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March 2, 2006

REPORT TO THE HONORABLE
MAYOR AND CITY COUNCIL

RESCISSION OF INDEMNIFICATION RESOLUTION, DETERMINATION
OF CONFLICT OF INTEREST AND REVIEW OF FRAUD AND RELATED
ALLEGATIONS AS THEY RELATE TO THE PROVISION OF DEFENSE TO EMPLOYEES
AND FORMER EMPLOYEES IN *TORRES v. CITY OF SAN DIEGO* (CASE NO. GIC 852293)

INTRODUCTION

The City Attorney filed a case entitled *People v. Grissom, et. al.*, in which, among others, employees Ronald L. Saathoff, John A. Torres, Sharon K. Wilkinson, Terri A. Webster, Cathy Lexin and Bruce Herring were named as defendants. (Case No. GIC 850246; a copy of the most recent amended complaint attached as Attachment 1.) The City Attorney also filed a cross-complaint in *SDCERS v. San Diego City Attorney Michael Aguirre, et. al.*, in which, among others, employees John Torres, Ron Saathoff, Mary Vattimo, Cathy Lexin, Terri Webster, and Sharon Wilkinson were named as cross-defendants. (Case No. GIC 841 845; a copy is attached as Attachment 2.) On August 3, 2005, the City Council addressed the question of whether the City should provide a defense for these employees in these civil actions. There was a vote of 4-2 in favor of providing the defense in *People v. Grissom, et. al.* with some reservations. Because 5 votes were required, the motion failed. The matter of *SDCERS v. Aguirre, et. al.* was referred to closed session without a vote.

On August 11, 2005, plaintiffs John A. Torres, Ronald L. Saathoff, Cathy Lexin, Terri A. Webster, and Sharon K. Wilkinson filed the above-titled case in the San Diego Superior Court. On September 14, 2005, plaintiff Bruce Herring filed his complaint-in-intervention to the above titled case. The plaintiffs sought specific performance under City Council Resolution R-297335, which was adopted on November 18, 2002, and declaratory relief under Government Code section 995.

On January 20, 2006, the Honorable Linda Quinn, ruled in favor of the plaintiffs and intervener and against the City in their motions for summary judgment. Judge Quinn granted summary judgment as to their causes of action for specific performance and declaratory relief.

As to the specific performance cause of action Judge Quinn opined,

The City Council Resolution sought to be specifically enforced in this cause of action requires the defense and indemnification of all past, present and future members of the SDCERS Board of Trustees in connection with any claim or lawsuit arising from any act or omission in the scope of their duties as SDCERS Board members. The City Council recognizes all members of the SDCERS Board of Trustees as City employees. There is no provision in the City Council Resolution that the SDCERS Board of Trustees must first prove they did something wrong before the City provides a defense. The City Council Resolution is not a private contract, but a public action unanimously approved and adopted by the City Council. There is no evidence the City has withdrawn or rescinded the City Council Resolution. There is no evidence of any defense to the plaintiffs' and plaintiff-in-intervention's claims under the City Council Resolution.

As to the declaratory relief cause of action Judge Quinn opined,

The plaintiffs and plaintiff-in-intervention tendered letters requesting that City defend them in the Civil Actions, and City refused to do so. City has never determined that the plaintiffs and plaintiff-in-intervention acted because of actual fraud, corruption, or actual malice when they took the actions giving rise to the alleged liability in the Civil Actions. There is no evidence the City ever made the determination on the conflict of interest exceptions found in Govt. Code § 995.2.

The court stated that once the City Council refuses to provide a defense under California Government Code Section 995, it is required to make a finding under section 995.2, and that the failure to do so obligates the City to provide for a defense.

The City Attorney recommends that the City file a motion for reconsideration of Judge Quinn's ruling. As part of the motion, the City Attorney recommends that resolution R-297335 be rescinded and that the City Council make a determination regarding the provision of a defense to the employees in the two civil actions.

The last possible moment to file a motion for reconsideration is Monday, March 6, 2006. A copy of the Court's tentative ruling along with the transcript of the argument on the ruling is attached as Attachment 3.

DISCUSSION

This case involves litigation brought by plaintiffs John Torres, Ronald L. Saathoff, Cathy Lexin, Terri A. Webster, Sharon K. Wilkinson, Mary Vittimo and Bruce Herring, [collectively, Plaintiffs] against the City of San Diego. The litigation seeks to have the City of San Diego pay for the Plaintiffs' legal fees in civil cases which have been brought by the City Attorney against them for their personal involvement in the pension crisis. Their lawsuit sought specific performance under City Council Resolution R-297335, and declaratory relief action under Government Code section 995. The trial court granted Plaintiffs' motion for summary judgment on both grounds.

I. Rescission of Resolution.

The City Council adopted Resolution R-297335 on November 18, 2002. The pertinent paragraphs of Council Resolution R-297335 read as follows:

BE IT RESOLVED, by the council of the City of San Diego that the City shall defend, indemnify and hold harmless all past, present and future members of the Retirement Board against all expenses, judgments, settlements, liability and other amounts actually and reasonably incurred by them in connection with any claim or lawsuit arising from any act or omission in the scope of the performance of their duties as Board Members under the Charter.

The Resolution goes on to say:

BE IT FURTHER RESOLVED that the City shall have no obligation to provide any defense or indemnification under this Resolution to any Board Member who: (1) fails or refuses to cooperate with the City Attorney or such other attorney who may be engaged to represent the Board Member; or (2) refuses to consent to a settlement (a) which does not require the Board Member to make any payment or perform any act; and (b) by with the settling plaintiff(s)/claimant(s) dismiss the Board Member from the complaint (if any) and generally release the Board Member from all liability arising from the acts or omissions which are the subject of the claim or lawsuit.

Pursuant to the resolution, the City agreed to defend and indemnify all past, present and future SDCERS Board Members for, "all expenses, judgments, settlements, liability and other amounts actually and reasonably incurred by them in connection with any claim or lawsuit arising from any act." The only available exceptions to defense and indemnity under the resolution occur when an employee, "fails or refuses to cooperate with the City Attorney or such

other attorney who may be engaged to represent the Board Member; or refuses to consent to a settlement.”

After Resolution R-297335 was passed, it was discovered that SDCERS board members’ actions were in violation of numerous statutes and have exposed the City of San Diego to potential liabilities in the range between \$1.4 billion and \$2 billion.

II. The Duty to Provide a Defense Pursuant to Government Code Section 995.

California Government Code section 995 requires that the City provide a defense to any civil action or proceeding brought against a former employee in his or her official or individual capacity on account of an act or omission in the scope of employment by the City. Government Code section 995 provides, in relevant part:

Except as otherwise provided in Section 995.2 and 995.4, upon request of an employee or former employee, a public entity shall provide for the defense of any civil action or proceeding brought against him, in his official or individual capacity or both, on account of an act or omission in the scope of his employment as an employee of the public entity. . .

Plaintiffs are employees and former employees that have requested that the City provide a defense in the lawsuits which they contend are related to their acts or omissions and were in the scope of their capacity as members of the SDCERS Board. They would be entitled to a defense provided by the City unless exceptions under sections 995.2 or 995.4 were found to be applicable in this circumstance.

California Government Code section 995.2(a) provides that a public entity may refuse to provide for the defense in an action brought against an employee or former employee if the public entity determines that: (1) the act or omission was not within the scope of employment; (2) the employee or former employee acted or failed to act because of actual fraud, corruption, or actual malice; or (3) the defense of the action by the public entity would create a conflict of interest between the public entity and the employee or former employee. Upon an employee’s request for a defense, the public entity must, within 20 days, inform the employee or former employee whether it will or will not provide a defense, and the reason for the refusal to provide a defense. Cal. Gov’t. Code § 995.2(b).

California Government Code section 995.4 provides that a public entity may, but is not required to, provide for the defense of: (a) an action brought by the public entity to remove, suspend, or otherwise penalize its own employee or former employee; or (b) an action or proceeding brought by the public entity against its own employee or former employee as an individual and not in his official capacity.

In either case, the City Council has the discretion to make a determination regarding the existence, or lack thereof, of these factors. If the City Council determines that these factors were present, then this exception to section 995 allows the City Council to refrain from providing a defense to a former employee.

The complaint and cross-complaint both allege that the Board Members committed actual fraud and violated statutory prohibitions against entering contracts for the SDCERS board in which they had personal interests and against incurring certain types of liabilities. They also allege facts which demonstrate a direct conflict of interest between the City of San Diego and the identified individuals. Accordingly, the City may refuse to provide a defense to Plaintiffs under the exception in section 995.2(a)(2) if it believes that they acted or failed to act because of actual fraud, corruption, or actual malice.

The City also may refuse to provide a defense under section 995.2(a)(3) if doing so would create a conflict of interest between the public entity and the former employee. Because the City is a plaintiff in the action and cross-complainant against City employees and former employees, an inherent conflict of interest exists.¹ As stated in *Stewart v. City of Pismo Beach*, 35 Cal. App. 4th 1600, 1606 (1995), “it is unreasonable to require a public entity to finance litigation directed against it.” When there is an actual conflict between a public entity and its employees “the public entity need not provide any defense whatsoever.” *City of Huntington Beach v. Petersen Law Firm*, 95 Cal. App. 4th 562, 567 (2002).

Similarly, section 995.4 permits a public agency to refuse to provide a defense in an action or proceeding brought by the public entity against its own former employee as an individual and not in his official capacity. “This obviously constitutes a conflict of interest of such magnitude that the entity should not be compelled to litigate, in effect, against itself.” California Government Tort Liability Practice § 4.25 (4th ed. 2004). Accordingly, the City has the discretion to refuse to provide a defense to plaintiffs under these circumstances.

II. Additional Considerations

This is just one of many demands for indemnity being brought by SDCERS Board Members, many of whom have been indicted in federal and state court for the very actions which have imposed massive liabilities upon the City, and which are the subject of the civil actions identified above and more. The cost to the City in attorney fees alone on the two matters noted above is likely to range in the hundreds of thousands of dollars, if not more. Not only that, there

¹ In *City of Redondo Beach v. Alice DeLong*, 123 Cal. App. 3d 1035 (1981), the court found that the City had no duty under California Government Code section 995.2 or 995.4 to provide DeLong, the City Treasurer, with an attorney or to pay her legal fees in the City’s action for a writ of mandamus to compel DeLong to perform her duties. *Id.* at 1043.

is still another lawsuit brought by SDCERS against the City to enforce the same 2002 indemnification resolution and have the City pay \$700,000 in attorney's fees related to the SEC investigation. There is no end in sight.

CONCLUSION

In general, the City must provide a defense to its employees and former employees for actions occurring within the scope of their employment. However, Government Code sections 995.2 and 995.4 both provide exceptions to the general rule. If the City Council determines that the Plaintiffs acted because of actual fraud or corruption, or that there is a conflict of interest between the City and the Plaintiffs, then the City is not required to provide a defense.

Respectfully submitted,

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MJA:JBC:amp
RC-2006-10

Attachments