ATTACHMENT A

THE PROPOSED DECISION

BEFORE THE BOARD OF ADMINISTRATION
CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM
STATE OF CALIFORNIA

In the Matter of the Appeal of Temporary Pay Rate Increase of:

DANA SUTTON KENNEDY,

and

FOOTHILL-DE ANZA COMMUNITY COLLEGE DISTRICT,

Respondents.

Agency Case No. 2021-0327

OAH No. 2021080927

PROPOSED DECISION

Administrative Law Judge Karen Reichmann, State of California, Office of Administrative Hearings, heard this matter on July 14, 2022, by videoconference.

John Shipley, Senior Attorney, represented the California Public Employees' Retirement System (CalPERS).

Attorney Bradley G. Booth represented respondent Dana Sutton Kennedy.

No appearance was made by or on behalf of the Foothill-De Anza Community College District.

The record remained open for briefing.

On August 9, 2022, CalPERS submitted a request for Judicial Notice of two exhibits, marked as Exhibits 24 and 25. No opposition was filed, and these exhibits are admitted into evidence. The parties' briefs were timely submitted and admitted into evidence as Exhibit 27 (CalPERS's brief) and Exhibit 28 (respondent's brief).

The record closed and the matter was submitted for decision on August 29, 2022.

ISSUE

Did CalPERS err in determining that a 5% pay increase for the 2018-2019 contract year, while pensionable income for "classic members," was not pensionable income for respondent because she is a "new member"?

FACTUAL FINDINGS

Stipulated Facts

The parties have stipulated to the following facts (edited slightly for clarity; footnotes from original):

1. This matter is properly before the Office of Administrative Hearings for an opinion as to whether or not a pay increase for 12 months is pensionable to "new members" as defined by the Public Employees' Pension Reform Act of 2013 (PEPRA).

2. Association of Classified Employees (ACE) is the exclusive representative for white collar employees at the [Foothill-De Anza Community College] District. Pursuant to Government Code section 3543.8, ACE has standing to sue in any action instituted in its representative capacity and on behalf of its members. All of the employees represented by ACE are also members of CalPERS.

3. Respondent Dana Sutton Kennedy (respondent Kennedy) is an employee of [the District]. Respondent Kennedy first became an employee of the District on or around April 28, 2014.

4. The District is a school public agency that contracts with CalPERS for retirement benefits for its eligible employees and whose classified employees are represented by [ACE], a bargaining unit of the District. The provisions of the District's contract with CalPERS[1] are contained in the California Public Employees' Retirement Law (PERL).

5. On August 27, 2018, the District's Board of Trustees held a meeting and approved a compensation settlement reached between the District and ACE for Classified Employees for 2017-2018 and 2018-2019 and adoption of 2017-2018 and 2018-2019 ACE salary schedules. The District's Agenda Item 23 (ACE Compensation Settlement 2017-2018 and 2018-2019) states in pertinent part:

---

[1] CalPERS is the state agency charged with enforcement and interpretation of the PERL.

The 2017-2018 and 2018-2019 settlement regarding compensation and other economic matters includes the following:

Effective July 1, 2017: Salary adjustment 0% on the ACE Classified salary schedule, Appendix C.

Effective July 1, 2018-June 30 2019: Salary adjustment of 5.00% on the ACE Salary Schedule (Appendix C), subject to the following terms.

Terms: On July 1, 2019, the ACE salary schedule (Appendix C) shall revert to the 2017-2018 salary schedule unless another agreement is reached.

6. On or about October 1, 2018, the District requested CalPERS to review its Cost of Living Allowance Memorandum for salary increase in 2017-2018 and 2018-2019 for all employee groups. The memorandum states in pertinent part:

<u>Effective July 1, 2017</u>

Salary Schedule Adjustment: A salary adjustment of "$0/0%" increase to all salary schedules, Appendices A, B, B.1, C, C.1, D, D.1, E & G

<u>Effective July 1, 2018-June 30, 2019</u>

Full-time Faculty

Salary Adjustment: A salary adjustment of 5.00% on the following full-time faculty schedules

Faculty: F1, F2, F3

Appendices A & B of the FA Agreement

Terms: On July 1, 2019, all salary schedules will revert to the 2017-2018 schedules unless another agreement is reached.

7. By email dated October 3, 2018, CalPERS informed the District that "Based on the memo and because the pay is only for the FY 2018/2019, the additional 5% cannot be reported as pay rate; rather it should be reported as Off-Salary Schedule Pay for classic members, and reflected as such in a written labor policy/agreement. It is not reportable for PEPRA members."[2]

8. By letter dated November 18, 2018, ACE's counsel requested CalPERS to allow the District to report the five percent temporary pay increase for all its members, including PEPRA members.

9. By letter dated February 4, 2019, CalPERS informed ACE's counsel that its original determination stands. The letter states in pertinent part:

> Pursuant to the Memorandum of Understanding (MOU) between the District and ACE, employees were granted a five percent increase effective July 1, 2018, through June 30, 2019. Effective July 1, 2019, this increase will automatically

---

[2] The District followed CalPERS' guidance by reporting the additional 5% as Off-Salary Schedule Pay for Classic members and adding language to their pay schedule and did not report the increase as pay rate or Off-Salary Schedule Pay for their PEPRA members.

end, and affected pay rates will return to the established pay rate levels that were in effect for the 2017-2018 contract year. This temporary increase does not meet the definition of “Compensation Earnable” or “Pensionable Compensation” as defined under the PERL.

Only compensation meeting the definition of “Compensation Earnable” for Classic members or “Pensionable Compensation” for PEPRA members is reportable to CalPERS. Pursuant to the ACE MOU, the five percent increase is only paid for a limited duration and is nullified as of July 1, 2019. Based on the temporary nature of this additional pay, it does not meet the PERL’s definition of “normal monthly rate of pay or base pay” under the definition of “Payrate” and “Pensionable Compensation.”

Additionally, this temporary pay increase does not meet the definition of any recognized type of compensation provided under C.C.R. section 571.1 which exclusively delineates the types of compensation that qualify as “Pensionable Compensation.” Accordingly, we advised the District to refrain from reporting the provisional increase, since it does not comply with the PERL. The District is required, upon contract with CalPERS, to adhere to the statutes and regulations contained in the PERL.

Calculating retirement allowance based upon a temporary pay rate increase would create a liability, that by definition,

> would be unfunded as time progresses. CalPERS has a fiduciary responsibility to ensure all compensation reported to our system is compliant with the PERL.

10. State Teachers Retirement System (STRS) is a comparable state retirement system which was also required to follow [PEPRA]. At the same time that CalPERS determined that the 5% one-year increase was not pensionable to "new members," STRS determined that it was pensionable to its "new members." Both systems are required to follow the law as dictated by PEPRA.

11. On March 11, 2019, ACE, through its counsel, filed a Petition for Preemptory Writ of Mandamus, Declaratory Relief and Other Appropriate Relief, in Sacramento County Superior Court (Court).

12. On July 10, 2020, the Court dismissed the action because CalPERS stated that it had not rendered a final decision on the pensionability for "new members" of the temporary increase, because ACE had not brought the matter before the Board of Administration through the hearing process.

13. By letter dated October 7, 2020, the District was notified of CalPERS's determination and advised of its appeal rights. To date, the District has not appealed CalPERS's determination.

14. By letter dated November 4, 2020, ACE, through its counsel, filed an appeal and has requested an administrative hearing. Notwithstanding ACE's authority under Government Code section 3543.8, ACE's counsel was informed that appeal rights were not provided to ACE; however, CalPERS agreed that if an impacted member wanted to appeal CalPERS's determination, he/she would be granted appeal rights.

15. Because ACE was denied the ability to file an appeal on behalf of its impacted members, by email dated February 23, 2021, respondent Kennedy, through her counsel, filed an appeal and has requested an administrative hearing.

16. By letter dated February 25, 2021, CalPERS acknowledged receipt of respondent Kennedy's appeal of CalPERS's October 7, 2020 determination regarding Temporary Pay Rate increase.

Other Evidence

17. The District's publicly available pay schedule for the 2018-2019 contract year for ACE-represented classified employees includes a chart with salaries for Grades 4 through 80, with 7 step levels in each Grade. The monthly salaries range from $1,766.19 for Grade 4, step 1 to $13,578.41 for Grade 80, step 7. Respondent's Grade and step level during the relevant time period, or at any time, were not established.

The following statement appears at the end of the pay schedule:

> Effective July 1, 2018 through June 30, 2019, the District provided a 5% on-schedule salary increase to the 2018-2019 salary schedules . . .CalPERS Retirement System has determined the on-schedule salary increase is considered temporary and, as such, is ineligible as creditable compensation for employees who are members of the CalPERS Retirement Plan. Therefore, CalPERS has requested the Board approve these 2018-2019 salary schedules without the 5% increase and instead include this notation to reflect that the 5% increase is creditable as Off Salary Schedule Payment (OSSP) for Classic PERS members only.

18. In September 2019, ACE and the District entered into an agreement regarding salaries for the 2019-2020, 2020-2021, and 2021-2022 contract years. This agreement provided, for the 2019-2020 contract year: "A 6.00% increase as an ongoing across-the-board adjustment to all faculty 2017-2018 Salary Schedules and equivalent increase to employee base salary."

19. For the 2020-2021 contract year, the agreement provided "An increase equal to the state approved COLA minus one-half of one percent (0.5%) as an ongoing across-the-board adjustment to all faculty 2019-2020 Salary Schedules and equivalent increase to employee base salary." The agreement further provided that if certain events altering the District's funding occurred, the parties could reopen negotiations. The agreement also provided that if certain other events transpired, the increase would not occur, and the parties would reopen negotiations.

20. For the 2021-2022 contract year, the agreement describes a number of scenarios depending on whether certain targets were met. Under certain scenarios, the salary schedules for the 2021-2022 year would be "equal to the 2017-2018 salary schedules increased by 3.5% and then compounded with half of the state provided 2020-2021 COLA," resulting in salaries lower than paid in previous years.

21. In June 2022, the District and ACE entered into an MOU regarding salaries for the 2021-2022 and 2022-2023 contract years. The MOU provides that, effective July 1, 2021, the salary schedule shall "Make the 2.5% that was temporary through June 2022, permanent, ongoing, and pensionable" and to add "an additional 5.07% ongoing, and pensionable."

LEGAL CONCLUSIONS

1. Respondent was hired by the District in April 2014. Accordingly, she is a "new member" of CalPERS subject to PEPRA (Gov. Code, § 7522 et seq).

Legal Authority Governing New Members

2. Government Code section 7522.34 defines "pensionable compensation" for new members such as respondent as follows:

> (a) "Pensionable compensation" of a new member of any public retirement system 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, subject to the limitations of subdivision (c).
>
> (b) Compensation that has been deferred shall be deemed pensionable compensation when earned rather than when paid.
>
> (c) Notwithstanding any other law, "pensionable compensation" of a new member does not include the following:
>
> (1) Any compensation determined by the board to have been paid to increase a member's retirement benefit under that system.

(2) Compensation that had previously been provided in kind to the member by the employer or paid directly by the employer to a third party other than the retirement system for the benefit of the member and which was converted to and received by the member in the form of a cash payment.

(3) Any one-time or ad hoc payments made to a member.

(4) Severance or any other payment that is granted or awarded to a member in connection with or in anticipation of a separation from employment, but is received by the member while employed.

(5) Payments for unused vacation, annual leave, personal leave, sick leave, or compensatory time off, however denominated, whether paid in a lump sum or otherwise, regardless of when reported or paid.

(6) Payments for additional services rendered outside of normal working hours, whether paid in a lump sum or otherwise.

(7) Any employer-provided allowance, reimbursement, or payment, including, but not limited to, one made for housing, vehicle, or uniforms.

(8) Compensation for overtime work, other than as defined in Section 207(k) of Title 29 of the United States Code.

(9) Employer contributions to deferred compensation or defined contribution plans.

(10) Any bonus paid in addition to the compensation described in subdivision (a).

(11) Any other form of compensation a public retirement board determines is inconsistent with the requirements of subdivision (a).

(12) Any other form of compensation a public retirement board determines should not be pensionable compensation.

(13)(A) Any form of compensation identified that has been agreed to be nonpensionable pursuant to a memorandum of understanding for state employees bound by the memorandum of understanding. The state employer subject to the memorandum of understanding shall inform the retirement system of the excluded compensation and provide a copy of the memorandum of understanding.

3. California Code of Regulations, title 2, section 571.1, further defines pensionable compensation for new members as follows:

(a) For purposes of determining "pensionable compensation" pursuant to Government Code section 7522.34 for new members under 7522.04(f), it must meet all the following four criteria:

(1) "Pensionable compensation" means the normal monthly rate of pay or base pay and;

(A) Must be for normally required duties.

(B) Must be historically consistent with prior payments for the job classification.

(C) Must be reported periodically as earned.

(2) "Pensionable compensation" is paid in cash to similarly situated members of the same group or class of employment;

(A) As used in this part, "group or class of employment" means a number of employees considered together because they share similarities in job duties, work location, collective bargaining unit, or other logical work-related grouping. One employee may not be considered a group or class.

(B) Increases in pensionable compensation granted to an employee shall be limited during the final compensation period applicable to the employee, as well as the two years immediately preceding the final compensation period, to the average increase in pensionable compensation during the same period reported by the employer for all employees who are in the closest related group or class.

(3) "Pensionable compensation" is for services rendered on a full-time basis during normal working hours; and

(4) "Pensionable compensation" is paid pursuant to a publicly available pay schedule which meets all the following criteria;

(A) Has been duly approved and adopted by the employer's governing body in accordance with requirements of applicable public meetings laws;

(B) Identifies the position title for every employee position used by the agency;

(C) Specifies the pensionable compensation amount of each identified position, which may be stated as a single amount or as multiple amounts within a range;

(D) Indicates the conditions for payment of the item of pensionable compensation, including, but not limited to, eligibility for, and amount of each component of pay;

(E) Is posted at the office of the employer or immediately accessible and available for public review from the employer during normal business hours or posted on the employer's internet website;

(F) Indicates an effective date and date of any revisions;

(G) Is retained by the employer and available for public inspection for not less than five years; and

(H) Does not reference another document in lieu of disclosing the item of pensionable compensation other than those outlined in Government Code section 20049.

(b) The following list exclusively identifies and defines the types of pay the Board has determined meet the criteria of "pensionable compensation" for those individuals that are "new members" as defined by Government Code section 7522.04(f), so long as each of the criteria in subdivision (a) have been met. For contracting agencies and school employers, all items in this subsection must be reported if contained in a publicly available pay schedule as defined in subsection (a) above.

[¶] . . . [¶]

(c) "Pensionable compensation" for all "new members" does not include all items listed under Government Code section 7522.34(c).

(d) The Board reserves the right to add to or delete from the list provided in subdivision (b) pursuant to the Administrative Procedure Act. The Board also reserves the right to add to the list of items excluded from "pensionable compensation" provided in Government Code section 7522.34(c) pursuant to the Administrative Procedure Act.

4. Regulation 571.1, subdivision (b), includes a long list of items qualifying as pensionable compensation, under the categories of Incentive Pay, Educational Pay, Special Assignment Pay, and Additional Items (Fair Labor Standards Pay and Holiday Pay are the only two items in this category). Off-Salary Schedule Pay is not on the list.

Legal Authority Governing Classic Members

5. Reportable compensation for classic members is referred to as "compensation earnable." (Gov. Code, §§ 20636, 20636.1). Compensation earnable is defined as the member's "payrate and special compensation." (*Id.*) Special compensation is defined as "payment received for special skills, knowledge, abilities, work assignment, workdays or hours, or other work conditions." (*Id.*) California Code of Regulations, title 2, section 571, is titled "Definition of Special Compensation." This regulation applies to classic members and contains a lengthy list of items that qualify as special compensation (similar – but not identical– to the list included under the definition of "Pensionable Compensation" for new members, in Regulation 571.1, subdivision (b)). In contrast to this statute and regulation, the above-cited statute and regulation applicable to new members do not contain the term "special compensation."

6. The term "Off-Salary-Schedule Pay" (OSSP) appears in California Code of Regulations, title 2, section 571, subdivision (a), under the category "Incentive Pay," and is defined as: "Compensation in addition to base salary paid in similar lump-sum amounts to a group or class of employees. These payments are routinely negotiated through collective bargaining in lieu of increases to the salary schedule. These payments are based on a similar percent of scheduled salary not to exceed six percent (6%) per fiscal year. The contracting agency or school employer may adopt similar action for non-represented groups or classes of employment as were negotiated

through collective bargaining." This language was added to the regulation, which defines what items of special compensation are reportable to CalPERS, in 1999. The regulation applies to classic members and does not apply to new members such as respondent. Although included in the regulation as a form of special compensation, OSSP does not constitute payment for "special skills, knowledge, abilities, work assignment, workdays or hours, or other work conditions."

7. CalPERS offered into evidence the Rulemaking File for the amendment to section 571 to add OSSP. The "Initial Statement of Reasons" in support of the amendment states:

> CalPERS became aware that school employers frequently negotiate "off-salary-schedule pay" in lieu of a payraise, which is then paid and reported as earned for all members of a group or class. CalPERS has determined that this type of pay satisfies the definition of compensation earnable at Government Code section 20636(c), and the regulatory funding criteria for an item of special compensation at Section 571(b). Thus it should be included in the exclusive list of such items at 571(a).

8. This history establishes that the 1999 amendment codified OSSP as reportable compensation, under the category of special compensation. The amendment was made to conform with CalPERS's determination that these payments met existing statutory requirements and should therefore be included in the "exclusive list of such items." The amendment corrected what CalPERS deemed to be an omission in the list of items that are reportable compensation for classic members. The decision to characterize OSSP as special compensation rather than payrate is not explained.

9. CalPERS contends that the specific inclusion of "Off-Salary-Schedule Pay" in the special compensation regulation pertaining to classic members, and the absence of the term in any statute or regulation pertaining to new members, signifies that such payments are not pensionable compensation for new members. CalPERS further contends that the fact that OSSP is treated as "special compensation" rather than "payrate" for classic members compels the conclusion that it cannot be considered "payrate" for new members. These contentions are rejected. The fact that CalPERS chose to include OSSP in its regulation as a form of special compensation for classic members does not prove that the legislature intended that these types of payments not be considered "payrate" for either classic members or new members. CalPERS failed to cite any Precedential Decisions or state court decisions concluding that a negotiated one-year pay increase given to all employees does not meet the definition of "payrate."

Determination of Appeal

10. In its October 2020 Determination Letter concluding that the 5% pay increase for the 2018-2019 was not reportable as pensionable compensation for new members, CalPERS stated "based on the temporary nature of this additional pay, it is not a 'normal monthly rate of pay or base pay.'"

11. The word "temporary" does not appear in either the statute or the regulation governing pensionable compensation for new members. The word "normal" is not defined in either the statute or the regulation.

12. Public employee salaries are not static; they increase or decrease for a variety of reasons. When a salary is adjusted, it does not mean that the prior salary was not "normal" for the purposes of calculating pensionable compensation.

13. Pursuant to an agreement between the District and the union representing respondent and other employees, respondent received a 5% pay increase during the entire 2018-2019 contract year. (Finding 5.) The pay increase was disclosed on the District's publicly available salary schedule. (Finding 17.) This increase was given to all similarly-situated employees; it was not an ad hoc payment to respondent. The pay was not made with the goal of unlawfully increasing respondent's retirement benefit. To the contrary, the record failed to establish whether the pay increase, if reportable as pensionable compensation, would increase respondent's retirement benefit, which will not be calculated until respondent retires. The evidence did not establish that treating the pay increase as pensionable compensation would create an unfunded liability, as alleged by CalPERS in the Statement of Issues and closing brief.

14. The 5% pay increase paid by the District to respondent during the 2018-2019 contract year meets the criteria set forth in Government Code section 7522.34. Accordingly, it is pensionable compensation.

15. Respondent met her burden of proving, by a preponderance of the evidence, that CalPERS erred in its determination that the 5% pay rate increase she received in the 2018-2019 contract year is not pensionable compensation because she is a new member.

ORDER

The appeal of respondent Dana Sutton Kennedy is granted. The 5% pay increase paid to respondent from July 1, 2018, through June 30, 2019, is pensionable compensation.

DATE: 09/23/2022

Karen Reichmann

KAREN REICHMANN

Administrative Law Judge

Office of Administrative Hearings