR12-009

CalPERS
Office of Audit Services
Attn: Margaret Junker, Chief
P. O. Box 942701
Sacramento, CA 94229-2701

The City of Pleasant Hill is in receipt of the draft report on your review of our agency. (Employer Code 0510, Job Number FR12-009). We have reviewed the draft report of the review of our agency and following is our response.

The City of Pleasant Hill disagrees with the auditor's conclusion that City employees assigned to work involving TRANSPAC/511 Contra Costa were inappropriately enrolled and reported under the City's contract with PERS. While we recognize that the role of the auditor is to conduct a very narrow and focused review, this situation requires a broader view and understanding of the circumstances regarding these employees and the nature of 511 Contra Costa.

511 Contra Costa is a comprehensive transportation demand management (TDM) program that implements vehicle trip reduction and air quality programs on behalf of local jurisdictions in Contra Costa County. The programs promote alternatives to the single-occupant vehicle. 511 Contra Costa has a cooperative agreement between the cities of Clayton, Concord, Martinez, Pleasant Hill, Walnut Creek and the County of Contra Costa (on behalf of unincorporated areas of Central Contra Costa County).

The audit fails to acknowledge that 511 Contra Costa is not a separate, independent legal entity. It also fails to even consider whether 511 Contra Costa has the authority to hire employees. Nonetheless, the employees in question are properly classified as employees of the City of Pleasant Hill for PERS retirement plan purposes. It is the City that has the right to control the manner and means of job performance. Given the nature of the City's control, the organization of 511 Contra Costa and the absence of the right to control by the 511 Contra Costa Board, the City is the only logical employer.

These employees are subject to the City's personnel system, including the City's personnel rules. Recruitment and selection are completed pursuant to the requirements of the rules and under the control of the City's Human Resources Department. Like any City department, the senior manager serves as the appointing authority and makes the hiring decision pursuant to the procedures and requirements of the rules and City policy. Discipline is conducted pursuant to the rules and culminates

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in a final decision by either the City Manager or an arbitrator, depending on the level of discipline. Salaries are set based on ranges established by the City Council and established internal relationships. These employees are evaluated according to City procedures, on City forms. These employees are covered as employees under the City's insurance and group insurance policies. The auditor noted that these employees are not in one of the City's bargaining groups with a recognized representative (union). This is true because the employees are part of the unrepresented employees, like other unrepresented City employees. The auditor also noted that some recordkeeping and formalities had not been completed according to current practices. For the most part, these are issues that have evolved and persisted over the 20+ year life of the program, started mostly before current guidelines were established. They can easily be corrected going forward.

Every common law employment/independent contractor analysis involves a mix of factors. Unfortunately, the audit only reports and analyzes factors supporting its conclusion. The audit fails to report or analyze any factors that support City employment status. However, once the relevant factors are analyzed and considered in total, the factors that predominate indicate that these employees are properly classified as City employees.

Finally, the audit fails to acknowledge the long and consistent history of this relationship and the practical problems involved in the auditor's apparent solution. This is particularly true with regard to employees who are already vested or retired. Making alterations will upset the settled expectations and plans of all those involved. Further, this is not a situation that was undertaken to evade other legal requirements or to undermine the integrity of the system. In fact, the enrollment of these workers is consistent with the goal of providing for secure retirement for those engaged in public service careers and contributions have been made in support of the benefits promised, as determined by PERS.

Consequently, we request your reconsideration of the draft audit's conclusion. If there are any questions or if there is more information we can provide, please let me know.

Sincerely,

Freda Warren

Freda Warren
Human Resources Manager

/fw